MF Banking Law [1957]

STUDY OF BANKING LAWS
FINANCIAL INSTITUTIONS ACT OF 1957

U. S. Congress

HEARINGS

BEFORE A

SUBCOMMITTEE OF THE
COMMITTEE ON BANKING AND CURRENCY
UNITED STATES SENATE

EIGHTY-FIFTH CONGRESS

FIRST SESSION

ON

A PROPOSED BILL TO AMEND AND REVISE THE STATUTES GOVERNING FINANCIAL INSTITUTIONS AND CREDIT

JANUARY 28, 29, 30, 31, FEBRUARY 1, 4, 5, 7, 8, 11, 12, 14, 15, AND 18, 1957

PART 2

Printed for the use of the Committee on Banking and Currency

STUDY OF BANKING LAWS
FINANCIAL INSTITUTIONS ACT OF 1957

U.S. Congress. Senate.

HEARINGS

BEFORE A

SUBCOMMITTEE OF THE
COMMITTEE ON BANKING AND CURRENCY
UNITED STATES SENATE

EIGHTY-FIFTH CONGRESS

FIRST SESSION

ON

A PROPOSED BILL TO AMEND AND REVISE THE STATUTES GOVERNING FINANCIAL INSTITUTIONS AND CREDIT

JANUARY 28, 29, 30, 31, FEBRUARY 1, 4, 5, 7, 8, 11, 12, 14, 15, AND 18, 1957

PART 2

Printed for the use of the Committee on Banking and Currency

UNITED STATES
GOVERNMENT PRINTING OFFICE
84444 WASHINGTON : 1957

COMMITTEE ON BANKING AND CURRENCY

J. W. FULBRIGHT, Arkansas, *Chairman*

A. WILLIS ROBERTSON, Virginia	HOMER E. CAPEHART, Indiana
JOHN J. SPARKMAN, Alabama	JOHN W. BRICKER, Ohio
J. ALLEN FREAR, Jr., Delaware	IRVING M. IVES, New York
PAUL H. DOUGLAS, Illinois	WALLACE F. BENNETT, Utah
A. S. MIKE MONRONEY, Oklahoma	PRESCOTT S. BUSH, Connecticut
FRANK J. LAUSCHE, Ohio	J. GLENN BEALL, Maryland
JOSEPH S. CLARK, Pennsylvania	FREDERICK G. PAYNE, Maine

J. H. Yingling, *Chief Clerk*
Robert A. Wallace, *Staff Director*

Subcommittee on Banking

A. WILLIS ROBERTSON, Virginia, *Chairman*

JOHN J. SPARKMAN, Alabama	HOMER E. CAPEHART, Indiana
J. ALLEN FREAR, Jr., Delaware	JOHN W. BRICKER, Ohio
PAUL H. DOUGLAS, Illinois	IRVING M. IVES, New York
A. S. MIKE MONRONEY, Oklahoma	WALLACE F. BENNETT, Utah
JOSEPH S. CLARK, Pennsylvania	PRESCOTT S. BUSH, Connecticut

Donald L. Rogers, *Counsel*

CONTENTS

STUDY OF BANKING LAWS

(Financial Institutions Act of 1957)

MONDAY, JANUARY 28, 1957

UNITED STATES SENATE,
COMMITTEE ON BANKING AND CURRENCY,
SUBCOMMITTEE ON BANKING,
Washington, D. C.

The subcommittee met, pursuant to call, in room 301, Senate Office Building, at 10:05 a. m., Senator A. Willis Robertson (chairman of the subcommittee) presiding.

Present: Senators Robertson, Frear, Clark, Bricker, and Bennett.

Senator ROBERTSON. The subcommittee will be in order.

Today the Subcommittee on Banking of the Senate Banking and Currency Committee is beginning hearings on a committee print bill to codify the banking and credit laws. The bill is the result of the study of the Federal statutes governing financial institutions which I, under the designation of the chairman of the full commitee, have been conducting on behalf of the committee since last July. The bill is based on recommendations submitted by the Federal supervisory agencies, by the various trade organizations in the financial field, by our 27-man advisory committee, and by many individuals. We are richly indebted to all of those groups for their helpful cooperation.

I was pleased that the Economic Report of the President, which was released last Wednesday, endorses our study. The report at page 49 states in part:

> The exceptionally heavy demands which economic expansion is placing on credit and capital markets have directed attention increasingly to questions concerning the adequacy of our financial facilities, and of the laws and regulations which govern their operation. Alert to these problems, the Senate Committee on Banking and Currency during the past year made an extensive and constructive investigation of Federal laws affecting financial institutions.

The economic report went on to cite that there were broader problems not covered by the study which should be studied, and the President strongly recommended the appointment of another Monetary Commission to operate perhaps along the line of the Aldrich Commission, which was authorized in 1908 and submitted its report in the summer of 1912. On the basis of that report the Congress in 1913 passed the Federal Reserve Act.

Of course, that Commission would study one of the vital problems of every nation, which is a stable currency. Everybody knows that we have not had a stable currency for a long time. Probably it was about as stable as we have known it in recent years, in 1928.

In 1929 our exports and our imports were balanced and the prices received by the farmers with relation to the prices they paid for manufactured goods were about as favorable to the farmers as any they had had for a long time. Of course, it wasn't perfect, it never has been perfect, but it was going along pretty well.

Then we had too much speculation, or gambling, if you please, on the stock exchanges, and we had a financial bust of the equity values. Then followed a period of depression that had already started abroad.

Before this downward trend was over we were in the midst of probably the worst depression that the Nation has ever had. Debts were so pressing and the money with which to pay them so scarce that the President had to declare a bank holiday and a bank could not pay any money out at all. There were quick examinations to see what could be done and if the RFC could help the few banks that did not open up.

Then the President said, money is too dear. We will make money cheaper.

You remember what my predecessor, Senator Glass, said about devaluing the dollar and artificially increasing the value of its backing—gold—going off the gold standard. He said it was an act of high immorality. In any event, there was no question about the fact that in 1933 and in 1934 money was very dear. The dollar was not stable.

President Roosevelt said, "Our objective is to get a stable dollar." That was his objective. But then political expediency moved in on him in a big way and in January of the next year he asked the Congress: "Give me $4,800 million to spend as I see fit for relief and recovery," and Congress did what he asked.

That was the commencement of the big deficit financing, and the dollar has never been stable since.

We cannot go into that question, but that will be one question that this Monetary Commission will have to consider. One reason why I personally would like to see the President have the kind of Commission he asked for is that you will not get a stable dollar without treading on a good many toes. There are a lot of people who do not want a stable dollar. There are people who think they can make money with a tight dollar, and others who think they can make money with a cheap dollar. Then you have the byproduct of the competition of the few agencies that now handle the dollars. There are some tax advantages and some question as to whether you have to keep this reserve when somebody else does not have to have the same reserve with respect to loans.

All of those things are broad questions of policy that our study did not embrace, and I want to make that very clear. In case we get requests from witnesses to go into thes broader matters, we cannot undertake that. Our study is largely technical. We are dealing with laws that go back to 1862 and that have never been codified.

We have brought them all together, to show you that, and in the publication of the laws we are letting some bankers know for the first time the laws under which they operate.

The Senator from New Mexico got a violent protest from the president of a building and loan association there about the provision in this tentative bill for the election of directors of the Home Loan Bank Board. He said under that law they are proposing a small State will never be able to elect a director. Of course, I pointed out that that is the present law, and has been ever since the law was passed, and that the Banking Committee recommended its continuance and the advisory committee recommended its continuance. Of course, if he wants to change it, he will be heard.

I suppose there were others who found out for the first time, after we brought all these laws together, some of the things under which they have been operating and never heard of before.

The committee print was prepared under my direction by the committee counsel, Mr. Donald L. Rogers, with the help, as I say, of these Federal agencies and other splendid groups.

I want to indicate again, as I did at the hearings of last November, that I am not finally committed to every section of the bill. There are 2 or 3 matters I put in because other people thought they ought to be in the bill. For instance, it was not my idea that we would go into the change of structure of the Federal Deposit Insurance Corporation, but there are some who thought it ought to be changed. The advisory committee thought it ought to changed, and I thought enough of their views to put it in for the purposes of the hearing. Some thought that the criminal laws on the future employment of bank examiners by banks, and loans to them from banks, were not tight enough and we should safeguard against another small bank situation such as occurred in Chicago. But since the language was put in there have been many complaints coming to me from former bank examiners who are now outstanding bankers, that it is unnecessarily drastic.

We can consider all of the changes of that kind and they can be duly ironed out. However, I am hopeful these hearings in the next 3 weeks will develop suggestions to improve the bill.

Incidentally, when I say "3 weeks," I wish to emphasize the "3," because I am informed that a House Appropriations Committee plans to finish action on its first appropriation bill, which is an appropriation of over $3 billion for the Treasury and Post Office Departments, before they recess on February 12 for the Lincoln Day speeches. Naturally we want to give all of our Republican colleagues an opportunity to get back among their constituents and make Lincoln Day speeches, because we think a lot of Lincoln. If Lincoln's views had prevailed after the war of 1861–65 we would have been in better shape than we were for 10 or 15 years.

Senator BRICKER. I understand our side feels so secure that they have called off that week of speeches.

Senator ROBERTSON. I did not know, but I saw some statement to the effect that they were really going to get the Congress 2 years from now, and I thought maybe they would start in on the Lincoln Day holiday. But if they already feel secure, that is different.

The point I was making was that after the Lincoln Day holiday the House will pass this appropriation bill, and I am chairman of the subcommittee that handles it on the Senate side. So I will then have to hold hearings on that, and I would like very much to complete these hearings before that time.

Senator BRICKER. May I say at the very beginning that I am indeed very grateful to you for the fine leadership you have given in preparing this bill. I agree wholeheartedly that it is not political in the sense that it is partisan in any way. It involves all of the people of the country and all of their financial interests. I am very grateful for the work of the Advisory Committee, of Mr. Cravens and his committee. I am particularly happy to have an Ohio representative, Mr. Everett Reese, who is past president of our Ohio Association and of the National Bankers Association, with us at this hearing.

I realize, of course, as you do, that some of the provisions are controversial, but I think we will work out a constructive bill so that we will have a codification of all the banking laws, and so that we may have the working tools by which we can improve and stabilize the whole banking structure of the country.

Senator ROBERTSON. Thank you, Senator Bricker.

The chairman wants to say he appreciates so much the cooperation that he has already been assured he is going to received from both sides of the Congress and this subcommittee. Incidentally, this subcommittee was increased by four members because this was regarded as one of the most important measures we will handle at this session.

As Senator Bricker says, there will be no politics in this if we can help it. We are dealing with everybody's money, and everybody's business, and it makes no difference whether the man in that business is Democratic, or Republican, or Socialist, or what not. We will study it from the technical financial viewpoint, and not from a partisan viewpoint.

There has been prepared a section by section analysis of the committee print bill we are considering, which for the information of all concerned will, without objection, be inserted in the record at this point.

(The analysis referred to follows:)

BRIEF SECTION BY SECTION ANALYSIS OF COMMITTEE PRINT BILL ENTITLED "FINANCIAL INSTITUTIONS ACT OF 1957"

TITLE I—NATIONAL BANK ACT

CHAPTER 1. SHORT TITLE AND DEFINITIONS

Section 1. Short title.—Same short title as contained in 12 U. S. C. 38.

Section 2. Definitions.—New section defining terms used in this act.

CHAPTER 2. COMPTROLLER OF THE CURRENCY

Section 3. Office of Comptroller of the Currency.—Revision of 12 U. S. C. 1 by substituting the word "office" for the obsolete word "bureau," by eliminating the obsolete reference to national currency and by clearly stating the Comptroller's responsibility for supervising national banks.

Section 4. Appointment of Comptroller.—Subsection (a) revises 12 U. S. C. 2 by eliminating obsolete reference to $15,000 annual salary for Comptroller as requested in recommendation 1.

Subsection (b) revises 12 U. S. C. 3 by providing for "a surety bond" and eliminating reference to "two responsible sureties."

Section 5. Deputy Comptrollers.—Revises 12 U. S. C. 4, 5, and 6 by authorizing the appointment of two additional Deputy Comptrollers as requested in recommendation 2 and by eliminating obsolete language.

Section 6. Chief National Bank Examiner.—Same as 12 U. S. C. 7, except specificaly authorizes title of "Chief National Bank Examiner."

Section 7. Employees and salaries.—Revises 12 U. S. C. 8, 9, 9a, and 10 by eliminating reference to classification of clerks by the Secretary of the Treasury as requested in recommendation 3, and by eliminating duplicating and obsolete provisions.

Section 8. Conflicts of interest prohibited.—Subsection (a) revises and strengthens 12 U. S. C. 11 regarding conflicts of interest on the part of the Comptroller and Deputy Comptrollers.

Subsection (b) is a new provision governing conflict of interests of employees of the Comptroller.

Section 9. Seal.—Same as 12 U. S. C. 12.
Section 10.—Office facilities.—Same as 12 U. S. C. 13.
Section 11. Annual report.—Same as 12 U. S. C. 14.

CHAPTER 3. ORGANIZATION OF NATIONAL BANKS

Section 12. Articles of association.—Same as 12 U. S. C. 21.

Section 13. Organization certificate.—Subsection (a) is the same as 12 U. S. C. 22.

Subsection (b) is the same as 12 U. S. C. 23.

Section 14. Commencement of business.—Subsection (a) is the same as 12 U. S. C. 26, except that in the first sentence "one hundred per centum" is substituted for "fifty per centum" as provided for in recommendation 12.

Subsection (b) is the same as 12 U. S. C. 27.

Subsection (c) is the same as 12 U. S. C. 28.

CHAPTER 4. CAPITAL, STOCK AND SHAREHOLDERS

Section 15. Capital.—Subsection (a) is the same as the first two sentences of 12 U. S. C. 51.

Subsection (b) is a revision of 12 U. S. C. 53 based on recommendation 12.

Subsection (c) is the same as the last two sentences of 12 U. S. C. 51.

Section 16. Capital stock.—Same as 12 U. S. C. 52.

Section 17. Payment by bank of deficiency in capital stock.—Same as 12 U. S. C. 55, except obsolete provisions eliminated.

Section 18. Increase in capital stock.—Same as 12 U. S. C. 57, except for provisions relating to stock purchases under section 31 (a) (9) of this act.

Section 19. Decrease in capital stock.—Same as 12 U. S. C. 59, except reference to circulation deleted.

Section 20. Preferred stock.—Revision of 12 U. S. C. 51a, 51b, 51b–1, and 51c to authorize issuance of preferred stock generally and not solely on an emergency basis. Based on recommendation 45D by the advisory committee.

Section 21. Capital notes and debentures.—New provision based on recommendation 45D.

Section 22. Dividends.—Subsections (a), (b), and (c) are a revision of 12 U. S. C 60 as provided in recommendation 13, including the 2-year amendment in subsection (b) recommended by the advisory committee.

Subsection (d) is a revision of 12 U. S. C. 56 as requested in recommendation 13.

Section 23. Shareholders' list.—Revision of 12 U. S. C. 62, including proposal of recommendation 17 (1) to delete reference to creditors plus new provision in last sentence of subsection (b) relating to the reporting of stock transactions.

Section 24. Shareholders' liability.—Subsection (a) is the same as 12 U. S. C. 66.

Subsection (b) is the same as 12 U. S. C. 67.

CHAPTER 5. DIRECTORS OF NATIONAL BANKS

Section 25. Number of directors.—Revision of 12 U. S. C. 71a by eliminating reference to members of the Federal Reserve System. Provision for member banks will be found in section 23 (h) of title II of this bill.

Section 26. Election of directors.—Subsection (a) revises 12 U. S. C. 71 by eliminating a duplicating provision on the number of directors and the last sentence thereof.

Subsection (b) is a revision of 12 U. S. C. 75 as provided in recommendation 20.

Subsection (c) is the same as the first two paragraphs of 12 U. S. C. 61, except the provision on cumulative voting is amended as provided in recommendation 15.

Subsection (d) is the same as the last sentence of 12 U. S. C. 71 plus 12 U. S. C. 74.

Subsection (e) is the same as 12 U. S. C. 72.

Section 27. Qualifications of directors.—Same as 12 U. S. C. 72.

Section 28. Oath of directors.—Same as 12 U. S. C. 73.

Section 29. Removal of officers and directors.—Revises 12 U. S. C. 77 by (1) eliminating reference to member banks (see sec. 29 of title II of this bill); (2) by substituting the words "has violated or is violating" for the words "have continued to violate"; (3) by substituting the words "has engaged in or is engaging in unsafe or unsound practices" for the words "have continued unsafe or unsound practices"; and (4) by providing that the hearing must be held pursuant to the Administrative Procedures Act and shall be subject to review.

Section 30. Liability of directors.—Same as 12 U. S. C. 93.

CHAPTER 6. POWER AND DUTIES OF NATIONAL BANKS

Section 31. Corporate powers.—Subsections (a) (1) to (6) are the same as the comparable provisions of 12 U. S. C. 24.

Subsection (a) (7) is the same as the first sentence of paragraph 7 of 12 U. S. C. 24, except the reference to circulating notes is deleted. (See sec. 32 of this title.)

Subsection (a) (8) revises paragraph 8 of 12 U. S. C. 24 as provided in recommendation 6.

Subsection (a) (9) is a new provision authorizing stock options based on advisory committee recommendations 45E.

Subsection (b) is the same as 12 U. S. C. 81.

Section 32. Dealing in securities.—Subsection (a) is the same as the provisions following the first sentence of paragraph 7 of 12 U. S. C. 24. except that the reference to obligations of the Home Owners' Loan Corporation is deleted as provided in recommendation 4.

Subsection (b) is a new provision based on recommendation 60.

Section 33. Trust powers.—Same as section 11 (k) of the Federal Reserve Act as amended in recommendation 34.

Section 34. Maximum loan limitation.—Subsections (a) and (b) (1), (2), (3), (4), and (5) are the same as the comparable provisions of 12 U. S. C. 84.

Subsection (b) (6) amends subparagraph (6) of 12 U. S. C. 84 as proposed in recommendation 23 (1).

Subsection (b) (7) amends subparagraph (7) of 12 U. S. C. 84 as proposed in recommendation 24.

Subsection (b) (8) amends subparagraph (8) of 12 U. S. C. 84 as proposed in recommendation 25.

Subsection (b) (9), (10), and (11) are the same as the comparable provisions of 12 U. S. C. 84.

Subsection (b) (12) is a new provision as provided in recommendation 23 (2) as amended by the advisory committee.

Section 35. Maximum rate of interest.—Subsection (a) is the same as 12 U. S. C. 85, except for new provision in last sentence.

Subsection (b) is the same as 12 U. S. C. 86.

Section 36. Real-estate loans.—Subsection (a) is the same as first paragraph of 12 U. S. C. 371, except (1) the words "under any provision of the National Housing Act" are substituted for the words "under the provisions of title II, title VI, title VIII, section 8 of title I or title IX of the National Housing Act"; (2) the aggregate limit on real-estate loans is increased by providing an alternative of 20 percent of demand deposits as proposed by the advisory committee in recommendation 35; and (3) recommendation 35 (2) is added.

Subsection (b) is the same as the second paragraph of 12 U. S. C. 371.

Subsection (c) amends the third paragraph of 12 U. S. C. 371 as proposed in recommendation 35 (1) as amended by the advisory committee.

Subsection (d) revises the fourth paragraph of 12 U. S. C. 371 by deleting obsolete reference to section 13 (b) of the Federal Reserve Act and to the Reconstruction Finance Corporation.

Subsection (e) adds a new provision as proposed in recommendation 35 (4) and modified by the advisory committee.

Subsection (f) adds a new provision as proposed in recommendation 35 (3).

Section 37. Limit on bank's indebtedness.—Amends 12 U. S. C. 82 by (1) striking paragraphs 1, 6, and 10 as proposed in recommendation 22 as amended by the advisory committee; (2) by increasing the total amount of permitted indebtedness as proposed in recommendation 45B by advisory committee; and (3) by adding a new exception at the end thereof as proposed by the advisory committee in recommendation 45B.

Section 38. Holding of real estate.—Same as 12 U. S. C. 28.

Section 39. Branches.—Same as 12 U. S. C. 36, except subsection (b) is amended as proposed in recommendation 9, and subsection (f) is amended as proposed in recommendation 11.

Section 40. Change of name or location.—Subsection (a) revises 12 U. S. C. 30 as proposed in recommendation 7.

Subsection (b) is the same as 12 U. S. C. 31.

Section 41. Dealing with own stock.—Same as 12 U. S. C. 83.

Section 42. Depositories and financial agents.—Same as 12 U. S. C. 90, except reference to national currency deleted.

Section 43. Investment in bank premises.—Revision of 12 U. S. C. 371d by increasing total permissible amount to 50 percentum of capital and surplus as proposed in recommendation 45C of the advisory committee, and by deleting reference to member banks. (See sec. 23 (j) of title II of this bill.)

Section 44. Restrictions on engaging in banking business.—Same as 12 U. S. C. 378, except amended in subsection (a) (2) as proposed in recommendation 36.

Section 45. Acting as insurance agent or broker.—Subsections (a) and (b) are new provisions as proposed in recommendation 45F by the advisory committee.

Subsection (c) is the same as 12 U. S. C. 92, except for new sentence at end thereof.

Section 46. Acts in contemplation of insolvency.—Same as 12 U. S. C. 91.

Section 47. General provision for amending articles.—New provision.

CHAPTER 7. NATIONAL BANK EXAMINATIONS AND REPORTS

Section 48. Examination of banks.—Subsection (a) is the same as first paragraph of 12 U. S. C. 481, except reference to definition of affiliates in Federal Reserve Act.

Subsection (b) is same as the second paragraph of 12 U. S. C. 481, except the duplicating provisions of the fourth sentence are deleted and fourth sentence is made subsection (c) of section 49.

Section 49. Expenses of examinations.—Same as 12 U. S. C. 482, except obsolete first sentence deleted and fourth sentence of second paragraph of 12 U. S. C. 481 set forth in subsection (c).

Section 50. Confidentiality of examination reports.—New provision based in part on recommendation 44.

Section 51. State examination or license prohibited.—New provision as proposed in recommendation 5.

Section 52. Reports by national banks.—Subsection (a) revises the first paragraph of 12 U. S. C. 161 based partly on recommendations 28, 29, and 58.

Subsection (b) is the same as the second paragraph of 12 U. S. C. 161.

Subsection (c) revises 12 U. S. C. 164 by eliminating obsolete reference to circulating notes.

CHAPTER 8. CONSOLIDATIONS, MERGERS AND CONVERSIONS

Section 53. Consolidation of national banks.—Revision of 12 U. S. C. 33 as proposed in recommendation 8.

Section 54. Consolidation of State bank into national bank.—Revision of 12 U. S. C. 34a as proposed in recommendation 8.

Section 55. Merger into national bank.—Revision of 12 U. S. C. 34 (b) as proposed in recommendation 8.

Section 56. Conversion of State banks.—Same as 12 U. S. C. 35.

Section 57. Conversion, merger, or consolidation of national banks into State banks.—Same as 12 U. S. C. 214a, 214b, and 214c.

CHAPTER 9. VOLUNTARY DISSOLUTION, RECEIVERS, AND CONSERVATORS

Section 58. Voluntary dissolution.—Subsection (a) revises 12 U. S. C. 181 as proposed in recommendation 30.

Subsection (b) is the same as the second paragraph of 12 U. S. C. 181.

Subsection (c) is the same as 12 U. S. C. 182.

Section 59. Appointment of receiver.—Subsection (a) is the same as 12 U. S. C. 191, except reference to personal liability of shareholders is deleted as proposed in recommendation 31.

Subsection (b) is the same as 12 U. S. C. 192, except (1) the reference to personal liability is deleted as proposed in recommendation 31 and the reference to section 12B of the Federal Reserve Act is changed to the Federal Deposit Insurance Act.

Subsection (c) is the same as 12 U. S. C. 193.

Section 60. Distribution of assets.—Revision of 12 U. S. C. 194 and 196 eliminating obsolete reference to national bank notes.

Section 61. Winding up business of bank.—Revision of 12 U. S. C. 197 as proposed in recommendation 32.

Section 62. Resumption of business.—Same as 12 U. S. C. 197a.

Section 63. Purchase of bank property.—Subsection (a) is the same as 12 U. S. C. 198.

Subsection (b) is the same as 12 U. S. C. 199.

Subsection (c) is the same as 12 U. S. C. 200.

Section 64. Conservators.—Subsections (a), (b), and (c) are the same as 12 U. S. C. 203, 204, and 205.

Subsection (d) is the same as 12 U. S. C. 206, except reference to withdrawal by depositors is eliminated.

Subsections (e), (f), (g), (h), and (i) are the same as 12 U. S. C. 207, 208, 209, 210, and 211.

Subsection (j) is a new provision as proposed in recommendation 33.

CHAPTER 10. MISCELLANEOUS

Section 65. Emergency powers of the President.—Same as 12 U. S. C. 95 and 95a, except obsolete reference to Philippine Islands is deleted.

Section 66. Ratification of certain acts.—Same as 12 U. S. C. 95b and 213.

Section 67. Taxation of national bank shares.—Same as 12 U. S. C. 548.

Section 68. Lawful reserves in Territories and possessions.—Subsection (a) is the same as 12 U. S. C. 143.

Subsection (b) revises 12 U. S. C. 144 as proposed in recommendation 27.

Section 69. Venue of actions.—Same as 12 U. S. C. 94.

Section 70. Territorial applicability of act.—Revision of 12 U. S. C. 40 and 41.

TITLE II—FEDERAL RESERVE ACT

CHAPTER 1. SHORT TITLE AND DEFINITIONS

Section 1. Short title.—Same as section 1 of the Federal Reserve Act.

Section 2. Definitions.—Same as section 1 of Federal Reserve Act.

CHAPTER 2. ORGANIZATION OF FEDERAL RESERVE BANKS

Section 3. Federal Reserve districts.—Revision of first two paragraphs of section 2 of Federal Reserve Act as proposed in recommendation 46, plus requirement of only one Federal Reserve city in each district.

Section 4. Branch offices.—Same as section 3 of Federal Reserve Act, except subsection (c) added as proposed in recommendation 64.

Section 5. Corporate powers of Federal Reserve banks.—Same as paragraph 4 of section 4 of Federal Reserve Act, except introductory portions amended as proposed in recommendation 50.

Section 6. Capital stock of Federal Reserve banks.—Same as section 5 of Federal Reserve Act.

Section 7. Division of earnings.—Section 7 of Federal Reserve Act amended by adding subsection (b) as proposed in recommendation 54.

Section 8. Federal Advisory Council.—Section 12 of Federal Reserve Act amended as proposed in recommendation 52.

CHAPTER 3. POWERS OF FEDERAL RESERVE BANKS

Section 9. Receipt of deposits and collections.—Same as paragraph 1 of section 13 and paragraph 14 of section 16 of Federal Reserve Act.

Section 10. Discount operations.—Same as paragraphs 2, 3, 4, and 5 of section 13 of Federal Reserve Act.

Section 11. Discount of agricultural paper.—Same as section 13a of Federal Reserve Act.

Section 12. Acceptances.—Same as paragraphs 6, 7, and 12 of section 13 of Federal Reserve Act.

Section 13. Advances.—Same as paragraphs 8 and 13 of section 13, except includes recommendation 70 and section 10b of Federal Reserve Act.

Section 14. Open market operations.—Same as section 14 of Federal Reserve Act.

Section 15. Government deposits.—Same as section 15 of Federal Reserve Act, except (1) eliminates obsolete reference to the Philippine Islands as proposed in recommendation 85E of the advisory committee; and (2) eliminates obsolete reference to National Agricultural Credit Corporation as proposed in recommendation 71.

CHAPTER 4. DIRECTORS OF FEDERAL RESERVE BANKS

Section 16. Duties of directors.—Same as paragraphs 6, 7, and 8 of section 4 of Federal Reserve Act.

Section 17. Classes of directors.—Subsection (a) is a revision of paragraph 9 of section 4 as proposed in recommendations 50 (c), 51, and 52, with an amendment on the residence requirement.

Subsection (b) is the same as paragraphs 10, 11, and 12 of section 4 of the Federal Reserve Act, except for the deletion proposed in recommendation 50 (d).

Subsection (c) is the same as paragraph 13 of section 4 of the Federal Reserve Act.

Section 18. Selection of class A and B directors.—Same as paragraphs 15, 16, 17, 18, and 19 of section 4 of the Federal Reserve Act.

Section 19. Federal Reserve agent.—Revision of paragraphs 20 and 21 of section 4 as proposed in recommendations 50 (e), 53, and recommendation 85D of the advisory committee.

Section 20. Compensation of directors, officers, and employees.—Same as paragraph 22 of section 4 of Federal Reserve Act.

CHAPTER 5. MEMBERSHIP IN THE FEDERAL RESERVE SYSTEM

Section 21. National banks as members.—Revision of paragraphs 6 and 7 of Federal Reserve Act as proposed in recommendation 47.

Section 22. Admission of State banks as members.—Same as paragraphs 1, 2, 3, and 16 of section 9 of Federal Reserve Act, except recommendation 57 is incorporated therein.

Section 23. Powers and duties of State member banks.—Subsection (a) is the same as the first sentence and part of the second sentence of paragraph of section 9 of Federal Reserve Act.

Subsection (b) is a revision of the remainder of paragraph 6 of section 9, including in part recommendation 58.

Subsection (c) is the same as paragraph 13 of section 9.

Subsection (d) revises paragraph 20 of section 9 as proposed in recommendation 60.

Subsections (e), (f), and (g) are the same as paragraphs 11, 4, and 5 of section 9 of Federal Reserve Act.

Subsection (h) revises 12 U. S. C. 71a.

Subsection (i) is a new provision.

Subsection (j) is a revision of section 24A and includes recommendation 45C by the advisory committee.

Subsections (k), (l), (m), (n), and (o) are the same as paragraphs 21, 15, 10, 14, and 9 of section 9 of the Federal Reserve Act.

Section 24. Examination of member banks.—Same as paragraph 7 of section 9 and paragraphs 5 and 6 of section 21 of Federal Reserve Act.

Section 25. Insolvency of member banks.—Same as section 6 of Federal Reserve Act.

Section 26. Member banks making security loans.—Same as paragraph 7 of section 19 of Federal Reserve Act.

Section 27. Member banks dealing with nonmembers.—Same as paragraph 8 of section 19 of Federal Reserve Act.

Section 28. Restrictions on officers and directors of member banks.—Subsections (a), (b), (c), and (d) are the same as subsections (d), (e), and (f) of section 22 of the Federal Reserve Act.

Subsection (e) revises subsection (g) of section 22 of Federal Reserve Act as proposed in recommendation 81 of the advisory committee.

Subsection (f) and (g) are the same as 12 U. S. C. 501 and 12 U. S. C. 78.

Section 29. Removal of directors.—Revision of 12 U. S. C. 77, including recommendation 84 and including other amendments similar to those described above under section 29 of title I.

Section 30. Liability of Federal Reserve bank shareholders.—Revision of paragraph 4 of section 2 of Federal Reserve Act as proposed in recommendation 48.

CHAPTER 6. AFFILIATES OF MEMBER BANKS

Section 31. Definitions.—Same as 12 U. S. C. 221a, except subsection (a) thereof is deleted.

Section 32. Dealing with affiliates.—Same as section 23A of the Federal Reserve Act.

Section 33. Voting permits of holding company affiliates.—Same as all after the first two paragraphs of 12 U. S. C. 61, except subparagraph (3) is amended as proposed in recommendation 16, including the advisory committee's additional recommendation.

Section 34. Agreement of State member affiliates.—Same as paragraph 22 of section 9 of Federal Reserve Act.

Section 35. Securities affiliates.—Same as 12 U. S. C. 377.

Section 36. Reports of State member affiliates.—Same as paragraphs 17, 18, and 19 of section 9 of Federal Reserve Act.

Section 37. Examination of State member affiliates.—Same as paragraph 23 of section 9 of the Federal Reserve Act and paragraph 9 of section 21 of the Federal Reserve Act.

CHAPTER 7. ORGANIZATION AND POWER OF BOARD OF GOVERNORS

Section 38. Organization.—Subsections (a) and (b) revise paragraphs 1 and 2 of section 10 of Federal Reserve Act in recommendation 61.

Subsections (c), (d), (e), (f), and (g) are the same as paragraphs 3, 4, 5, 7, and 10 of section 10 of Federal Reserve Act, except amendments proposed in recommendations 62 and 68 are included in subsections (d) and (e).

Subsection (h) is a new provision as proposed in recommendation 85A of the advisory committee.

Subsection (i) is a new provision regarding conflicts of interest.

Section 39. General powers of board.—Subsection (a) is the same as subsection (a) of section 11 of Federal Reserve Act.

Subsection (b) is the same as subsection (b) of section 11, except for change in voting requirement as proposed by advisory committee in recommendation 66.

Subsections (c), (d), (e), (f), (g), (h), (i), (j), and (k) are the same as subsections (c), (d), (e), (f), (g), (h), (i), (j), and (l) of section 11 of Federal Reserve Act.

Subsection (l) is the same as subsection (m) of section except for change in voting requirement as proposed by advisory committee in recommendation 66.

Subsection (m) revises paragraph 7 of section 21 as proposed by the advisory committee in recommendation 85B.

Subsections (n) and (o) are the same as paragraph 15 of section 16 and paragraph 10 of section 13 of Federal Reserve Act.

Section 40. Open market committee.—Same as section 12A of the Federal Reserve Act.

Section 41. Payment of interest.—Same as paragraphs 1, 12, and 13 of section 19 of Federal Reserve Act, except for deletion made pursuant to recommendation 78.

Section 42. Bank reserves.—Same as paragraphs 2, 3, 4, 5, 6, 9, 10, and 11 of section 19 of Federal Reserve Act, except for change in voting requirement as proposed by recommendation 66 of advisory committee.

Subsection (f) revises paragraph 14 of section 19 as proposed in recommendation 79.

Section 43. Federal Reserve notes.—Revision of first 13 paragraphs of section 16 as proposed in recommendation 74, plus 12 U. S. C. 121a and 122a except for obsolete provisions.

CHAPTER 8. FOREIGN BRANCHES AND FOREIGN BANKING CORPORATIONS

Section 44. Foreign branches.—Same as section 25 of Federal Reserve Act, except for deletion in subsection (a) as proposed in recommendation 82, and new authority in subsection (f) as proposed in recommendation 83.

Section 45. Organization of foreign banking corporations.—Same as paragraphs 1, 2, 3, 4, and 23 of section 25 (a) of Federal Reserve Act, except obsolete reference to Philippine Islands is deleted in subsection (a).

Section 46. Capital stock and shareholders.—Same as paragraphs 12, 13, 14, 15, 19, and 20 of secion 25 (a) of Federal Reserve Act.

Section 47. Powers of foreign banking corporations.—Same as paragraphs 5, 6, 7, 8, 9, 10, 11, and 22 of section 25 (a) of Federal Reserve Act.

Section 48. Taxation.—Same as paragraph 21 of section 25 (a) of Federal Reserve Act.

Section 49. Voluntary liquidation and insolvency.—Same as paragraphs 17 and 18 of section 25 (a) of Federal Reserve Act.

Section 50. Penalties.—Same as paragraphs 16, 24, and 25 of section 25 (a) of Federal Reserve Act.

Section 51. Receipt of foreign property.—Same as paragraphs 3, 4, 5, and 6 of section 25 (b) of Federal Reserve Act including recommendation 59.

Section 52. Venue of actions for foreign transactions.—Same as paragraph 1 of section 25 (b) of Federal Reserve Act.

CHAPTER 9. REGULATION OF BANK HOLDING COMPANIES

Section 53. Definitions.—Same as 12 U. S. C. 1841.

Section 54. Acquisition of bank shares or assets.—Same as 12 U. S. C. 1842.

Section 55. Interest in nonbanking organizations.—Same as 12 U. S. C. 1843.

Section 56. Administration.—Same as 12 U. S. C. 1844.

Section 57. Borrowing by bank holding company or its subsidiaries.—Same as 12 U. S. C. 1845.

Section 58. Reservation of rights to States.—Same as 12 U. S. C. 1846.

Section 59. Penalties.—Same as 12 U. S. C. 1847.

Section 60. Judicial review.—Same as 12 U. S. C. 1848.

Section 61. Savings clause.—Same as section 11 of the Bank Holding Company Act of 1956.

CHAPTER 10. MISCELLANEOUS

Section 62. Settlement fund.—Revision of paragraph 16 of section 16 of Federal Reserve Act as proposed in recommendation 73, plus present provisions of paragraphs 17 and 18 of section 16.

Section 63. Reservation of powers.—Revision of paragraph 6 of section 10 of Federal Reserve Act as proposed in recommendation 63.

Section 64. Delivery of gold to Treasurer.—Same as subsection (n) of section 11 of Federal Reserve Act.

Section 65. Venue of actions generally.—Same as second paragraph of section 25 (b) of Federal Reserve Act.

TITLE III—FEDERAL DEPOSIT INSURANCE ACT

CHAPTER 1. SHORT TITLE AND DEFINITIONS

Section 1. Short title.—Same as section 1 of Federal Deposit Insurance Act.

Section 2. Definitions.—Subsections (a), (b), (c), (d), (e), (f), (g), and (h) are the same as subsections (a), (b), (c), (d), (e), (h), (i), (j) of section 3 of Federal Deposit Insurance Act.

Subsection (i) revises subsection (k) of section 3 of Federal Deposit Insurance Act pursuant to recommendation 115H of advisory committee.

Subsection (j) is a revision of subsection (l) of section 3 of Federal Deposit Insurance Act as proposed in recommendations 89 and 90.

Subsection (k) is a revision of subsection (m) of section 3 of Federal Deposit Insurance Act as proposed in recommendation 91.

Subsection (l) is a revision of subsection (n) of section 3 of Federal Deposit Insurance Act as proposed in recommendation 92.

Subsection (m) is a revision of subsection (o) of section 3 of Federal Deposit Insurance Act as proposed in recommendations 93 and 115C.

Subsection (n) is the same as subsection (p) of section 3 of Federal Deposit Insurance Act.

CHAPTER 2. CREATION OF CORPORATION AND POWERS

Section 3. Creation of corporation.—Same as section 1 of Federal Deposit Insurance Act.

Section 4. Insurance fund.—Revision of subsection (a) of section 11 of Federal Deposit Insurance Act as proposed in recommendation 105.

Section 5. Corporate powers.—Same as section 9 of Federal Deposit Insurance Act, except incorporates amendments proposed in recommendations 100 and 101.

CHAPTER 3. POWERS AND DUTIES OF ADMINISTRATOR

Section 6. Management of corporation.—New provision based on recommendation 115H of advisory committee.

Section 7. Advisory board.—New provision based on recommendation 115H of advisory committee.

Section 8. Administration.—Subsection (a) and (b) are the same assubsections (a) and (f) of section 10 of Federal Deposit Insurance Act, except the word "Administrator" is substituted for "Board of Directors," which is done throughout the act.

Subsection (c) amends subsection (g) of section 10 of Federal Deposit Insurance Act as proposed in recommendation 104, plus amendment of advisory committee.

Section 9. Examinations and reports.—Same as subsections (b) and (e) of section 10 of Federal Deposit Insurance Act.

Section 10. Confidentiality of records.—New provision incorporating recommendation 115E, plus additional amendments.

Section 11. Hearings.—Same as subsection (c) and (d) of section 10 of Federal Deposit Insurance Act, except includes recommendation 103.

CHAPTER 4. ADMISSION TO INSURANCE

Section 12. Continuance of insured status.—Same as subsection (a) of section 4 of Federal Deposit Insurance Act.

Section 13. Member banks.—Same as subsection (b) of section 4 of Federal Deposit Insurance Act.

Section 14. Nonmember banks.—Same as section 5 of Federal Deposit Insurance Act.

Section 15. Factors to be considered.—Same as section 6 of Federal Deposit Insurance Act.

CHAPTER 5. ASSESSMENT

Section 16. Assessment rates.—Same as subsection (a) of section 7 of Federal Deposit Insurance Act, except for inclusion of recommendation 96.

Section 17. Certified statement.—Same as subsections (b) and (c) of section 7 of Federal Deposit Insurance Act.

Section 18. Assessment credits.—Same as subsection (d) of section, except includes recommendation 97 in part.

Section 19. Refund of assessments.—Same as subsection (e) of section 7 of Federal Deposit Insurance Act.

Section 20. Penalties.—Same as subsections (g), (f), and (h) of section 7 of Federal Deposit Insurance Act, plus recommendation 98.

CHAPTER 6. SUPERVISION OF INSURED BANKS

Section 21. Display of official sign.—Same as subsection (a) of section 18 of Federal Deposit Insurance Act.

Section 22. Dividends.—Same as subsection (b) of section 18 of Federal Deposit Insurance Act.

Section 23. Mergers and consolidations.—Revision of subsection (c) of section 18 of Federal Deposit Insurance Act as proposed in recommendations 42, 85, and 114.

Section 24. Branches.—Same as subsection (d) of section 18 of Federal Deposit Insurance Act.

Section 25. Idemnity insurance.—Same as subsection (e) of section 18 of Federal Deposit Insurance Act.

Section 26. Payment of interest.—Revision of subsection (g) of section 18 of Federal Deposit Insurance Act based on recommendation 115F of advisory committee.

Section 27. Shareholders' list.—New provision.

Section 28. Trust funds.—Revision of subsection (i) of section 7 of Federal Deposit Insurance Act as proposed in recommendation 89.

Section 29. Termination of insured status.—Revision of susbection (a) of section 8 of Federal Deposit Insurance Act as proposed in recommendation 99, plus additional amendments.

Subsections (b), (c), and (d) are the same as subsections (b), (c), and (d) of section 8 of Federal Deposit Insurance Act.

CHAPTER 7. INABILITY OF BANKS TO PAY DEPOSITORS

Section 30. Payment to depositors by corporation.—Subsections (a) and (b) are revisions of subsections (b) and (f) of section 11 of Federal Deposit Insurance Act as proposed in recommendations 106 and 92.

Subsections (c) and (d) are new provisions based on recommendation 106.

Subsection (e) is the same as subsection (g) of section 11 of Federal Deposit Insurance Act.

Subsections (f), (g), (h), and (i) are the same as subsections (b), (c), (d), and (e) of section 12 of Federal Deposit Insurance Act, plus recommendation 110.

Section 31. Corporation as receiver of insured banks.—Subsections (a), (b), and (d) are the same as subsections (c), (d), and (e) of section 11 of Federal Deposit Insurance Act plus recommendation 107.

Subsection (c) is the same as subsection (a) of section 12 of Federal Deposit Insurance Act.

Subsection (e) is a new provision as proposed in recommendation 109.

Section 32. Organization of a new national bank.—Same as subsections (h) to (l), inclusive, of section 11 of Federal Deposit Insurance Act plus recommendation 108.

Section 33. Loans and purchases of assets.—Same as subsections (c), (d), and (e) plus recommendation 111.

CHAPTER 8. CORPORATE FUNDS AND OBLIGATIONS

Section 34. Borrowing authority.—Same as section 14 of Federal Deposit Insurance Act.

Section 35. Investment of funds.—Same as subsections (a) and (b) of section 13 of Federal Deposit Insurance Act.

Section 36. Obligations of corporation.—Same as sections 15 and 16 of Federal Deposit Insurance Act.

CHAPTER 9. MISCELLANEOUS

Section 37. Annual report.—Same as subsection (a) of section 17 of Federal Deposit Insurance Act.

Section 38. Annual audit.—Revision of subsections (b), (c), and (d) of section 17 as proposed in recommendation 113.

Section 39. Civil-service benefits.—New provision as proposed in recommendation 112.

Section 40. Penalties.—Subsection (a) is the same as subsection (f) of section 18.

Subsection (b) is the same as subsection (h) of section 18.

Subsection (c) is the same as section 19 of Federal Deposit Insurance Act.

Subsection (d) is a new provision based on recommendation 115B.

Section 41. Nondiscriminatory provisions.—Same as section 20 of Federal Deposit Insurance Act.

Section 42. Abolition of board of directors.—New provision based on recommendation 115H.

Section 43. Effective date.—New provision.

TITLE IV—FEDERAL HOME LOAN BANK ACT

Section 1. Short title.—Same as section 1 of the Federal Home Loan Bank Act.

Section 2. Definitions.—Revision of section 2 of Federal Home Loan Bank Act as proposed in recommendation 117.

Section 3. Federal home loan bank districts.—Revision of section 3 of Federal Home Loan Bank Act as proposed in recommendation 118.

Section 4. Eligibility of members.—Subsection (a) amends subsection (a) of section 4 of Federal Home Loan Bank Act as proposed in recommendation 119.

Subsection (b) amends subsection (b) of section 4 of Federal Home Loan Bank Act as proposed in recommendation 120.

Subsection (c) same as subsection (c) of section 4 of Federal Home Loan Bank Act.

Subsection (d) is a new provision.

Section 5. Limitation on interest rate.—Same as section 5 of Federal Home Loan Bank Act.

Section 5A. Liquidity requirement.—Same as section 5A of Federal Home Loan Bank Act.

Section 6. Capital of Federal home loan banks.—Revision of section 6 of Federal Home Loank Bank Act as proposed in recommendation 122.

Section 7. Management of banks.—Subsections (a) through (h) of section 7 of Federal Home Loan Bank Act are revised as proposed in recommendation 123.

Subsections (i) and (j) are same as present law.

Section 8. Examination and studies by board.—Same as section 8 of Federal Home Loan Bank Act.

Section 8A. Federal savings and loan advisory council.—Section 8A of Federal Home Loan Bank Act revised as proposed in recommendation 124.

Section 9. Eligibility to secure advances.—Same as section 9 of Federal Home Loan Bank Act.

Section 10. Advances to members.—Revision of section 10 of Federal Home Loan Bank Act as proposed in recommendation 125.

Section 10A. Advances to nonmembers.—Same as section 10b of Federal Home Loan Bank Act (see recommendation 126 for elimination of section 10a of Federal Home Loan Bank Act).

Section 11. General powers and duties of banks.—Subsections (a), (b), and (c) of section 11 of Federal Home Loan Bank Act amended as proposed in recommendation 127.

Subsections (d) and (e) are the same as present law.

Subsection (f) is amended as proposed in recommendation 128.

Subsection (g) is amended as proposed in recommendation 129.

Subsections (h), (i), and (j) are the same as present law.

Section 12. Incorporation of banks and corporate powers.—Amends section 12 of Federal Home Loan Bank Act in recommendations 130 and 131.

Section 13. Exemption from taxation.—Amends section 13 of Federal Home Loan Bank Act as proposed in recommendation 132.

Section 14. Depositories and financial agents.—Same as section 14 of Federal Home Loan Bank Act.

Section 15. Obligations of banks.—Amends section 15 of Federal Home Loan Bank Act as proposed in recommendation 133.

Section 16. Reserves and dividends.—Amends section 16 of Federal Home Loan Bank Act as proposed in recommendation 134.

Section 17. Federal Home Loan Bank Board.—Amends section 17 of Federal Home Loan Bank Act as proposed in recommendation 135, except for proposal in (2) thereof to delegate authority.

Section 18. Assessment on banks.—Amends section 18 of Federal Home Loan Bank Act as proposed in recommendation 136.

Section 19. Officers and employees.—Subsection (a) is the same as section 19 of Federal Home Loan Bank Act.

Subsection (b) is a new provision relating to conflicts of interest.

Section 20. Examinations and reports.—Amends section 20 of Federal Home Loan Bank Act as proposed in recommendation 137.

Section 21. Reports and records of other agencies.—Amends section 22 of Federal Home Loan Bank Act as proposed in recommendation 138.

Section 22. Forms of stock, debentures and bonds.—Same as section 23 of Federal Home Loan Bank Act.

Section 23. Eligibility for membership under act.—Same as section 24 of Federal Home Loan Bank Act.

Section 24. Succession of Federal home loan banks.—Same as section 25 of Federal Home Loan Bank Act.

Section 25. Liquidation or reorganization of banks.—Amends section 26 of Federal Home Loan Bank Act as proposed in recommendation 139.

Section 26. Eligibility for stock subscription.—Same as section 27 of Federal Home Loan Bank Act.

Section 27. Effect of partial invalidity of act.—Same as section 28 of Federal Home Loan Bank Act.

Section 28. Territorial applicability of act.—Amends section 29 of Federal Home Loan Bank Act as proposed in recommendation 140.

Section 29. Right to amend or repeal.—Same as section 30 of Federal Home Loan Bank Act.

TITLE V—FEDERAL SAVINGS AND LOAN ASSOCIATION ACT

Section 1. Short title.—Changes title of act from "Home Owners' Loan Act of 1933" to "Federal Savings and Loan Association Act."

Section 2. Definitions.—Amends section 2 of Home Owners' Loan Act as proposed in recommendation 142.

Section 3. Repeat of direct loan provisions of Federal Home Loan Bank Act.—Same as section 3 of Home Owners' Loan Act.

Section 4. Regulation of interest rates.—New provision as proposed in recommendation 143.

Section 5. Federal savings and loan associations.—Subsections (a), (b), (c), (d) (1), and (d) (2) are the same as the comparable provisions of the present law.

Subsection (d) (3) is a new provision based on advisory committee recommendation 144.

Subsections (e) and (f) are the same as subsections (e) and (f) of section 5 of Home Owners' Loan Act.

Subsection (g) is the same as subsection (h) of section 5 of Home Owners' Loan Act.

Subsections (h), (i), and (j) are the same as subsection (i) of section 5 of Home Owners' Loan Act, except as amended pursuant to recommendation 146.

Subsection (k) is the same as subsection (h) of section 5 of Home Owners' Loan Act.

Section 6. Federal savings and loan branches.—New provision based in part on advisory committee recommendation 166C.

Section 7. Restriction on associations, directors, and officers.—Subsections (a) and (b) are new provisions based on advisory committee recommendation 166G and are similar to section 22 (d) of the Federal Reserve Act.

Subsection (c) is a new provision based on advisory committee recommendation 166G and is similar to section 22 (e) of the Federal Reserve Act.

Subsection (d) is a new provision based on advisory committee recommendation 166H and is similar to 22 (f) of the Federal Reserve Act.

Subsection (e) is a new provision based on advisory committee recommendation 166F and should be compared with section 22 (g) of the Federal Reserve Act.

Section 8. Territorial applicability of act.—Revision of section 7 of Home Owners' Loan Act as proposed in recommendation 148.

Section 9. Separability provision.—Same as section 9 of Home Owners' Loan Act.

Title VI—Federal Savings and Loan Insurance Corporation Act

INSURANCE OF SAVINGS AND LOAN ACCOUNTS

Section 401. Short title.—New provision.

Section 402. Definitions.—Revision of section 401 of title IV of the National Housing Act (Housing Act) as proposed in recommendations 150, 151, and 152 and advisory committee recommendation 166B.

Section 403. Creation of Federal Savings and Loan Corporation Act.—Revision of section 402 of Housing Act as proposed in recommendations 153, 154, 155, and 156.

Section 404. Insurance of accounts and eligibility provisions.—Revision of section 403 by amending subsection (c) as proposed in recommendation 159 and by adding new subsections (e) and (f) as proposed in recommendation 158 (1).

Section 405. Premiums on insurance.—Amends section 404 of Housing Act as proposed in recommendations 160 and 161. (See also sec. 805 of committee print bill in regard to recommendation 161.)

Section 406. Payment of insurance.—Amends section 405 of Housing Act as proposed in recommendation 161 and including a provision similar to that proposed in recommendation 92 as contained in advisory committee recommendation 166K.

Section 407. Liquidation of insured institutions.—Amends section 406 of Housing Act as proposed in recommendation 162 as modified by advisory committee.

Section 408. Termination of insured status.—Amends section 407 of Housing Act as proposed in advisory committee recommendation 163.

Section 409. Regulation of holding companies.—New provision based on advisory committee recommendation 166A.

Title VII—Federal Credit Union Act

Section 1. Short title.—Same as section 1 of Federal Credit Union Act.

Section 2. Definitions.—Revision of section 2 of Federal Credit Union Act with no substantive changes.

Section 3. Creation of bureau.—New provision.

Section 4. Federal credit organization.—Same as section 3 of Federal Credit Union Act.

Section 5. Approval of organization certificate.—Same as section 4 of Federal Credit Union Act.

Section 6. Fees.—Same as section 5 of Federal Credit Union Act.

Section 7. Reports and examinations.—New subsection (b) added to section 6 of Federal Credit Union Act as proposed in advisory committee recommendation 190.

Section 8. Powers.—Same as section 7 of Federal Credit Union Act.

Section 9. Bylaws.—Amends section 8 as proposed in recommendation 167.

Section 10. Membership.—Same as section 9 of Federal Credit Union Act.

Section 11. Members' meetings.—Same as section 10 of Federal Credit Union Act.

Section 12. Management.—Same as section 11 (a) of Federal Credit Union Act.

Section 13. Officers.—Amends section 11 (b) of Federal Credit Union Act as proposed in recommendation 169.

Section 14. Directors.—Amends section 11 (c) by striking the words "recommend the declaration of dividends" (see sec. 18 of committee print bill) and incorporates recommendation 170.

Section 15. Credit committee.—Amends section 11 (d) of Federal Credit Union Act as proposed in recommendation 171 as modified by advistory committee.

Section 16. Supervisory committee.—Same as 11 (e) of Federal Credit Union Act.

Section 17. Reserves.—Same as section 12 of Federal Credit Union Act.

Section 18. Dividends.—Amends section 13 as proposed by advisory committee recommendation 180.

Section 19. Expulsion and withdrawal.—Same as section 14 of Federal Credit Union Act.

Section 20. Minors.—Same as section 15 of Federal Credit Union Act.

Section 21. Certain powers of director.—Same as section 16 of Federal Credit Union Act, except new subsection (i) added relating to conflicts of interest.

Section 22. Fiscal agents and depositories.—Same as section 17 of Federal Credit Union Act.

Section 23. Taxation.—Same as section 18 of Federal Credit Union Act.

Section 24. Partial invalidity; right to amend.—Same as section 20 of Federal Credit Union Act.

Section 25. Space in Federal buildings.—Amends section 21 of Federal Credit Union Act as proposed in recommendation 173 and modified by advisory committee.

Section 26. Territorial applicability of act.—Amends section 22 of Federal Credit Union Act as proposed in advisory committee recommendation 181.

Title VIII—Miscellaneous Amendments

Section 801. Repealing provision.—This section repeals all the present statutes relating specifically to national banks. These statutes, except for obsolete provisions, are reenacted in title I of the committee print bill.

Section 802. Federal intermediate credit banks.—Amends Federal Farm Loan Act as proposed in recommendation 38.

Section 803. Amendments to Criminal Code.—Adds new provisions to Criminal Code including recommendations 43, 164, 165, 166, and 174.

Section 804. First and Second Liberty Bond Acts.—Amends the First and Second Liberty Bond Acts as proposed in recommendation 79.

Section 805. Savings clause.—Subsection (a) is a savings provision for national bank notes .

Subsection (b) is a savings provision for loans under section 13 (b) of the Federal Reserve Act.

Subsection (c) is the same as the proviso clause in section 26 of the Federal Reserve Act.

Subsection (d), see recommendation 161.

Section 806. Separability provision.—New provision.

Section 807. Right to amend.—New provision.

Senator Robertson. Now, gentlemen of the committee, our first witness today is the very fine and able chairman of our advisory committee, Mr. Kenton R. Cravens, president of the Mercantile Trust Co., of St. Louis.

Mr. Cravens and the members of his advisory committee have done a splendid job, and I am sure that is appreciated by all of the members of our committee. I am happy that Mr. Cravens has brought with him today the chairmen of four of his subcommittees. He will make the initial statement and I assume it would be better for us to let him make it without interruption, and then there can be questions, and after that he can present his subcommittee chairmen to emphasize and buttress any particular point he thinks ought to be reinforced.

Mr. Cravens.

STATEMENT OF KENTON R. CRAVENS, CHAIRMAN; ACCOMPANIED BY EVERETT D. REESE, SUBCOMMITTEE ON NATIONAL BANKS; REESE H. HARRIS, JR., SUBCOMMITTEE ON FEDERAL DEPOSIT INSURANCE CORPORATION; HENRY A. BUBB, SUBCOMMITTEE ON SAVINGS AND LOAN ASSOCIATIONS; WILLIAM W. PRATT, SUBCOMMITTEE ON FEDERAL CREDIT UNIONS, ADVISORY COMMITTEE FOR THE STUDY OF FEDERAL STATUTES CONCERNING FINANCIAL INSTITUTIONS AND CREDIT

Mr. Cravens. Mr. Chairman and members of the committee, as Senator Robertson has stated, I do have with me today 4 of our 5 subcommittee chairmen, Mr. Everett D. Reese, chairman of our Subcommittee on National Banks; Mr. Reese Harris, Jr., Subcommittee on the Federal Deposit Insurance Corporation; Mr. Henry A. Bubb, Subcommittee on Savings and Loan Associations, to my right; and Mr. William W. Pratt, chairman of the Subcommittee on Federal Credit Unions, to my left.

I am sorry to report that my vice chairman, C. Francis Cocke, has still not recuperated sufficiently to be here on his own power, and we regret his absence.

Unfortunately Mr. John J. McCloy, chairman of the Subcommittee on the Federal Reserve Act, was not able to be here.

On behalf of each of the members of the advisory committee, I desire to thank the Senate Banking and Currency Committee for the unique opportunity which has been accorded us to serve in this important undertaking. Each of our members, our secretary and our counsel has given freely of his time and energies in the pursuit of our duties. I trust that our report adequately reflects the unselfish, conscientious, and objective manner in which they approached the many problems which they considered. As indicated in my letter of transmittal, our committee unanimously agreed to our report, except as to three recommendations noted therein.

At the outset I should apologize for the length of this statement, but it is a long bill and I think we should put in the record all of the comments we have with respect to the various sections.

Senator Robertson. Let me say this is not going to be a precedent for all of the witnesses, but I just want to point out that we have had the benefit of Mr. Cravens' services now for going on 2 months, and we not only have not paid him anything, but he has paid for all traveling expenses. I think under the circumstances, therefore, he would certainly be entitled to tell us what he has found out for us in that period.

Mr. Cravens. If you are following my statement you will find that I do depart from it in many places and omit in some places.

The statement is broken up into five parts:

Part I: Instances where recommendations of the advisory committee have been followed in matters of more or less technical nature.

Unless questions arise, I will not discuss these but will place in the record a list of such recommendations by their numbers and will follow them by reference to the pages of the bill at which they have been implemented. Needless to say, our committee was pleased to see that they were adopted.

Senator ROBERTSON. If you will permit the chairman to interrupt you there, he will say that without objection your entire statement and all of the exhibits will go into the record at the end of your remarks. You may proceed to give us orally what you have to say.

Mr. CRAVENS. Thank you, Mr. Chairman.

Senator ROBERTSON. You may proceed.

Mr. CRAVENS. Part II. Instances where recommendations of the advisory committee have been followed on matters which I believe warrant discussion in some detail.

Part III: Instances where the committee print does not follow recommendations of the advisory committee. These I will discuss separately.

Part IV: Instances where the bill includes matters which are new in that the advisory committee has not considered them. As to these I am not in a position to speak for the advisory committee. Thus I would like to have the benefit of testimony of others, then give the advisory committee an opportunity to consider these new matters and thereafter, if such be your pleasure, appear before you again and at that time report the advisory committee's views on these new matters and discuss any other points which may have been raised by the intervening testimony. Or I might say we could just submit a statement to that effect.

Part V are those instances where recommendations made by the advisory committee have not been incorporated in the bill, we assume because jurisdiction over them lies elsewhere.

RECOMMENDATION 2—APPOINTMENT OF TWO ADDITIONAL DEPUTY COMPTROLLERS

The bill at page 2, section 5, provides for an increase in the number of Deputy Comptrollers from 3 to 5. In the light of the testimony which Comptroller Gidney gave before this committee on November 9, 1956, the advisory committee favors this change in the law.

RECOMMENDATION 45E—EMPLOYEE STOCK OPTIONS; RECOMMENDATION 45D—ISSUANCE OF PREFERRED STOCK OR DEBT OBLIGATIONS BY BANKS

I have purposely put these recommendations together because they go a long way in answering the urgent need of banking; namely, the need for better management and more capital funds.

Frankly, banks are at a serious disadvantage competing for qualified executive personnel because they are not permitted to use the strong inducement provided by employee stock-option plans. This situation must be remedied if we are to improve the caliber of management in the Nation's banking system. At present there is no statutory authority by which national banks are permitted to establish such programs.

Equally important as good management is adequate capital. Since under the present law a national bank may issue preferred stock only as an emergency measure, the statutes are meaningless. Furthermore, under present law a national bank cannot issue debt obligations as a means of acquiring additional capital. Therefore, limiting national banks access to capital by way of common stock only is unrealistic and a great deterrent to the banking system's efforts to raise the capital funds it needs. Preferred stock or subordinated debenture issues might well offer a better and more feasible means of acquiring additional capital. Then, too, the redemption features of such securities provide a flexible means of adjusting the requirements of the banks to the needs of the times. If the Nation's banking systems are going to supply the needs of our present dynamic and full economy, the national banking system must provide leadership on these constructive measures.

RECOMMENDATION 13—UNEARNED DIVIDENDS

At page 11 of the bill, section 22 implements this recommendation. The present law is changed to authorize quarterly declaration of dividends as well as semiannual and annual declarations. Section 22 (b) provides that the approval of the Comptroller of the Currency shall be required if the total of all dividends declared in any calendar year exceeds the net profits of that year combined with its retained net profits of the preceding 2 years less any required transfers to surplus.

We believe that these changes are constructive.

RECOMMENDATION 17—SHAREHOLDERS' LISTS

At page 12 of the bill, 12 United States Code, section 62 is revised based on this recommendation. The bill, however, does not follow the recommendation of the Comptroller which the advisory committee approved, but continues the present law to the effect that the statutory right of inspection by a shareholder of a national bank is not qualified by a requirement of showing proper purpose. The committee fails to understand the necessity for granting to a shareholder of a national bank a broader right of access to a stockholder's list than is enjoyed by shareholders of corporations generally. Thus section 23 (a) of the bill and the corresponding sections which I will mention should be amended to conform to the Advisory Committee's recommendation.

It should be noted that the substance of section 23 (a) is repeated at page 94 of the bill as section 23 (i) relating to State member banks of the Federal Reserve System and at page 164 as section 27 of the Federal Deposit Insurance Act. While no recommendations were made as to this, either by the supervisory agencies or by the advisory committee, these sections have been inserted apparently on the basis of uniformity.

Further at page 12, section 23 (b) requires that a national bank shall notify the Comptroller immediately of any single transaction involving "the purchase or sale of 10 percentum or more of the outstanding shares" of the association. This language is repeated as to State member banks at page 94 and as to insured banks at page 164. This is an entirely new provision. While we take no particular exception to the principle of reporting stock transfers, we question the language which has been used as it leaves the situation in a twilight zone. If the idea is adopted it should be limited to a transaction as reflected by the stock transfer records of the particular banking institution.

May I say at that point, Mr. Chairman, that this would put the president or the management of a bank in a very precarious position. You might be at a social event, or walking down the street, and hear all kinds of gossip as to who had bought a large block of your stock, and you would not know whether it was or was not true; but this bill would require you to report that to the Comptroller. It just will not work. It has to be a matter certainly limited to the transfer records of the bank itself.

Senator ROBERTSON. Mr. Cravens, one of the ideas of these hearings is to get the advice of experts—and I am not one of them—on how to make the bill better.

Mr. CRAVENS. I think the bill would be better if it were limited to the transfer records of the particular bank.

RECOMMENDATION 15—CUMULATIVE VOTING IN ELECTION OF DIRECTORS

At page 13 of the bill section 26 (c) implements this recommendation. This language is similar, if not identical, to S. 256, which passed the Senate of the 84th Congress and was reported favorably by the House Banking and Currency Committee.

I believe there was so much said at that time that I will pass any comments on it other than it is good and should be included in this bill as it has been.

RECOMMENDATION 21—REMOVED OFFICER OR DIRECTOR PROHIBITED FROM VOTING STOCK

At page 15 of the bill section 29 revises 12 United States Code, section 77, as it relates to the removal of officers or directors of national banks. The bill includes a comparable provision relating to officers and directors of State member banks at page 101 and further at page 207 includes a comparable or similar provision relating to officers and directors of Federal savings and loan associations.

All of this material is new and was not the subject of any recommendation. I feel, however, that the changes which have been made do meet with the approval of the advisory committee. I note particularly the fact that the procedures are tied in with the Administrative Procedures Act and that the review by the courts shall be upon the weight of the evidence. This is a very sound change.

RECOMMENDATION 6—CONTRIBUTIONS BY NATIONAL BANKS

At page 18 of the bill, section 31 (a) (8) implements this recom mendation by authorizing national banks to make contributions irrespective of State law to nonprofit educational institutions and to nonprofit civic organizations. In his original recommendation the Comptroller did not recommend the use of the word "nonprofit" in the case of civic organizations. The advisory committee approved of the Comptroller's recommendation. Now the bill limits the contributions to nonprofit civic organizations. Speaking personally, I feel that it would be better if the word were not used in the bill in this particular instance as the purpose is the controlling factor and is well defined.

In order words, it is not what kind of a corporation—profit or nonprofit—but what is the purpose of the corporation that should be the rule and the governing factor.

RECOMMENDATION 60—STOCK ACQUISITIONS IN CONNECTION WITH ABSORPTIONS

At pages 20 and 93 of the bill section 32 (b), relating to national banks, and section 23 (d), relating to State member banks, implement this recommendation. While both the Board of Governors and the advisory committee suggested that permission might be granted to "purchase and hold temporarily" stock of another bank, the bill discards the word "temporarily" and fixes the period of holding at a maximum of 90 days. We concede that "temporarily" is not as definite as is 90 days, but we wonder if there is real need of being so definite here where the approval of the appropriate supervisory authority has to be obtained in advance. In some instances 60 days' notice must be given for stockholders' meetings. Thus 90 days may be too limited a period. It would seem that a period of 6 months would not be excessive in this situation.

RECOMMENDATION 34—TRUST POWERS

The Comptroller recommended that the authority to license and regulate the exercise of trust powers by national banks historically reposing in the Board of Governors of the Federal Reserve be transferred to him. At page 20 of the bill section 33 implements this recommendation which was approved by the advisory committee. At the earlier hearings Governor Robertson interposed no objection to this action but suggested that, if it be adopted, the Board's regulatory authority over common trust funds likewise be transferred to the Comptroller. The bill does not make this additional change and the advisory committee agrees that it should not be made.

RECOMMENDATION 24—EXCEPTION TO 10 PERCENT LOAN LIMIT ON OBLIGATIONS CONCERNING DAIRY CATTLE

At page 25 of the bill section 34 (b) (7) (B) implements this recommendation so that the loan limit with respect to obligations arising out of the sale of dairy cattle is increased to 25 percent with the result that the same limitations as are applicable to livestock will be applicable to dairy cattle. The advisory committee could not see why that was not the case originally.

RECOMMENDATION 23 (1)—EXCEPTION TO 10 PERCENT LOAN LIMIT ON OBLIGATIONS CONCERNING INSURABLE PERISHABLE READILY MARKETABLE STAPLES UNDER REFRIGERATION

At page 25 of the bill section 34 (b) (6) (B) implements this recommendation and increases to 25 percent of capital and surplus the applicable loan limit as relates to such staples except where the obligations are "secured by the identical staples for more than 6 months." As a practical matter we can see trouble ahead through the use of the word "identical." Doesn't the language mean that the 6-month period can be increased by the bank obtaining substitution of collateral in a minimum percentage?

In any event, I suggest that this language be checked.

RECOMMENDATION 23 (2)—LOAN LIMIT ON INSTALLMENT CONSUMER PAPER

At page 27 of the bill section 34 (b) (12) implements the recommendation which the advisory committee made on this subject. Here the recommendation of the Comptroller has been supplemented by a proviso to the effect that the 10 percent limitation (as regards the maker) shall apply rather than the 25 percent limitation (as regards the endorser) where, after evaluation of the responsibility of each maker has been made, an officer of the bank, designated for such purpose by its board of directors, certifies that in acquiring such paper from the particular seller the acquiring bank is relying primarily upon the obligations of the makers for payment of the paper.

Senator ROBERTSON. May I interrupt you there? I said I am not going to ask you any questions and I am not going to ask any questions; but yesterday I heard a fine sermon on faith and the description of the difference between the definition of faith, Paul's famous definition, which was, "the evidence of things unseen; the substance of things hoped for," and the faith of the centurion. He was a Roman in the Jewish community and was asking a Jew to heal his suffering. That was the picture.

Now you are discussing a technical thing. Instead of giving us a definition, could you give us a picture of it?

Mr. CRAVENS. Yes. We will start with the easiest kind of an example.

Let us say an automobile dealer selling automobiles on time payments. At the present time under the law if he uses a conditional sales contract in certain States, which is nonnegotiable, the buyer has no limitation on the amount of paper that they purchase. If he uses a chattel mortgage, which is negotiable, they may be limited. That is one point.

The second point is that if the purchasing bank buys that paper with recourse we say that if they rely entirely on the endorser, the dealer's guaranty, then they should be subject to some limitation. But we also say that if they investigate the credit of each of the people that buy each automobile and are satisfied as to the credit standing of that particular buyer, then they should not be limited as to the amount of paper they buy from that dealer, notwithstanding the fact that they buy it with recourse.

In other words, we say if you investigate the buyer of that car then loan limitation should be applied to him. If you do not investigate and buy it on the guaranty of the dealer selling you the paper, then the loan limit should apply to the guarantor.

Does that clear it?

Senator ROBERTSON. That helps to eliminate that question.

RECOMMENDATION 35—LIMITATION ON REAL ESTATE LOANS

Mr. CRAVENS. This recommendation was divided into four parts plus an additional recommendation of the advisory committee. Each has been followed in the bill, viz:

Recommendation 35 (2) is implemented at page 28 by section 36 (a), which section at page 29 also incorporates the committee's additional suggestion. Recommendation 35 (2) would permit national banks to make loans on leaseholds having at least 10 years to run beyond the maturity of the loan.

We think that is ample time to provide safety.

At page 29 the maximum aggregate of real-estate loans which may be made by a national bank is limited by a third alternative, i. e., 20 percent of demand deposits.

I might mention there, presently their limit is 60 percent of their savings. This gives them an alternative provision which makes it more flexible.

The advisory committee favors these additions to the statute.

Recommendation 35 (1): This is implemented in accordance with the advisory committee's recommendation by section 36 (c), which appears at page 30 of the bill.

Recommendation 35 (4): At page 30 of the bill section 36 (e) implements this recommendation.

This recommendation would permit national banks to make loans to manufacturing and industrial businesses which are secured by liens on the plant real estate where the loans are for the purpose of furnishing working capital, without such loans being considered as real-estate loans. These loans are really business loans and represent ordinary business financing, and should not be treated as real-estate loans subject to the provisions of the law relating to real-estate loans of national banks. To meet industrial needs, national banks are making such loans today, but are forced to make them on an unsecured basis. While the bank may expect repayment of such loans through liquidation of inventory or receivables, or through the operations and earnings expected to be derived from the additional facilities so financed, nevertheless, they should not be denied the benefit of the additional collateral which could be provided by mortgage on the company's plant real estate taken as a precaution against contingencies.

In other words, they should not be forced to loan unsecured simply because they want some additional collateral.

Recommendation 35 (3): This is implemented by section 36 (f) at page 31 of the bill where it is provided that national banks may make loans to finance construction of buildings upon the security of purchase contracts entered into under the Public Buildings Purchase Contract Act of 1954 and the Post Office Department Property Act of 1954 without regard to the limitations in regard to real estate loans.

With these forgoing changes made in the real estate loan section of the National Bank Act, such will represent a vast improvement over our present law.

RECOMMENDATION 45B—INCREASE IN DEBT LIMIT OF A NATIONAL BANK

This and recommendation 22 have been implemented at page 31 of the bill by section 37, which revises 12 United States Code, section 82, to increase the debt limit of a national bank from 100 percent of its capital to 100 percent of capital and surplus and renders the section inapplicable to capital funds obtained through the issuance of capital notes or debentures outstanding under section 21, set forth on page 10 of the bill.

Incidentally, those would be subordinate debentures and should be exempt.

The Advisory Committee believes that these are constructive changes in the law.

RECOMMENDATION 9—BRANCHES RETAINED AFTER MERGER, ETC.

At page 32 of the bill section 39 (b) implements this recommendation as to which the Advisory Committee in its report stated at page 3 thus:

This recommendation would permit a national bank continuing on merger or consolidation with another bank under a resultant national-bank charter to operate the branches the national bank theretofore lawfully operated without obtaining new approval from the Comptroller. The committee understands the proposition to be one of merely eliminating unnecessary paperwork in such cases as compared with broadening the power of national banks to have and operate branches. On the basis of such understanding being correct, this recommendation is approved.

It seems to us that the implementing language goes on further than our understanding.

RECOMMENDATIONS 11 AND 115C—SCHOOL SAVINGS PROGRAMS

At pages 34 and 149 of the bill section 39 (f) of the National Bank Act and section 2 (m) of the Federal Deposit Insurance Act define "branches" so as not to include school-savings programs. The Advisory Committee approved of these changes and is glad to not that such programs are confined to schools—

located in the trade area of the bank and within the State in which the bank is situated.

RECOMMENDATION 45C—LOANS AND INVESTMENT ON BANK BUILDINGS

Heretofore both National and State member banks have been limited to 100 percent of their capital as regards the amount they may have invested in bank premises or in an affiliate holding the bank premises. At pages 35 and 94 of the bill section 43 and section 23 (j) change the maximum to 100 percent of capital or 50 percent of combined capital and surplus, whichever is greater.

For example, many banks may have $100,000 capital and $1 million surplus. In that particular case it is a great hardship on the bank having that. You force them to transfer from their surplus to their capital accoun. If we take whichever is greater, that is 100 percent of capital or 50 percent of combined capital and surplus, we think it is infinitely more fair.

The purpose of the change is to give relief to the bank which has a large surplus and a small capital. In giving this relief, however, the bank which has made its future projections based on a larger capital and a lesser surplus should not be prejudiced. Thus the Advisory Committee favors these provisions.

RECOMMENDATION 36—DEPOSITS IN CORPORATIONS NOT SUPERVISED BY ANY STATE BANKING AUTHORITY

Here the Advisory Committee approved a recommendation which the Comptroller made in regard to amending 12 United States Code, section 378, so as to require that a corpration receiving deposits shall be subject to examination under the banking laws. This recommendation has been implemented at page 36 by section 44 (a) (2) (A), wherein new language appears. It appears to us that the new language of the bill does not go as far as the Comptroller suggested that the change go. If the Comptroller believes that the new language is adequate, certainly we would recommend no change.

RECOMMENDATION 45F—NATIONAL BANKS WRITING INSURANCE

At page 37 of the bill section 45 implements this recommendation which is that 12 United States Code, section 92, be revised so as to permit National banks located in towns of 5,000 or more to write insurance if State banks in such towns are permitted to do so by State law.

Section 45 includes paragraph (b) which is new and was not the subject of a specific recommendation; and paragraph (c) includes a grandfather clause. Both of these additions were considered and are within the area of the recommendation. The purpose of these changes is to place National banks on a parity with State banks in these particulars.

RECOMMENDATION 5—RESTRICT STATE AUTHORITIES FROM SUBJECTING NATIONAL BANKS TO LICENSING, ETC.

At page 41 of the bill section 51 implements this recommendation to the end that whatever doubt has existed as to the right of a National bank to exercise its corporate powers without State or local interference is resolved.

Most assuredly, the Advisory Committee favors the inclusion of the new provision in the statutes.

RECOMMENDATION 28—REPORTS TO COMPTROLLER

At page 42 of the bill section 52 (c) implements the recommendation, in principle, of our committee. Our recommendation, based on that of the Comptroller's, was to change from 5 to 10 days the time within which National banks must transmit required call reports to the Comptroller, as provided for in S. 2996, introduced by Senator Robertson in the 84th Congress.

RECOMMENDATION 58—REPORTS FROM MEMBER BANKS

At pages 42 and 92 of the bill will be found language which implements this recommendation of the Board of Governors which was discussed by the committee as to the authority of the Board of Governors to prescribe different forms of reports of condition, earnings, and dividends, and to require such reports on a sample basis. In addition the bill follows the recommendations of the Advisory Committee with respect to publication of earnings, expenses and dividends; namely, that the Board should not be so authorized and accordingly the bill does not give the Board this requested authority. If the Board of Governors wishes to propose a reasonable classification of banks according to size and to recommend that the group of smaller banks shall not be required to furnish more than two reports in any year, the Advisory Committee would concur in that recommendation provided that a reasonable limitation is placed on the number and kinds of reports which the group of larger banks may be required to furnish in each year. This applies with equal force to section 52 of title 2 of the committee print which gives similar authority to the Comptroller of the Currency. If adopted, the same reports should be authorized and required by the Federal Deposit Insurance Corporation.

In short, I think the Advisory Committee is opposed to these provisions as now written at pages 42 and 92.

Note that I said "I think." Frankly, I am confused in this situation of implementing language. I don't know what it means, and as a result I think I will not talk any more about that.

RECOMMENDATION 33—APPOINTMENT OF CONSERVATORS; RECOMMENDATION 106—LIABILITY OF FEDERAL DEPOSIT INSURANCE CORPORATION FOR INSURED DEPOSITS

By recommendation 33 the Comptroller urged that the Bank Conservation Act be amended to authorize him to appoint a conservator for a national bank which has sustained substantial losses resulting from defalcations. The Advisory Committee approved and the recommendation has been implemented by section 64 (j) at page 64 of the bill. We note that section 64 (d) at page 61 of the bill does not read the same as does section 205 of the Bank Conservation Act, but understand that the reason therefor is the fact that the Federal Deposit Insurance Act has been changed to read as it does at page 168 of the bill, where section 30 (c) implements recommendation 106, which was approved by the Advisory Committee.

We believe that there still remains the problem of depositors whose deposits exceed the insured amount and suggest that payments to them on their noninsured balances should be made ratably as provided for other creditors.

I have been advised that the Comptroller believes that this power exists without further change in the statute. If that be the case our suggestion becomes moot.

I will now mention some of the more important changes in the Federal Reserve Act.

RECOMMENDATION 54—PAYMENT OF RESERVE BANK EARNINGS TO THE TREASURY

In keeping with this recommendation of the Board of Governors which was approved by the advisory committee, the bill at page 73 in section 7 of the Federal Reserve title provides that each Federal Reserve bank shall annually pay 90 percent of its net earnings to the Treasury as a franchise tax. This is the simplest method of clarifying the matter and its effect is to restore the situation as it existed prior to 1933 and the creation of the Federal Deposit Insurance Corporation in that it channels 90 percent of the net earnings of the Federal Reserve into the Treasury.

RECOMMENDATION 51—FEDERAL RESERVE BANK DIRECTORS RESIDENTS OF DISTRICT

At page 86 of the bill section 17 (a) implements both the recommendation of the Board of Governors and that of the advisory committee. This section of the bill provides that every Federal Reserve bank director shall be a resident of the district of the Federal Reserve bank on whose board he is serving, or shall reside within a 50-mile radius of such bank. Our committee preferred the pertinent qualification for appointment to, and continuation on, the board of directors of a Federal Reserve bank, be based on the principal place of business of the person appointed, and not the place of residence. Nevertheless, the "within 50-mile radius" qualification satisfies our committee's recommendation and the requirements for some metropolitan districts—New York City is a good example.

RECOMMENDATION 81—LOANS TO EXECUTIVE OFFICERS

At page 99 of the bill section 28 (e) implements the recommendation which was made in regard to the matter of member banks making loans to their executive officers. The committee print adopts the recommendation made by the Board of Governors and that of the advisory committee except in one particular. The advisory committee felt that the statute itself should define "executive officer" rather than leaving this to the Board to cover by regulation.

RECOMMENDATION 66—SIMPLE MAJORITY FOR BOARD ACTIONS

The Board of Governors recommended that the act be amended to provide that Board action might be taken upon the affirmative vote of a majority of a quorum of members. The advisory committee disapproved of this and recommended that the statute provide that the Board should act in all matters upon the affirmative vote of not less than a majority of the members of the Board in office at the particular time. The committee print bill follows this recommendation to the extent of placing in the law at the various places where particular votes are specified a new provision that the vote shall be by the affimative vote of a majority of the members of the Board in office. We urge that section 38 (d) at page 112 of the bill be amended to include a sentence providing that any action which the Board is authorized to take shall be taken by the affirmative vote of a majority of the members of the Board in office at the time.

RECOMMENDATION 83A—AUDIT OF FEDERAL RESERVE ROARD; RECOMMENDATION 85B—AUDIT OF FEDERAL RESERVE BANKS

At page 113, section 38 (h) implements recommendation 85A where it provides that accounts of the Board of Governors shall be audited at least once a year by certified public accountants. Further, at page 116, section 39 (m) provides that the Board shall have the adequacy of the procedures which it follows in examining the Federal Reserve banks reviewed by certified public accountants. These new provisions are based upon recommendations which the Board of Governors made and of which the advisory committee approves. They represents constructive legislation in the public interest.

RECOMMENDATION 83—POWERS OF FOREIGN BRANCHES OF NATIONAL BANKS

This recommendation of the Board of Governors in which the advisory committee concurred was that the powers of foreign branches of national banks should be enlarged upon as set out in S. 3922 of

Senator Robertson in the Eighty-fourth Congress. At page 125 of the bill section 45 (f) implements this recommendation, and we are happy to see it included.

RECOMMENDATION 85F—REPEAL OF SECTION 13B OF THE FEDERAL RESERVE ACT

The advisory committee recommended that section 13B of the Federal Reserve Act be repealed on the grounds that it has been little used and that the Federal Reserve banks should not compete with commercial banks in the lending field.

I should like to add, it is not the function of a central bank to lend. A supervisory agency and an agency responsible for the monetary and credit management should not be a lender under any circumstances.

I now pass to title III of the bill, which relates to the Federal Deposit Insurance Corporation.

RECOMMENDATION 115H—CHANGE IN ORGANIZATION OF FEDERAL DEPOSIT INSURANCE CORPORATION

At pages 148, 151, 152, and 153 will be found language implementing recommendation 115H of the committee.

These provisions vest the management of the Corporation in a single executive and administrator to be appointed by the President by and with the advice and consent of the Senate, and would create an Advisory Board of the Federal Deposit Insurance Corporation consisting of the Comptroller of the Currency, Chairman of the Board of Governors of the Federal Reserve System or his designee, and one person to be selected by the President who is a State official exercising functions relating to the supervision of State banks. We believe that this provision is highly desirable to promote greater efficiency and better management.

The single executive would achieve better administration and such an advisory board would provide a means of assuring to the administrator the benefits now derived from the presence of the Comptroller of the Currency, and add the benefits of Federal Reserve Board and State supervisory participation, all so necessary in a situation so complex as that presented by our present banking structure.

RECOMMENDATION 91—INSURANCE OF INTEREST ON DEPOSITS

At page 149 of the bill section 2 (k) includes as an insured deposit "interest accrued to the date of the closing of the bank." This language implements recommendation 91, which was approved by the advisory committee and is a constructive, and should I say equitable, change in the law.

RECOMMENDATION 92—TRANSFERRED DEPOSIT

At page 149 of the bill section 2 (l) restores to the law the express assurance that a transferred deposit means a demand deposit in a new bank or other insured bank.

The philosophy of this is that if the bank closes and the Federal Deposit Insurance Corporation does not have anyone to assume the liabilities of that bank, then the insured depositor gets cash up to

$10,000, even though he has a time or savings account. If the Federal Deposit Insurance Corporation is fortunate enough to get another bank to assume those liabilities, we think the depositor should have the benefit of a demand account in that new institution, which is exactly the same place he would have been, had the deposit not been transferred to another bank.

It is equitable and fair and it should be noted that a comparable change is made at page 223 of the bill, pursuant to recommendation 166K, which has to do with the Federal Savings and Loan Insurance Corporation.

RECOMMENDATION 97—ASSESSMENT CREDIT

This recommendation in the form in which it was approved by the advisory committee has been implemented in section 18 at page 159 of the bill. Recommendation 97 (e) which was disapproved is not included in the bill. As section 18 is written it appears to reflect properly the thinking of our committee. Later I will comment on the failure of the bill at this point to implement recommendation 115G of the advisory committee.

RECOMMENDATIONS 42, 85, AND 114—REGULATION OF MERGERS

Each of the supervisory agencies recommended that section 18 (c) of the Federal Deposit Insurance Act be amended as it was sought to be amended by S. 3911 of the 84th Congress and the advisory committee approved.

As the record on S. 3911 before this committee is full and adequate, I will not repeat here.

RECOMMENDATION 99—PROCEDURE FOR TERMINATION OF INSURED STATUS

At page 165 of the bill section 29 implements the Federal Deposit Insurance Corporation's recommendation in this regard as it was approved by the advisory committee. In addition, however, section 29 provides that the hearing on termination shall be held in accordance with the provisions of the Administrative Procedure Act and that review by the courts shall be upon the weight of the evidence. This was added as it has been in the statutes relating to the termination of insurance of accounts of Federal savings and loan associations. These provisions should in fairness be available to banks.

RECOMMENDATION 112—CIVIL SERVICE RETIREMENT

The advisory committee interposed no objection to this recommendation of the Federal Deposit Insurance Corporation provided that the cost was charged to the capital account of the Federal Deposit Insurance Corporation and not to "net assessment income." We are pleased to see that section 39 of the bill does just that.

RECOMMENDATION 115B—AUTHORITY TO PRESCRIBE BY REGULATION EMPLOYMENTS THAT MAY INVOLVE CONFLICT OF INTEREST

The Federal Deposit Insurance Corporation recommended that it be authorized to make regulations governing the employment of its employees by insured banks in situations involving a possible conflict of interest. The advisory committee approved this recommendation, noting, however, that the Comptroller of the Currency through the years apparently has had no difficulty with this problem even though he has not had the benefit of a statute on this point.

At page 180 of the bill section 40 (d) implements this recommendation providing that it shall not be lawful for any employee or former employee of the Federal Deposit Insurance Corporation to accept employment in any insured bank except pursuant to regulations prescribed by the Federal Deposit Insurance Corporation. The section further provides penalties upon conviction of any violation of the section.

Comparable provisions relating to the Office of the Comptroller, the Federal Reserve Board, the Federal Home Loan Bank Board, and the Bureau of Federal Credit Unions have been inserted at other points in the committee print in order to achieve uniformity. We do not feel that any exception can be taken to this.

We note, however, that at pages 248 and 249 of the bill there appear provisions which seem to be in direct conflict with the sections of the bill which I have just referred to. As the advisory committee has not considered this new material, I am not in a position to state its views. Speaking personally, however, I am constrained to think that the provisions at pages 248 and 249 of the bill are much too broad, and should be removed from the bill.

Senator ROBERTSON. May I interrupt there to say that I agree with you on that, and before you conclude your testimony I would be glad to have your recommendations on how it should be revised.

Mr. CRAVENS. Thank you. I intend to comment more on this later, and following that I will be glad to give you my recommendations.

RECOMMENDATION 115F—ABSORPTION OF EXCHANGE AS INDIRECT PAYMENT OF INTEREST

The Board of Governors of the Federal Reserve System by their recommendation 77 suggested that the words "directly or indirectly by any device whatsoever" be removed from section 19 of the Federal Reserve Act and that it be made clear that the term "interest" should include only cash payments made or credits given by a bank for the account or benefit of a depositor and further that appropriate amendments be made to make certain that the same limitations as to the payment of interest should apply both to member and nonmember insured banks either by an explicit statement in the law as to both types of banks as to whether absorption of exchange charges shall be deemed a payment of interest or by a provision authorizing either the Board of Governors or the Federal Deposit Insurance Corporation to define the term "interest" for both classes of banks. The Federal Deposit Insurance Corporation made no specific recommendation on this subject but in the testimony given by its representatives in November it was stated that there is unfairness when one bank can absorb and another cannot, depending upon whether or not it is a member of the Federal Reserve System.

I think I should like to depart right there and maybe get this problem in a little better focus.

We really have two problems here. One is what constitutes—I might say the first problem is whether or not we take the recommendation of the Federal Reserve Board and limit what constitutes interest on demand deposits to cash or credit, or whether we include it indirect by any device whatsoever.

The second problem is the absorption of exchange. The Federal Deposit Insurance Corporation position has been that absorption of exchange did not constitute payment of interest on deposits of the member banks——

Sentor ROBERTSON. Have you found any law in the Federal Deposit Insurance Corporation Act that authorized them to pass on what is and what is not interest?

Mr. CRAVENS. Well, not being a lawyer, I have not. My own counsel has some grave doubts about that too.

I would like to say this, though, with respect to the Federal Reserve that I am not happy to see a Federal agency make the reservation it did simply to make its job easier. They frankly admitted they would like to have it cash or credit because that was easy to define.

Senator ROBERTSON. Mr. Cravens, as we know, this committee went into the problems of this bill on the absorption of exchange. I am informed that a thousand banks out of some 14,000 do not pay an exchange charge, and some have just a small exchange charge, and some have up to one-eighth of a percent, I am told. A number of them surround a bank, for instance, like a member bank in Wilson, N. C., which makes it very tough.

I have already mentioned the difference between a definition and a picture. Can you give us a picture of this absorption of exchange?

Mr. CRAVENS. I think I will complete my written testimony on this, so that will put it all on the table, and then I will give you some examples.

The advisory committee at page 30, et seq., of its report suggested that the Federal Deposit Insurance Act be amended to read the same as the Federal Reserve Act with respect to the payment of interest on demand deposits. The reasons for this recommendation were that our committee thinks that the present lack of uniformity on this subject is deplorable; that uniformity should be achieved as we believe the Congress originally intended; that the direct or indirect payment of interest on demand deposits should be unlawful both as to nonmember insured banks as well as member banks; that the ruling as to the absorption of exchange constituting a prohibited payment of interest should be the rule.

Since the date of advisory committee's report legal questions have arisen as to whether or not the implementation of our committee's recommendation will, as a matter of law, produce the result which our committee intended to achieved. In the light of this fact and for the reasons stated at length in the advisory committee report, I feel that this issue should be met squarely, to the end that absorption of exchange shall be outlawed and shall be outlawed for all insured banks alike, whether or not they are members of the Federal Reserve System. Thus, I urge that the committee print bill be amended as follows:

At page 163 of the bill strike out the first sentence of section 26 and substitute the following:

No insured bank, whether or not it is a member of the Federal Reserve System, shall, directly or indirectly, by any device whatsoever, pay any interest on any deposit payable on demand except as now or hereafter may be permitted by law or regulation of the Board of Governors of the Federal Reserve System in the case of a member bank of the Federal Reserve System.

Senator ROBERTSON. That is pretty clear.

Mr. CRAVENS. The result of this suggested change would clearly be—and I hope it is clear—that all insured banks, non-members as well as members, would be controlled by the regulations of the Board of Governors issued pursuant to section 41 at pages 117–118 of the bill. The Board consistently since September 1943 has ruled that absorption of exchange is an unlawful payment of interest.

In addition to the foregoing amendment, another might be made at page 118 of the bill. On that page the period at the end of section 41 (a) might be changed to a comma and the following added:

And provided further, That within the meaning of the provisions of this section the absorption of exchange shall be deemed to be a payment of interest.

I urge that even though this last amendment is not made, that section 26 on page 163 be changed to read as I have suggested. If the only way to achieve uniformity is by the Congress forcing one agency to agree with another, then such action certainly should be taken here in order to eliminate the terrible inequity which has existed far too long.

The problem arises because we have quite a number of banks throughout the country that do not operate on a par clearance basis. Here is a simple illustration: When a check is drawn on a no-par bank payable to a third party, when the item is cleared on the no-par drawee bank, that bank makes a charge for clearance. We will say that the check is for $100 and the no-par drawee bank remits $99 and retains $1 as a charge. Naturally, the payee of that check is thus going to lose $1. The payee deposits the check with his own bank. That collecting bank then clears it on the no-par bank. If the payee's bank of deposit could absorb that dollar's exchange, it would be rendering its customer a great service and might induce him to carry larger balances; but by so doing it would actually be paying him $1 interest on his demand deposit, and this it may not do if it is a member bank.

So we have the situation where a nonmember bank may absorb that $1 and in effect pay interest to its customer on a demand deposit, but we have right across the street a member bank that cannot do it. Therefore, the nonmember bank says to member bank's customer, "Bank with me and I will absorb the exchange." Therefore the nonmember bank gets the business.

I think that is as simply as I can explain it. It is just deplorable that we have for so many years had a situation which permits banks here doing one thing and over here they are not permitted to do it.

Do you have any questions to ask on the absorption of exchange?

Senator ROBERTSON. I think you have made that clear.

Mr. CRAVENS. Then yet us turn to the Federal Home Loan Bank Act and the Federal savings and loan associations, Mr. Bubb.

Recommendations 118 through 140, except recommendation 121, have all been incorporated in the revision of the Federal Home Loan Bank Act as it appears from pages 181 through 202 of the bill. All of these are recommendations of the Federal Home Loan Bank Board which the advisory committee deemed to have merit and thus approved them. We have assumed that that Board will check the implementing language more closely than have I.

At page 203 of the bill section 501 of the Home Owners Loan Act is amended to provide for a Federal Savings and Loan Association Act. While this was not the subject of a particular recommendation, I am pleased to see that this has occurred.

I note that recommendation 144 as made by the advisory committee at page 40 of its report has been implemented at page 207 of the bill by section 5 (d) (3), which is modeled after title 12 United States Code, section 77, as it is revised at page 15 of the bill as relates to national banks and at page 101 as it relates to State member banks. This provides uniformity and is in keeping with the thoughts of the advisory committee.

RECOMMENDATION 166C—BRANCHES OF FEDERAL SAVINGS AND LOAN ASSOCIATIONS

At page 211 of the bill section 6 pertains to branches of Federal savings and loan associations, and as we understand the situation it follows the language of H. B. 972, as passed by the Senate in the 84th Congress.

Recommendations 166F, G, and H: These recommendations of the Advisory Committee related to all insured savings and loan associations, and to all noninsured savings and loan associations, which are members of the Federal Home Loan Bank.

First I will take recommendation 166F. To eliminate the amount which any such association might loan to any of its officers or directors.

Recommendation 166G prohibits any such association from making or paying any greater distribution or dividend to any of its officers, directors, or employees than is received by its accountholders generally at any time within 1 year of the date of that payment.

Recommendation 166H makes directors of such associations liable for damages resulting from the violation of certain laws relating to such associations.

At pages 212 and 213 of the bill these recommendations have been implemented, but only as it relates to federally chartered savings and loan associations.

This is all right as far as it goes, but it does not go as far as we suggested. We believe it should be implemented as we suggested, even though it would require incorporating comparable provisions to nonmember insured banks.

I would like to stop here for just a minute. It is true that our committee did not consider the matter of subjecting nonmember insured banks to similar provisions, but we believe that it is so important and the provisions are so sound that they should be carried over to nonmember banks as well as member banks, and they should be carried over to all savings and loan associations, whether or not their accounts are insured by FSLIC.

Mr. Bubb may want to comment on this later, and I realize that this is new material as it relates to the bankers, but what I have said, at least is my personal position.

RECOMMENDATION 158 (1)—REGULATION OF INSURED INSTITUTIONS

At page 221 of the bill section 404 (e) implements this recommendation by providing that except with prior approval of the Federal Deposit Insurance Corporation no insured savings and loan association shall be a party to a merger or consolidation or purchase assets or accounts from other associations. This is something comparable to section 23 of the Federal Deposit Insurance Act as it appears at page 162 of the bill. Our committee feels that these provisions are in the public interest.

RECOMMENDATION 166A—HOLDING COMPANIES

At page 227 of the bill section 409 implements the recommendation which our committee made in regard to having holding company legislation relating to savings and loan associations. It is our understanding that the language employed is that which was used in the bill which Representative Spence, of Kentucky, introduced on this subject in the 84th Congress. Our committee did not consider this language, but it strongly endorses the principle.

Now I will turn to Federal credit unions.

Title VII of the bill recasts the Federal Credit Union Act beginning at page 229 of the bill. All of the recommendations which were made as to Federal credit unions which were approved by the Advisory Committee have been implemented by the bill. We believe that as a result the practices and procedures of these worthy organizations will be vastly improved.

I believe that is an understatement. We have made many fine improvements in this legislation that will be beneficial to the credit unions, and I am sure beneficial to their members.

I note particularly that recommendation 190 in regard to audits is implemented by section 7 (b) at page 231 of the bill. This provides that credit unions with assets of $50,000 or more shall have an annual audit by outside auditors approved by the Director of Federal credit unions and that unions with assets of less than $50,000 shall be audited annually by the Bureau of Credit Unions.

At page 235 of the bill section 15 increases the size of unsecured loans which may be made from $400 to $500, and also provides that the Director may impose by regulation maximum loan limits for all Federal credit unions or for any one or more classes provided the same is within the statutory limits. This last provision will provide a greatly needed safety factor in the operations of such credit unions.

At page 241 of the bill section 25 of the Credit Union Act implements recommendation 173 of the Advisory Committee and amends section 21 of the old act so that a credit union—

> the membership of which is composed exclusively of persons who are either presently Federal employees or are retired Federal employees and members of their families—

shall be eligible applicants for the allotment of space in Federal buildings.

I won't comment on the other changes in the Federal Credit Union Act, but I will simply say again that I think the changes are good and very helpful changes in the law.

I want to come to those matters now which have not been implemented in the committee print bill, which were recommendations of the Advisory Committee.

RECOMMENDATION 52—SERVICE ON RESERVE BANK BOARD OF FEDERAL ADVISORY COUNCIL

It is actually "and" service on the Reserve Bank Board and also on the Council.

At pages 74 and 85 of the bill will be found provisions which relate to the subject of this recommendation. Section 7 (a) at page 85 provides, among other things, that Federal Reserve bank directors, other than the Chairman, shall be prohibited from serving more than 2 full consecutive terms of 3 years each without an intervening period of not less than 3 years, and section 8 (a) at page 74 provides that members of the Feedral Advisory Council shall be prohibited from serving more than 6 consecutive terms of 1 year each without a similar intervening period.

It is the committee's opinion that advantages of preserving and promoting the autonomy of the Federal Reserve banks outweigh the possible benefits from rotation and that the present system has been beneficial and should be retained.

I think I ought to note again that Professor Chandler dissented on this recommendation.

RECOMMENDATION 79—RESERVES AGAINST DEPOSIT OF PUBLIC MONEYS

At page 120 of the bill will be found language which implements this recommendation of the Board of Governors, the first part of which our committee approved, and the second part disapproved.

The second part, as provided for in section 42 (f) at page 120 of the bill provides that member banks shall maintain the same reserves against public funds as against other deposits.

Our committee does not recommend—and I want to get that clear—standby authority with respect to waiving reserves against public deposits in case of an emergency—that authority can be readily provided in such case—but it based its recommendation primarily on the principle of giving the Board of Governors the broadest authority possible for the discharge of its monetary and credit control responsibilities.

Recommendation 115: The Federal Deposit Insurance Corporation recommended that sections 217 and 218 of the Criminal Code be amended to permit member banks to make loans to examiners and assistant examiners of the Federal Deposit Insurance Corporation when the loans were made in accordance with the Federal Deposit Insurance Corporation regulations. The advisory commitee approved this suggestion. The bill does not implement this recommendation. To the contrary, the bill at pages 248 and 249 makes it a crime for any member bank or any insured nonmember bank to make a loan to examiners who have, or within 2 years preceding the making of the loan have had, any duties in connection with the lending bank. I will refer to this subject later on in more detail.

Now we go to recommendation 115G.

RECOMMENDATION 115G—INCREASE IN ASSESSMENT CREDIT; RECOMMENDATION 166K—WITH REFERENCE TO THE FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION

Recommendation 115G of the committee was that a study be undertaken promptly and expeditiously to determine a reasoned formula for computing the proper premium cost to the insured banks for the risk involved, in the light of the present size of the Federal Deposit Insurance Corporation Deposit Insurance Fund supplemented by annual increases from income and assessments; and that meanwhile, the

Congress amend section 7 (d) of the Federal Deposit Insurance Act so as to provide that 1 year from the date of enactment of the act the annual net assessment income shall be credited pro rata to the insured banks.

Committee recommendation 166K was intended to treat the Federal Savings and Loan Insurance Corporation on a comparable basis.

These two important recommendations are not included in the bill yet; as I am sure that this committee will want to consider them, I bring them to your attention.

To place the problem in the proper perspective it is first necessary to establish a common, proper concept of the purpose of the Federal Deposit Insurance Corporation and the Federal Savings and Loan Insurance Corporation. Our committee concluded that the only possible purpose these insurance corporations could serve was to insure depositors against losses resulting from the day-to-day institutional failures occasioned by mismanagement, inadequate capital, local disaster, defalcation, and many other similar institutional casualties. It is also quite apparent that it is completely unrealistic to believe that these corporations could possibly insure depositors and account holders against losses occurring on a major scale incident to economic or other disaster, any more than the private insurance industry could insure losses incident to an all-out atomic war. No insurance company, private or public, could provide any real protection against universal economic disaster, and it would be immoral to mislead the public that it could.

If this is a proper concept of the purpose of these insurance corporations, then the Federal Deposit Insurance Fund seems to be adequate at this time. Such fund now exceeds $1.7 billion, which is equal to 1.41 percent of insured deposits. In the 22 years that the Federal Deposit Insurance Corporation has been in existence it has disbursed for working-capital purposes in the aggregate of less than $290 million in connection with receivership and deposit-assumption cases. More particularly, of this amount actual losses during the entire period amounted to only $19 million, and estimated possible future losses on cases that are still active amount to only $9 million. Thus, total actual or contingent losses of $28 million during the entire period are substantially less than the $39 million of income from investments accruing to the fund in the year 1955 alone. Furthermore, the fund was increased by more than $56 million in the year 1955 as a result of assessments.

While this record seems to be impressive, it is by no means conclusive because of the lack of comprehensive and actuarial information. It is a bare, startling fact that, inconceivable as it may seem, no study has been made which would provide an actuarial basis for determining the underwriting liabilities of the Federal Deposit Insurance Corporation and the Federal Savings and Loan Insurance Corporation. Let me qualify that by saying at least our committee could find none, nor was any made available to it.

It is essential that such a study be made. Our committee feels that such a study is feasible and this bill to amend and revise the statutes governing financial institutions and credit would be sorely lacking if it did not provide for such a study. Our recommendation would, in effect, force the proper agencies to make such a study and give them 1 year in which to do it. Results of such a study would clearly point out the problems and give the Congress the kind of information it needs to provide insurance protection to the Nation's savers without misleading them and without creating too heavy a burden on the Nation's banks and savings institutions.

We recommend that the present assessment rate continue during the period of this study, but that if the study is not completed by the end of the time provided for, and a more scientific assessment rate is not established, then further accumulations should be dispensed with until such scientific assessment rate is established.

Probably the most important aspect of the committee's recommendation with respect to these two insurance corporations is that the study would afford a Monetary and Financial Commission, should it be established, a place to start in reviewing the overall insured deposits program.

May I add, let us not wait for all of the time necessary for such a commission to act. Let us incorporate these changes in this bill, and force this study immediately.

I am sure I speak for every member of our Committee in strongly urging the Senate Banking and Currency Committee to consider these recommendations favorably.

RECOMMENDATION 166D—PROHIBITED PRACTICE

The advisory committee recommended making it unlawful for any institution organized under the laws of either the United States or a State which is not authorized to engage in the business of receiving deposits to represent or hold itself out in any manner that it is a bank. The committee print bill does not implement this recommendation because, as we understand it, within the time available it was impossible to work out proper implementing language.

I do have some implementing language, and with your permission, I will place it in the record, Mr. Chairman.

Senator ROBERTSON. It may be so inserted.

(The document referred to follows:)

MEMO IN REGARD TO RECOMMENDATION 166D

See page 36 of the committee print where title 12 United States Code, section 378, is amended in accordance with recommendation 36.

Here the draftsmen failed to implement Advisory Committee recommendation 166D. In order to implement this recommendation it is suggested that section 44 of the committee print be amended as follows:

1. In subsection (b) strike the designation "(b)" and substitute in lieu thereof "(c)."
2. Then insert a new subsection "(b)" reading as follows:

"(b) From and after the effective date of this Act it shall be unlawful for any institution organized under the laws of the United States in any manner to represent by its name, advertisements, communications or otherwise that it is a bank unless the law under which such institution is organized expressly authorizes it to engage in the business of receiving deposits and of making loans and discounts, or if not authorized to engage in such business, expressly authorizes the use of the word 'bank' in its corporate or business name."

RECOMMENDATION 195—MONETARY AND FINANCIAL INSTITUTIONS COMMISSION

Mr. CRAVENS. This recommendation was perhaps the most important one made by our committee. It was that the 85th Congress enact without delay legislation providing for the establishment of a Commission for the purpose of making an objective study and appraisal of the use of monetary controls to stabilize the Nation's economy and the impact of such controls upon the American system of free enterprise, and of the adequacy and responsibility of all financial institutions as custodians of the Nation's savings, to provide, individually and collectively under existing laws, the State and national financial needs for the continuing growth of our dynamic economy, giving appropriate consideration to deposit and savings insurance programs, the essentiality of Government lending and investing, and the tax burden on debtors, creditors, and equity owners.

May I say at the outset that this is not a matter that should necessarily be brought before Congress by incorporating it in the bill to amend and revise statutes governing financial institutions and credit. Accordingly, we considered that it was appropriate to omit this particular recommendation from the bill. As a matter of fact, it is preferable to have it incorporated in a separate bill in order to expedite the consideration of the recommendation.

The urgent need for such a study can hardly be questioned, both from the standpoint of the great many years since we have had one and also because of the tremendous changes in our economy during the intervening period.

As our Chairman today mentioned, the last such study was made by the National Monetary Commission in 1908 and it lead to the formation of the Federal Reserve System in 1913. The major economic and social changes which have occurred since 1908 have substantially altered the functions, types, and relationship of financial institutions to public need and the economy. Notwithstanding the new demands occasioned by these changes, all we have had is piecemeal legislation to meet the day-to-day needs of the economy.

We are indeed pleased to see the introduction of S. 599 to establish a National Monetary and Financial Commission, and we strongly urge the study and consideration of this bill. We favor, however, an amendment to the bill broadening the composition of the Commission to include adequate representation of the Congress as we originally recommended. The legislative branch should be represented by not less than 4 and not more than 6 members of the Banking and Currency Committees of the House of Representatives and the Senate, consisting of the chairmen and the ranking members.

Basically our committee felt the scope of such a Commission's functions should be stated in the broadest terms in order to avoid disputes in the initial stages over controversial issues, and the Commission after an exploratory period would be in a better position to define its areas of study. Nevertheless, section 3 of S. 599 seems to be conclusive and adequate, but if I properly interpret the views of the members of our committee, I would have to take strong exception to section 3 (f) (3). Certainly our committee wants no legislation that in the remotest way would prejudice the independence of the Federal Reserve System. This particular section might possibly—I don't say it would be, but it might possibly—be interpreted as a mandate by Congress for the Commission to question the System's independence of structure and power. Personally I believe that section 3 (f) (3) adds very little and that it might possibly be misinterpreted. Thus I feel that it should be delated from S. 599. I do not think it is too important, but it might well be deleted.

Senator ROBERTSON. May I ask if in your opinion there is anything in the Capehart resolution that would appear to be inimical to the banking system between the Federal banks and State banks?

Mr. CRAVENS. No. Definitely not.

Senator ROBERTSON. That is not involved?

Mr. CRAVENS. No.

We now turn to the measures which are not specifically covered by the report of the advisory committee.

See, for example, the last sentence of section 35 (a) at page 27 of the bill. There it is provided in the section dealing with interest which may be charged by a national bank that the purchase of evidence of indebtedness from the owner shall not be deemed to be a loan or discount except to the extent that "they" may be construed as loans or discounts under the laws of the State in which the bank is located. I am informed that the purpose of this provision is to legislate away the holding of the old case of *National Bank* v. *Johnson* (104 U. S. 271). This has not been considered by the advisory committee. Speaking solely for myself, I believe that this is a fair provision for national banks if my understanding of its purpose is correct. For example, in my home State the supreme court of Missouri has held that where paper is purchased from the payee or other holder at a discount, usury is not present whatever amount the purchaser pays, as it is a purchase and not a loan even though the holder endorses with recourse. In any event, I suggest that the language should be improved upon to make clear just what the purpose is.

I do have some implementing language in this case, and I will offer it for the record.

Senator ROBERTSON. Without objection, it will be received.

(The document referred to follows:)

Page 27 of bill, strike the last sentence in section 35 (a) and substitute the following:

"The purchase of obligations or evidences of indebtedness from the actual owner thereof shall not, for the purposes of this section, be deemed a loan or discount if such purchase would not, under the law of the State in which the purchasing bank is located, be deemed a loan or extension of credit subject to the interest or usury statutes of such State."

Mr. CRAVENS. In recommendation 44 the Comptroller suggested the need for a statute providing that reports of examinations of national banks, and so forth, shall be deemed confidential and privileged against disclosure to unauthorized persons except with the consent of the Comptroller. Recommendation 115E of the Federal Deposit Insurance Corporation was comparable. Both were approved by our committee. Section 50 at page 41 of the bill implements the former and section 10 at page 153 of the bill the latter.

I think a comparable provision should be inserted for the Federal Reserve Board.

I mention these sections at this point because each adds a "Provided, however," clause to the effect that the privileged documents shall be made available to the committees of the Congress upon request. The advisory committee report at page 30 states that our committee by its approval did not intend to take a position for or against disclosure by the executive branch to the legislative branch.

You see, we are diplomatic at times.

Senator ROBERTSON. You remember Senator Douglas expressed very definite views at our previous hearing on this subject.

Mr. CRAVENS. Could I urge you, Mr. Chairman, if you do retain that provision, that you limit it to executive sessions? Is that not proper?

Senator ROBERTSON. It would be well worth considering.

Mr. CRAVENS. At page 183 of the bill section 4 (d) of title IV makes it unlawful for any uninsured member of the Federal home loan bank to advertise or represent that it is connected with the Home Loan Bank System except as may be authorized by regulation. While the advisory committee made no formal recommendation as to this, it was discussed informally and I feel certain that I properly sense the feeling of our committee when I express approval of its having been inserted in the committee print bill.

Would you say that is correct, Mr. Bubb?

Mr. BUBB. Yes.

Mr. CRAVENS. In my discussion of recommendation 155B I alluded briefly to the criminal provisions which appear at pages 248 and 249 of the bill. As I have stated, these are new provisions which were not considered by the advisory committee; thus my remarks represent only my personal views. It seems to me that these provisions at pages 248 and 249 as they relate to employees of the supervisory agencies becoming employees of any institution which they may have examined is much too broach, as I have already stated, and if enacted will produce results of as serious a nature as are the results which the provisions were designed to prevent occurring.

One of the big problems of banking today is the matter of obtaining qualified personnel. Without elaborating on the basic proposition, I want to say that the provisions of the bill I am referring to will for all practical purposes cut off one of the best sources of supply of qualified personnel for the banking system, namely, the employees of the supervisory agencies. This of itself is not in the public interest, because for each instance which these provisions are designed to prevent occurring there are dozen of instances of honorable relationships which have arisen between banking institutions and former employees of the supervisory agencies. A great many leaders in banking today are products of the examining agencies.

There is another harmful aspect which I think merits your consideration. Means should be found and employed to strengthen the quality of bank supervision, not weaken it. I feel that these provisions will inevitably make it more difficult for the agencies themselves to obtain the services of younger qualified personnel and conceivably can result in the rapid decimation of their present complements.

I therefore earnestly suggest that your committee find some way of achieving the purpose you have in mind without exposing both the banking system and its supervisors to the hazards I have mentioned.

I have not said enough about it actually. We suggested in recommendation 166 I that section 217 be made applicable to all members of the Federal Home Loan Bank System. We did not, however, recommend that it be extended to cover the stockholders owning 10 percent or more of the stock. Then we take particular exception to subsection (ii) because it refers to employment, which I have already commented upon, and because it has been extended to all officers and all employees, which goes way beyond the present Criminal Code.

Third, that while it undoubtedly was poorly expressed, all we meant to suggest by recommendation 166 I was that the rules applicable in the case of all banks should be made applicable in the case of all savings and loan, including—including now the relaxation of the rules as we recommend by our recommendation 115.

In summary, sections 217 and 218 of the Criminal Code as set out in the committee print do not reflect our committee's recommendation. Those sections have no place in the bill and ought to be eliminated.

You asked me a little earlier if I had any specific recommendations. I do.

First I would recommend that you eliminate all reference to employment in sections 217 and 218. All references. I have heard that the supervisory agencies are anxious to amend the committee print bill to provide a 2-year limitation of the agencies over people employed. I think the bill is perfectly adequate as it now stands, that they may so regulate under the bill, but if they wish that 2-year limitation as something to hang their hat on, I would certainly have no objection to it.

Now as to lending.

Senator ROBERTSON. Let me see if I am clear on this. If we eliminate those two sections, do you feel there would still be left in the bill sufficient language to prevent a repetition of the Elmwood Bank case, where, as you remember from our previous hearings in Chicago, Senator Fulbright did not like what happened, and Senator Douglas was very critical about what happened?

Mr. CRAVENS. If you eliminate all reference to employment you still retain the other provisions in section 217 and section 218. If you do not broaden it and go beyond examiners and assistant examiners, you might miss the General Counsel of the Federal Deposit Insurance Corporation, for example, or a few people like that. But the minute you try to broaden it you get it into—you create injustices all the way across the line.

I think with the changes I have suggested you would still have adequate power to cover the Elmwood situation, or almost any situation except one like I just happened to mention. That probably would not be covered, would it, Mr. Rogers?

Mr. ROGERS. No.

Senator ROBERTSON. I understand you take out these two sections, but you do have some language to put in?

Mr. CRAVENS. Yes. I still have some more recommendations.

Senator ROBERTSON. Our counsel, Mr. Rogers.

Mr. ROGERS. To clarify it, would the provision we have under each title applying to each agency and their employees in the front part of the bill, be adequate to cover the situation?

Mr. CRAVENS. Completely adequate.

Mr. ROGERS. So your recommendation would be to eliminate refer ences to employment in sections 217 and 218 of the Criminal Code and let the other provisions stand as they are, except that you would go along with a 2-year limitation on the previous section?

Mr. CRAVENS. That is right. With one more suggestion.

Mr. ROGERS. All right.

Mr. CRAVENS. And that is that you do not change the present language in the Criminal Code with respect to the coverage. In other

84444—57—pt. 2——4

words, do not use this new language going all the way down to employees, but limit it to examining personnel.

Mr. ROGERS. As I understand you, when you eliminate any reference to employment that would take care of that situation?

Mr. CRAVENS. Yes; but I want to talk a little bit on the lending now. We intended in our recommendation 166 I, of course, to broaden the scope of the prohibition on lending, but we did not intend to broaden the applications clear down to the office boy. The way it is now written no one could borrow any money from anyone, because you covered every lending agency and every employee of anybody in the supervisory staff, and you covered it both as to State and National banks, insured and noninsured. So I would suggest you strike that part of it. Keep the lending prohibition, but limit it to examiners and assistant examiners. Put in all you want about gifts and gratuities. That is fine. Tie it down as tight as you want to. But leave the lending prohibition limited at least to assistant examiners and examiners.

I have one other suggestion with respect to section (d) (2) of section 610. I think that entire section should be eliminated.

Mr. ROGERS. That relates to political contributions?

Mr. CRAVENS. That is right.

Mr. ROGERS. Would you like to explain that?

Mr. CRAVENS. Under section (d) (2), as I understand it—I may misinterpret it, but as I understand it, under section (d) (2) at the last general election I could not have made a contribution personally to President Eisenhower's campaign, or to anyone else's campaign, simply because at that same time in Missouri there was being elected a State treasurer. Have I interpreted that properly, Mr. Rogers?

Mr. ROGERS. I think it could be interpreted that way. Yes.

Mr. CRAVENS. If that be true, is it not grossly unfair to me as a banker not to let me exercise my constitutional rights? You would be in the same category, Mr. Bubb, and everyone here who is connected with the leading business would

Senator ROBERTSON. Let us get this situation a little clearer. State what the present law is with reference to bank making contributions.

Mr. CRAVENS. Well, national bank corporations are prohibited by Federal law from making contributions in the case of Federal elections, and State member banks are prohibited certainly in Missouri by Missouri law. I would like to ask Mr. Neill, counsel for this Advisory Committee if that is not a correct statement.

Mr. NEILL. It is. Section 610 of the Criminal Code relates to national banks. The present Federal Criminal Codes does not apply to State-chartered banks. They are covered by the laws of the States of their incorporation.

Mr. CRAVENS. I would not object to section (d) (1), Mr. Chairman. That would go a long way toward tightening up the situation, but section (d) (2) is just grossly unfair.

Senator ROBERTSON. Thank you. I think you have explained that.

Senator BRICKER. Are not all corporations in most States prohibited from making political contributions?

Mr. CRAVENS. That is my understanding.

Senator ROBERTSON. But you do not want it to apply to a banker just because he is a banker.

Mr. CRAVENS. That is right.

Senator ROBERTSON. When the president of any other corporation can contribute whatever the law permits anybody to contribute.

Mr. CRAVENS. Any more than I would want the members of a labor union to be denied their constitutional right.

Anyhow, prior to concluding, I will mention two recommendations which were made by the Advisory Committee which have not been implemented by the committee print—and properly so—but which our committee hopes that your committee—the Senate Banking and Currency Committee—will pass along with your favorable recommendation for action by the appropriate committees of Congress.

First there is the matter of postal savings. Our committee believes that following the recommendations of the Comptroller General and the Hoover Commission, the Postal Savings System should be liquidated in an orderly fashion forthwith. It has outlived its original purpose and private enterprise provides adequate facilities for the savings of our people.

Second, all banks, State-chartered as well as national, should by law be permitted to establish adequate and realistic bad debt reserves under statutory formula.

Reserves permitted by present Treasury regulations are inadequate on the basis of past experience and penalize prudent management. This inadequacy is even more pronounced if the banking system is to meet the huge and increasing demands for credit in a dynamic economy and protect the depositors. Our present economy requires the extension of many types of credit never before provided primarily by the banking system. As a result, the banking system must provide enormous amounts of consumer, mortgage, capital, and term credit, which types of credit carry risks not present in banking in the historical sense.

Accordingly, a new concept of the adequacy of reserves for losses for eligible loans outstanding in the banking system must be forthcoming. Consideration of the risks and the inadequacy of capital in the banking system forcibly demonstrates that any reserves less than 5 percent of eligible loans outstanding is wholly inadequate and unrealistic. The banking system should therefore be permitted to accumulate reserves in excess of this amount.

Thus, the Advisory Committee recommends that commercial banks be permitted under the Internal Revenue Code to add to reserves for bad debts in any taxable year up to a percentage of not less than one-half of 1 percent and not more than 1 percent of eligible loans, provided that no addition under the formula to such reserves in any taxable year shall cause the aggregate thereof to exceed a percentage of not less than 5 percent and not more than 10 percent of the eligible loans.

So again I urge your committee favorably to recommend this recommendation to the appropriate committees.

Senator ROBERTSON. The chairman wishes to comment that he has officially transmitted to the chairman of the Ways and Means Committee of the House of Representatives and the chairman of the Finance Committee of the Senate that recommendation since it was outside of the jurisdiction of the Banking and Currency Committee. The chairman of the House Tax Committee, where the bill must originate, has acknowledged receipt of the recommendation and has promised to bring it to the attention of his committee. He also said that if, as and when the full Banking and Currency Committee endorsed this type of provision we should please advise him.

I have asked Chairman Fulbright of the full committee to bring it to the attention of the Banking and Currency Committee at its first regular meeting because I felt sure that the Banking and Currency Committee would gladly endorse this tax provision.

Personally, I think it is only fair and it will help in some ways to equalize competition. I do not think it will cost the Treasury enough money to affect the balancing of the budget, for instance. In other words, I think it is a good recommendation and we are hoping that the tax committees of the House and Senate will so consider it.

Mr. CRAVENS. Thank you. I am delighted to hear that you are going to consider it. I would be remiss if I did not make one more comment before concluding, Mr. Chairman. There have been many kind remarks about the work of the 27-man committee, but I have heard none with respect to the outstanding job your counsel Mr. Donald Rogers and your staff have done in the preparation of this bill. It has been outstanding and I want the record to show that we think it is a tremendous job. We also want to record our appreciation for the cooperation which all of your staff has accorded us.

Now I would be glad to answer any questions, if you have them, with respect to this bill.

Senator ROBERTSON. I want to say you have given us a splendid analysis of what we are trying to do and what we have done up to this point. I think everybody interested in this legislation will appreciate the comments that you have made on what is in there and what was left out that you think should be in there.

Are there any questions?

Senator BRICKER. One question in connection with the tax situation in regard to bank management, and the new system of banking and the reserves that should be allowed. Would you explain a little more fully this statement:

> * * * the banking system must provide enormous amounts of consumer, mortgage, capital, and term credit, which types of credit carry risks not present in banking in the historical sense.

Which of those categories and in what way do they carry additional risks that are not present in the historical sense of banking?

Mr. CRAVENS. I will try to answer your question and then I would like to ask Mr. Everett Reese, or any of the other members of my committee, to add their comments.

What I meant by that statement—and I answer first because I wrote it—was that historically when the present laws were written banking generally was confined to short-term credit—90-day credit. That was about the only type of loans the banks made.

Our economy has changed and we have expanded our industrial capacity to such lengths that we have had to provide funds for every kind of purpose. For example, we are called upon to finance the purchases of the consumers up to 3 to 5 years for automobiles and everything known to man, on the time-payment plan, which the banks never did in the twenties.

Business now borrows large sums of its capital from the banks on a term basis of 5, 10, and 15 years—partly due to our tax laws. They can deduct the interest as an expense, but if they sell stock they cannot deduct it at the same time.

All the way down the line we have banks entering into very hazardous lending which was not conceived when these tax laws were written. I say if we want the banking system to continue to provide the credit that our economy needs then the Congress should provide some means to build a reserve to protect them.

I think it is important that the credit do be provided and I want the banks to have the courage to lend. If we give them adequate reserves they will have the courage to lend.

Senator BRICKER. Assuming it is desirable to continue that type of credit—and I so believe—has experience demonstrated that there is greater risk in the new types of credit—the consumer, mortgage, capital, and term credit—than in the short-term credit formerly given to business?

Mr. CRAVENS. Most assuredly. Mr. Reese, would you like to comment on that?

Mr. REESE. The banks have been expanding their services to serve more people in more ways, which is a wonderful thing for all of the people of the country.

Senator BRICKER. I know that, and I am for it.

Mr. REESE. And so there have been new ways of lending to people to take care of their credit needs, and extending the time. Whenever you project anything into the future there is more risk involved in it. On the other hand we have been doing these things in a time of great prosperity, for the last 20 years. We do not know what the experience will be.

Senator BRICKER. That is why I asked you if your experience justified it.

Mr. REESE. Up to date there have been practically no losses in the banking business during that period of time. Maybe we are so good and so right that there will not be any losses, but at the same time we do not know, because we have been operating in this period of high prosperity.

Mr. CRAVENS. May I interrupt? In your State of Ohio, Mr. Reese and Senator Bricker, it just came to my attention that a certain manufacturing company has now gone into bankruptcy and a certain New York bank has a $1,750,000 loan to it that I doubt it will ever collect. It was a term loan. Sure we have losses and have them every day, and we know we are going to get more, particularly if we have a change a little excessive in our economic climate.

Senator BRICKER. Your experience then and your anticipation of losses are such as in your judgment to call for an increase in the reserves?

Mr. CRAVENS. Most decidedly.

Senator BRICKER. That was what I was getting at. I do not think the experience overall of the last 10 years, for instance, would show greater losses in these particular fields.

Mr. CRAVENS. That is correct.

Senator BRICKER. Greater than in the ordinary banking fields.

Mr. CRAVENS. I think that is correct.

Mr. REESE. If we had a proper system of reserves it would put the bankers in the frame of mind that they would adequately serve the credit needs as they develop and come along. In the field of small business we would be sure the banker is going to serve those needs he has been, but he must be kept flexible enough and have the confidence to go ahead in serving the credit needs of the people with real vision.

Senator BRICKER. I think that is right.

Senator ROBERTSON. Any further questions? Does any member of Mr. Craven's staff or the subcommittee chairmen wish to make any statements?

Mr. HARRIS. Thank you, Senator. I would like to emphasize too the points which the chairman made so adequately on the matter of absorption of exchange. I have, and the members of the committee, all had many letters from bankers protesting this situation. I think it is significant that we have had none supporting it.

On the matter of Federal Deposit Insurance Corporation assessments——

Senator BRICKER. None supporting the change?

Mr. HARRIS. None supporting the present situation which results in the discrimination. All letters have urged that the change which the Advisory Committee recommended be made in order to remove the discrimination which presently exists.

Senator BRICKER. I see.

Mr. HARRIS. On the matter of Federal Deposit Insurance Corporation assessments, it may be thought to be a difficult task to determine a reasonable basis for computing this assessment, but I would like to point out recently the private insurance industry undertook a $50 million risk in the operation of atomic-power plants where they have absolutely no past experience to proceed on. This organization has had 25 years almost, and it ought to be able to do something.

Senator ROBERTSON. Mr. Pratt.

Mr. PRATT. I have no further material comments to make to Mr. Cravens' comments. I think we have here gone into the bill. There are however a few minor changes in wording that the Bureau of Federal Credit Unions will convey to your committee on the section on expenses for the credit committee and dividends.

I would like to support the views expressed by Mr. Cravens.

Senator ROBERTSON. You remember King Solomon said in Ecclesiastes, "In that war there is no discharge." He dratfed men for war and they had to serve a reasonable length of time and then he let them go. He drafted men to build his temple and let them go. But when he referred to the war of life he said, "In that war there is no discharge." You are in for the duration and can only get out when you die.

So, I do not think I shall let this fine advisory committee go. I want you to keep in touch with the hearings. You know our plan. After we hear all of the private agencies and the individuals we shall try to wrap it up with the wisdom of the Federal agencies.

Then I want you gentlemen to take another look at it and we will sit down and let our hair down, as Fred Vinson used to say, and see what goes into the final bill.

Mr. PRATT. Thank you. Just one comment in connection with sections 217 and 218. Even if it were advisable to set up some limitation on these loans we felt this went so far in that capacity that no Federal employee in any one of these institutions could even belong to and borrow from a credit union organized in his own group. It went so far, in addition to employment, that I think it should be, as Mr.

Cravens said, removed. And the other section in the Federal part, regulating employment, is adequate.

Senator ROBERTSON. Any further comment?

Mr. BUBB. I would like to add this, Senator Robertson and Senator Bricker. I want to second what Mr. Cravens had to say about your work and that of the other Senators on this committee and particularly the capable contribution of your staff and general counsel. We too are most appreciative of that.

Another thing I think has some out of this. Sometimes competing businesses seem to have some differences and when they are aired, if they could sit down around a table like we have done in this group, the difficulties would fade away in the twilight. If there is anything this group has done it has shown the public at last that the savings-and-loan business and the banking business can sit down and work out their problems in peace and harmony.

I think if for no other reason, in being on the Cravens committee and in meeting with the men I have met with such as Ev Reese, and Reese Harris and Bill Pratt and John McCloy and others, particularly on our executive committee, we ironed out many problems that could not have been handled otherwise. There are a few minor things I wish to address myself to but I understand I am to testify Thursday morning and I do not want to take up your time twice on them.

Senator ROBERTSON. I understand we will have the pleasure of seeing you on Thursday.

Mr. BUBB. Yes.

Senator ROBERTSON. And we will look forward to it.

Mr. BUBB. I am not in disagreement except on minor language changes on some of the matters where lawyers enter into it. I will take up different matters then. However, as long as this is part of the advisory committee and Mr. Cravens referred to section 5 (d) (2) on page 206 of the act, I would like to say something on that. We agreed on the committee that the Board—which means the Federal Home Loan Bank Board—should not proceed under paragraph 2 if they could proceed under paragraph 1, and that was left out of the print. It sounds minor but frankly it is not minor.

Also, under subsection 3 of that same part where we use the words "after having been warned" in the desist clause, we feel that should be "warned in writing." That sounds technical but I believe it is not and it would be a good thing for both parties just to add that. Do you agree with me on that?

Mr. CRAVENS. Yes; I do.

Mr. BUBB. Those are the only subjects I want to bring up today. I want to tell you again, Ken Cravens, and you and your staff, we appreciate very much having had this opportunity.

Senator ROBERTSON. Mr. Reese has been very helpful in the preliminary studies and in the questions he asked in the November hearings. Did you have any comment to make this morning?

Mr. REESE. Thank you, Senator Robertson. I think Mr. Cravens so adequately and so well covered this that there is nothing I could add. I want to thank you for the privilege of serving on this group, and I hope it will make a fine contribution to the future of banking. I certainly appreciate the fine cooperation between the savings and loan and the banks and credit unions and other agencies involved.

(Mr. Cravens' prepared statement follows:)

STATEMENT OF KENTON R. CRAVENS, CHAIRMAN OF THE ADVISORY COMMITTEE FOR THE STUDY OF FEDERAL STATUTES CONCERNING FINANCIAL INSTITUTIONS AND CREDIT

Mr. Chairman and members of the committee, I appear before you in my capacity as chairman of your advisory committee to testify in regard to the committee print bill known as the Financial Institutions Act of 1957. Seated with me are the following chairmen of subcommittees of the advisory committee: Mr. Everett D. Reese, of the Subcommittee on National Banks; Mr. Reese H. Harris, Jr., of the Subcommittee on Federal Deposit Insurance Corporation; Mr. Henry A. Bubb, of the Subcommittee on Savings and Loan Associations; Mr. William W. Pratt, of the Subcommittee on Federal Credit Unions.

Unfortunately, neither Mr. C. Francis Cocke, vice chairman of the Advisory Committee; nor Mr. John J. McCloy, Chairman of the Subcommittee on the Federal Reserve Act, is able to be in attendance today.

On behalf of each of the members of the advisory committee, I desire to thank the Senate Banking and Currency Committee for the unique opportunity which has been accorded us to serve in this important undertaking. Each of our members, our secretary, Mr. James Saxon, and our counsel, Robert Neill, has given freely of his time and energies in the pursuit of our duties. I trust that our report adequately reflects the unselfish, conscientious, and objective manner in which they approached the many problems which they considered. As indicated in my letter of transmittal, our committee unanimously agreed to our report except as to three recommendations noted therein.

For the convenience of your committee I believe that it would be better if my testimony were to follow the bill page by page. Even so, my testimony will be broken up into five parts as follows:

Part I: Instances where recommendations of the advisory committee have been followed in matters of more or less technical nature. Unless questions arise, I will not discuss these but will place in the record a list of such recommendations by their numbers and will follow them by reference to the pages of the bill at which they have been implemented. Needless to say our committee was pleased to see that they were adopted.

Part II: Instances where recommendations of the advisory committee have been followed on matters which I believe warrant discussion in some detail.

Part III: Instances where the committee print does not follow recommendations of the advisory committee. These I will discuss separately.

Part IV: Instances where the bill includes matters which are new in that the Advisory Committee has not considered them. As to these I am not in position to speak for the Advisory Committee. Thus I would like to have the benefit of testimony of others, then give the Advisory Committee an opportunity to consider these new matters and thereafter, if such be your pleasure, appear before you again and at that time report the Advisory Committee's views on these new matters and discuss any other points which may have been raised by the intervening testimony.

Part V: Lastly, I will mention the instances where recommendations made by the Advisory Committee have not been incorporated in the bill, we assume because jurisdiction over them lies elsewhere.

Following this outline, I offer for the record schedule 1 to be attached to my testimony. This schedule lists the recommendations which fall in the first category.

In the second category I refer particularly to the following recommendations which have been incorporaed in the bill and in the order in which they appear in the committee print.

Recommendation 2—Appointment of 2 additional deputy comptrollers

The bill at page 2, section 5, provides for an increase in the number of Deputy Comptrollers from 3 to 5. In the light of the testimony which Comptroller Gidney gave before this committee on November 9, 1956, the Advisory Committee favors this change in the law.

Recommendation 45E—Employee stock options; recommendation 45D—Issuance of preferred stock or debt obligations by banks

I have purposely put these recommendations together because they go a long way in answering the urgent need of banking; namely, the need for better management and more capital funds. On pages 8 and 18 and on 9 and 10 of the bill will be found language implementing recommendations 45 E and 45D, respectively. I refer to sections 8 and 31 (a) (9) and 20 and 21 respectively.

Frankly, banks are at a serious disadvantage competing for qualified executive personnel because they are not permitted to use the strong inducement provided by employee stock option plans. This situation must be remedied if we are to improve the caliber of management in the Nation's banking system. At present there is no statutory authority by which national banks are permitted to establish such programs.

Equally important as good management is adequate capital. Since under the present law a national bank may issue preferred stock only as an emergency measure the statutes are meaningless. Furthermore, under present law a national bank cannot issue debt obligations as a means of acquiring additional capital. Therefore, limiting national banks' access to capital by way of common stock only is unrealistic and a great deterrent to the banking system's efforts to raise the capital funds it needs. Preferred stock or subordinated debentures issues might well offer a better and more feasible means of acquiring additional capital. Then too, the redemption features of such securities provide a flexible means of adjusting the requirements of the banks to the needs of the times. If the Nation's banking systems are going to supply the needs of our present dynamic and full economy, the national banking system must provide leadership on these constructive measures.

Recommendation 13—Unearned dividends

At page 11 of the bill, section 22 implements this recommendation. The present law is changed to authorize quarterly declaration of dividends as well as semiannual and annual declarations. Section 22 (b) provides that the approval of the Comptroller of the Currency shall be required if the total of all dividends declared in any calendar year exceeds the net profits of that year combined with its retained net profits of the preceding 2 years less any required transfers to surplus. As the Advisory Committee stated in its report, it believes that these changes are constructive.

Recommendation 17—Shareholders' lists

At page 12 of the bill, 12 United States Code, section 62 is revised based on this recommendation. The bill, however, does not follow the recommendation of the Comptroller which the Advisory Committee approved, but continues the present law to the effect that the statutory right of inspection by a shareholder of a national bank is not qualified by a requirement of showing proper purpose. The committee fails to understand the necessity for granting to a shareholder of a national bank a broader right of access to a stockholder's list than is enjoyed by shareholders of corporations generally. Thus section 23 (a) of the bill and the corresponding sections which I will mention should be amended to conform to the Advisory Committee's recommendation.

It should be noted that the substance of section 23 (a) is repeated at page 94 of the bill as section 23 (i) relating to state member banks of the Federal Reserve System and at page 164 as section 27 of the Federal Deposit Insurance Act. While no recommendations were made as to this, either by the supervisory agencies or by the Advisory Committee, these sections have been inserted apparently on the basis of uniformity. For the moment I merely note their presence.

Further at page 12, section 23 (b) requires that a national bank shall notify the Comptroller immediately of any single transaction involving "the purchase for sale of 10 percentum or more of the outstanding shares" of the association. This language is repeated as to State member banks at page 94 and as to insured banks at page 164. This is an entirely new provision. While we take no particular exception to the principle of reporting stock transfers, we question the language which has been used as it leaves the situation in a twilight zone. If the idea is adopted it should be limited to a transaction as reflected by the stock transfer records of the particular banking institution.

Recommendation 15—Cumulative voting in election of directors

At page 13 of the bill section 26 (c) implements this recommendation. This language is identical, to S. 256 which passed the Senate of the 84th Congress and was reported favorably by the House Banking and Currency Committee.

While undoubtedly sound in theory, mandatory cumulative voting in practice works to the detriment of good bank management. The responsibilities of the members of the boards of directors of banks are such that any serious discord or friction might shake the confidence of its stockholders or depositors as well as the public. This is particularly true in small communities. There have been situations where a minor stockholder, elected a director, has conducted himself in a manner which obstructed the orderly conduct of the business of the board of directors or which resulted in divulging to outsiders confidential information about the business of the bank, its borrowing customers, and its depositors.

Therefore, the committee believes that a permissive provision as provided by the committee print is more preferable to the existing mandatory provision.

Recommendation 21—Removed officer or director prohibited from voting stock

At page 15 of the bill section 29 revises 12 United States Code section 77 as it relates to the removal of officers or directors of national banks. The bill includes a comparable provision relating to officers and directors of State member banks at page 101 and further at page 207 includes a comparable provision relating to officers and directors of Federal savings and loan associations. See section 29 at page 101 and section 5 (d) (3) at page 207. (The material found at p. 207 of the bill implements recommendation No. 144.)

All of this material is new and was not the subject of any recommendation. I feel, however, that the changes which have been made do meet with the approval of the advisory committee. I note particularly the fact that the procedures are tied in with the Administrative Procedures Act and that the review by the courts shall be upon the weight of the evidence. This is a very sound change.

Recommendation 6—Contributions by the national banks

At page 18 of the bill, section 31 (a) (8) implements this recommendation by authorizing national banks to make contributions irrespective of State law to nonprofit educational institutions and to "nonprofit" civic organizations. In his original recommendation the Comptroller did not recommend the use of the word "nonprofit" in the case of civic organizations. The advisory committee approved of the Comptroller's recommendation. Now the bill limits the contributions to "nonprofit" civic organizations. Speaking personally, I feel that it would be better if the word were not used in the bill in this instance as the purpose is the controlling factor and is well defined.

Recommendation 60—Stock acquisitions in connection with absorptions

At pages 20 and 93 of the bill section 32 (b) relating to national banks and section 23 (d) relating to State member banks implement this recommendation. While both the board of governors and the advisory committee suggested that permission might be granted to "purchase and hold temporarily" stock of another bank, the bill discards the word "temporarily" and fixes the period of holding at a maximum of 90 days. We concede that "temporarily" is not as definite as is 90 days, but we wonder if there is real need of being so definite here where the approval of the appropriate supervisory authority has to be obtained in advance. In some instances 60 days' notice must be given for stockholders' meetings. Thus 90 days may be too limited a period. It would seem that a period of 6 months would not be excessive in this situation.

Recommendation 34—Trust powers

The Comptroller recommended that the authority to license and regulate the exercise of trust powers by national banks historically reposing in the Board of Governors of the Federal Reserve be transferred to him. At page 20 of the bill section 33 implements this recommendation which was approved by the advisory committee. At the earlier hearings Governor Robertson interposed no objection to this action but suggested that if it be adopted that the Board's regulatory authority over common trust funds likewise be transferred to the Comptroller. The bill does not make this additional change and the advisory committee agrees that it should not be made. (See note at bottom of page 9 of the advisory committee report.)

Recommendation 24—Exception to 10 percent loan limit on obligations concerning dairy cattle

At page 25 of the bill section 34 (b) (7) (B) implements this recommendation so that the loan limit with respect to obligations arising out of the sale of dairy cattle is increased to 25 percent with the result that the same limitations as are applicable to livestock will be applicable to dairy cattle. The advisory committee saw no reason for the existing difference.

Recommendation 23 (1)—Exception to 10 percent loan limit on obligations concerning insurable perishable readily marketable staples under refrigeration

At page 25 of the bill section 34 (b) (6) (B) implements this recommendation and increases to 25 percent of capital and surplus the applicable loan limit as relates to such staples except where the obligations are "secured by the identical staples for more than 6 months." As a practical matter we can see trouble ahead through the use of the word "identical." Doesn't the language mean that the 6-month period can be increased by the bank obtaining substitution of collateral in a minimum percentage?

While I have not checked every page of the bill, I think I am correct when I say that only on page 25 of the bill will be found the phrase "and/or." With due respect to the draftsmen, I wonder if this phrase cannot and should not be eliminated, not only in section 34 (b) (6) (B), but also in the next to last line of the preceding paragraph, where it appears as part of present law? In any event I suggest that this language be checked.

Recommendation 23 (2)—Loan limit on installment consumer paper

At page 27 of the bill section 34 (b) (12) implements the recommendation which the advisory committee made on this subject. Here the recommendation of the Comptroller has been supplemented by a proviso to the effect that the 10 percent limitation (as regards the maker) shall apply rather than the 25 percent limitation (as regards the endorser) where, after evaluation of the responsibility of each maker has been made, an officer of the bank, designated for such purpose by its board of directors, certifies that in acquiring such paper from the particular seller the acquiring bank is relying primarily upon the obligations of the makers for payment of the paper. Certainly there is no valid reason to distinguish between nonnegotiable paper and negotiable paper with respect to loan limitations, and this provision cures this. If the acquiring bank is relying primarily upon the responsibility of the endorser or guarantor, then a reasonable limitation should apply, but when the acquiring bank is looking to the maker, the transaction should be looked upon as a loan to the maker rather than a loan to the endorser.

This is an important and much needed revision in the national bank act.

Note lastly that the word "appreciable" in the third to last line should be "applicable."

Recommendation 35—Limitation on real-estate loans

This recommendation was divided into four parts plus an additional recommendation of the advisory committee. Each has been followed in the bill, viz:

Recommendation 35 (2) is implemented at page 28 by section 36 (a), which section at page 29 also incorporates the committee's additional suggestion. Recommendation 35 (2) would permit national banks to make loans on leaseholds having at least 10 years to run beyond the maturity of the loan. At page 29 of the maximum aggregate of real-estate loans which may be made by a national bank is limited by a third alternative, i. e., 20 percent of demand deposits. The advisory committee favors these additions to the statute.

Recommendation 35 (1).—This is implemented in accordance with the advisory committee's recommendation by section 36 (c) which appears at page 30 of the bill.

Recommendation 35 (4).—At page 30 of the bill section 36 (e) implements this recommendation.

This recommendation would permit national banks to make loans to manufacturing and industrial businesses which are secured by liens on the plant real estate where the loans are for the purpose of furnishing working capital, without such loans being considered as real-estate loans. These loans are really business loans and represent ordinary business financing and should not be treated as real-estate loans subject to the provisions of the law relating to real-estate loans of national banks. To meet industrial needs national banks are making such loans today, but are forced to make them on an unsecured basis. While the bank may expect repayment of such loans through liquidation of inventory or receivables, or through the operations and earnings expected to be derived from the additional facilities so financed, nevertheless, they should not be denied the benefit of the additional collateral which could be provided by mortgage on the company's plant real estate taken as precaution against contingencies.

Recommendation 35 (3).—This is implemented by section 36f at page 31 of the bill where it is provided that national banks may make loans to finance construction of buildings upon the security of purchase contracts entered into under the Public Buildings Purchase Contract Act of 1954 and the Post Office Department Property Act of 1954 without regard to the limitations in regard to real-estate loans.

With the foregoing changes made in the real-estate loan section of the National Bank Act, such will represent a vast improvement over present law.

Recommendation 45B—Increase in debt limit of a national bank

This and recommendation 22 have been implemented at page 31 of the bill by section 37 which revises title 12, United States Code, section 82 to increase the debt limit of a national bank from 100 percent of its capital to 100 percent of capital and surplus and renders the section inapplicable to capital funds obtained through the issuance of capital notes or debentures outstanding under section 21 set forth on page 10 of the bill. The advisory committee believes that these are constructive changes in the law.

Recommendation 9—Branches retained after merger, etc.

At page 32 of the bill section 39 (b) implements this recommendation as to which the advisory committee in its report stated at page 3 thus:

"This recommendation would permit a national bank continuing on merger or consolidation with another bank under a resultant national bank charter to operate the branches the national bank theretofore lawfully operated without obtaining new approval from the Comptroller. The committee understands the proposition to be one of merely eliminating unnecessary paperwork in such cases as compared with broadening the power of national banks to have and operate branches. On the basis of such understanding being correct, this recommendation is approved."

It seems to us that the implementing language goes no further than our understanding.

Recommendations 11 and 115C—School savings programs

At pages 34 and 149 of the bill section 39 (f) of the National Bank Act and section 2 (m) of the Federal Deposit Insurance Act define "branches" so as not to include school-savings programs. The advisory committee approved of these changes and is glad to note that such programs are confined to schools "located in the trade area of the bank and within the State in which the bank is situated."

Recommendation 45C—Loans and investment on bank buildings

Heretofore both National and State member banks have been limited to 100 percent of their capital as regards the amount they may have invested in bank premises or in an affiliate holding the bank premises. At pages 35 and 94 of the bill section 43 and section 23 (j) change the maximum to 100 percent of capital or 50 percent of combined capital and surplus whichever is greater. The purpose of the change is to give relief to the bank which has a large surplus and a small capital. In giving this relief, however, the bank which has made its future projections based on a larger capital and a lesser surplus should not be prejudiced. Thus the advisory committee favors these provisions.

Recommendation 36—Deposits in corporations not supervised by any State banking authority

Here the advisory committee approved a recommendation which the Comptroller made in regard to amending 12 United States Code section 378 so as to require that a corporation receiving deposits shall be subject to examination under the banking laws. This recommendation has been implemented at page 36 by section 44 (a) (2) (A) wherein new language appears. It appears to us that the new language of the bill does not go as far as the Comptroller suggested that the change go. If the Comptroller believes that the new language is adequate, we would suggest no change in the committee print.

Recommendation 45F—National banks writing insurance

At page 37 of the bill section 45 implements this recommendation which is that 12 United States Code section 92 be revised so as to permit national banks located in towns of 5,000 or more to write insurance if State banks in such towns are permitted to do so by State law.

Section 45 includes paragraph (b) which is new and was not the subject of a specific recommendation; and paragraph (c) includes a grandfather clause. Both of these additions were considered and are within the area of the recommendation. The purpose of these changes is to place national banks on a parity with State banks in these particulars.

Recommendation 5—Restrict State authorities from subjecting national banks to licensing, etc.

At page 41 of the bill section 51 implements this recommendation to the end that whatever doubt has existed as to the right of a national bank to exercise its corporate powers without State or local interference is resolved. The advisory committee favors the inclusion of this new provision in the statutes.

Recommendation 28—Reports to comptroller

At page 42 of the bill section 52 (c) implements the recommendation, in principle, of our committee. Our recommendation, based on that of the comptroller's, was to change from 5 to 10 days the time within which national banks must transmit required call reports to the Comptroller, as provided for in S. 2996 introduced by Senator Robertson in the 84th Congress.

Recommendation 58—Reports from member banks

At pages 42 and 92 of the bill will be found language which implements this recommendation of the Board of Governors which was disapproved by the committee as to the authority of the Board of Governors to prescribe different forms of reports of condition, earnings, and dividends; and to require such reports on a sample basis. In addition, the bill follows the recommendations of the advisory committee with respect to publication of earnings, expenses, and dividends, namely, that the Board should not be so authorized and accordingly the bill does not give the Board this requested authority. If the Board of Governors wishes to propose a reasonable classification of banks according to size and to recommend that the group of smaller banks shall not be required to furnish more than two reports in any year, the advisory committee would concur in that recommendation provided that a reasonable limitation is placed on the number and kinds of reports which the group of larger banks may be required to furnish in each year. This applies with equal force to section 52 of title 2 of the committee print which gives similar authority to the Comptroller of the Currency. If adopted, the same reports should be authorized and required by the Federal Deposit Insurance Corporation.

In short, I think that the advisory committee is opposed to these provisions as now written at pages 42 and 92. I find the implementing language confusing. In short, I would say that the present authority be continued, or the bill be written with appropriate safeguard to the smaller banks as to a reasonable limitation on the number and kinds of reports which the larger banks may be required to furnish each year.

Recommendation 33—Appointment of conservators; recommendation 106—Liability of FDIC for insured deposits

By recommendation 33 the Comptroller urged that the Bank Conservation Act be amended to authorize him to appoint a conservator for a national bank which has sustained substantial losses resulting from defalcations. The advisory committee approved and the recommendation has been implemented by section 64 (j) at page 64 of the bill. We note that section 64 (d) at page 61 of the bill does not read the same as does section 205 of the Bank Conservation Act but understand that the reason therefor is the fact that the Federal Deposit Insurance Act has been changed to read as it does at page 168 of the bill where section 30 (c) implements recommendation 106, which was approved by the advisory committee. We believe that there still remains the problem of depositors whose deposits exceeds the insured amount and suggests that payments to them on their noninsured balances should be ratably as provided for other corporations. Thus the language of section 63 (d) should receive further consideration.

I will now mention some of the more important changes in the Federal Reserve Act.

Recommendation 54—Payment of Reserve bank earnings to the Treasury

In keeping with this recommendation of the Board of Governors which was approved by the advisory committee, the bill at page 73 in section 7 of the Federal Reserve title provides that each Federal Reserve bank shall annually pay 90 percent of its net earnings to the Treasury as a franchise tax. This is the simplest method of clarifying the situation and its effect is to restore the situation as it existed prior to 1933 and the creation of FDIC in that it channels 90 percent of the net earnings into the Treasury.

Recommendation 51—Federal Reserve bank directors residents of district

At page 86 of the bill, section 17 (a) implements both the recommendation of the Board of Governors and that of the advisory committee. This section of the bill provides that every Federal Reserve bank director shall be a resident of the district of the Federal Reserve bank on whose board he is serving, or shall reside within a 50-mile radius of such bank. Our committee preferred the pertinent qualifications for appointment to, and continuation on, the board of directors of a Federal Reserve bank, be based on the principal place of business of the person appointed, and not the place of residence. Nevertheless, the "within 50 mile radius" qualification satisfies our committee's recommendation and the requirements for some metropolitan districts.

Recommendation 81—Loans to executive officers

At page 99 of the bill, section 28 (e) implements the recommendation which was made in regard to the matter of member banks making loans to their executive officers. The committee print adopts the recommendation made by the Board of Governors and that of the advisory committee except in one particular. The advisory committee felt that the statute itself should define "executive officer" rather than leaving this to the Board to cover by regulation. In order to advise you of our position and with your permission I quote briefly from page 22 of the advisory committee report, viz:

"(*b*) The statute itself should define executive officers and as including only (i) the principal executive officers, (ii) the officers who are heads or acting heads of departments, divisions, or branches, and (iii) any officer who, under the operating procedures or rules of the particular bank, has individual authority to make loans in excess of $5,000.

"The Board of Governors, in regulation O has defined an executive officer to mean 'every officer of a member bank who participates in or has authority to participate in the operating management of the bank or any branch thereof otherwise than in the capacity of a director of the bank, regardless of whether he has an official title or whether his title contains a designation of assistant and regardless of whether he is serving without salary or other compensation' (sec. 1 (*b*), regulation O).

"Obviously this definition includes substantially every officer of a bank and many nonofficers whether or not such persons have any authority or function whatever in reference to the making of loans. The committee feels that the statute should contain the definition which it has suggested."

Recommendation 66—Simple majority for Board actions

The Board of Governors recommended that the act be amended to provide that Board action might be taken upon the affirmative vote of a majority of a quorum of members. The advisory committee disapproved of this and recommended that the statute provide that the Board should act in all matters upon the affirmative vote of not less than a majority of the members of the Board in office at the particular time. The committee print bill follows this recommendation to the extent of placing in the law at the various places where particular votes are specified a new provision that the vote shall be by the affirmative vote of a majority of the members of the Board in office. (See, for example, p. 114, sec. 39 (b), p. 115, sec. 39 (1).) We believe that section 38 (d) at page 112 of the bill should be amended to include a sentence providing that any action which the Board is authorized to take shall be taken by the affirmative vote of a majority of the members of the Board in office at the time. We suggest this particular place in the bill as it appears to us to be the logical place and it is the place at which the Board suggested that its recommendation be inserted, i. e., section 38 (d) is 12 United States Code, section 244.

Recommendation 85A—Audit of Federal Reserve Board; Recommendation 85B—Audit of Federal Reserve banks

At page 113, section 38 (h) implements recommendation 85A where it provides that accounts of the Board of Governors shall be audited at least once a year by certified public accountants. Further, at page 116, section 39 (m) provides that the Board shall have the adequacy of the procedures which it follows in examining the Federal Reserve banks reviewed by certified public accountants. These new provisions are based upon recommendations which the Board of Governors made and of which the advisory committee approves. They represent constructive legislation in the public interest.

Recommendation 83—Powers of foreign branches of national banks

This recommendation of the Board of Governors in which the advisory committee concurred was that the powers of foreign branches of national banks should be enlarged upon as set out in S. 3922 of Senator Robertson in the 84th Congress. At page 125 of the bill section 45 (f) implements this recommendation, we are happy to see.

Recommendation 85F—Repeal of section 13B of the Federal Reserve Act

The advisory committee recommended that section 13B of the Federal Reserve Act be repealed on the grounds that it has been little used and that the power is not compatible with central banking functions. We are pleased to see that this recommendation of the advisory committee has been adopted.

I now pass to title III of the bill which relates to the Federal Deposit Insurance Corporation.

Recommendation 115H—Change in organization of Federal Deposit Insurance Corporation

At pages 148, 151, 152 and 153, will be found language implementing recommendation 115H of the committee.

These provisions vest the management of the Corporation in a single executive and administrator to be appointed by the President by and with the advice and consent of the Senate, and would create an Advisory Board of the Federal Deposit Insurance Corporation consisting of the Comptroller of the Currency, Chairman of the Board of Governors of the Federal Reserve System or his designee, and one person to be selected by the President who is a State official exercising functions relating to the supervision of State banks. We believe that this provision is highly desirable to promote greater efficiency and better management.

The single executive would achieve better administration and such an Advisory Board would provide a means of assuring to the Administrator the benefits now derived from the presence of the Comptroller of the Currency, and add the benefits of Federal Reserve Board and State supervisory participation, all so necessary in a situation so complex as that presented by our present banking structure.

Recommendation 91—Insurance of interest on deposits

At page 149 of the bill section 2 (k) includes as an insured deposit "interest accrued to the date of the closing of the bank." This language implements recommendation 91 which was approved by the advisory committee and is a constructive change in the law.

Recommendation 92—Transferred deposit

At page 149 of the bill section 2 (l) restores to the law the express assurance that a transferred deposit means a demand deposit in a new bank or other insured bank. It properly implements the Federal Deposit Insurance Corporation recommendation which was approved by the advisory committee. It should be noted that a comparable change is made at page 223 of the bill pursuant to recommendation 166K of our committee.

Recommendation 97—Assessment credit

This recommendation in the form in which it was approved by the advisory committee has been implemented in section 18 at page 159 of the bill. Recommendation 97 (e) which was disapproved is not included in the bill. As section 18 is written it appears to reflect properly the thinking of our committee. Later I will comment on the failure of the bill at this point to implement recommendation 115G of the advisory committee.

Recommendations 42, 85 and 114—Regulation of mergers

Each of the supervisory agencies recommended that section 18 (c) of the Federal Deposit Insurance Act (12 U. S. C. sec. 1828c) be amended as it was sought to be amended by S. 3911 of the 84th Congress and the advisory committee approved. At page 162 of the bill section 23 implements these recommendations in the language of S. 3911 which was passed by the Senate. The committee feels that this is constructive legislation and urges that it be retained in the bill.

Recommendation 99—Procedure for termination of insured status

At page 165 of the bill section 29 implements the Federal Deposit Insurance Corporation's recommendation in this regard as it was approved by the advisory committee. In addition, however, section 29 provides that the hearing on termination shall be held in accordance with the provisions of the Administrative Procedure Act and that review by the courts shall be upon the weight of the evidence. This was added as it has been included in the statutes relating to the termination of insurance of accounts of Federal savings and loan associations. (See, for example, sec. 408 at p. 225 of the bill.) These provisions should in fairness be available to banks.

At page 168 of the bill section 30 (c) implements recommendation 106 to which reference has been made heretofore.

Recommendation 109 is implemented at page 171 of the bill by section 31 (e) which reads as was suggested at page 28 of the advisory committee report.

Recommendation 113 is implemented at page 177 of the bill where section 38 (a) changes the fiscal year of the Corporation to the calendar year and thereby makes it conform to the Corporation's system of accounting.

Recommendation 112—Civil service retirement

The advisory committee interposed no objection to this recommendation of Federal Deposit Insurance Corporation provided that the cost was charged to the capital account of Federal Deposit Insurance Corporation and not to "net assessment income." We are pleased to see that section 39 of the bill as it appears at page 179 specifically so provides.

Recommendation 115B—Authority to prescribe by regulation employments that may involve conflict of interest

The Federal Deposit Insurance Corporation recommended that it be authorized to make regulations governing the employment of its employees by insured banks in situations involving a possible conflict of interest. The advisory committee approved this recommendation, noting, however, that the Comptroller of the Currency through the years apparently has had no difficulty with this problem even though he has not had the benefit of a statute on the point.

At page 180 of the bill section 40 (d) implements this recommendation providing that it shall not be lawful for any employee or former employee of Federal Deposit Insurance Corporation to accept employment in any insured bank except pursuant to regulations prescribed by the Federal Deposit Insurance Corporation. The section further provides penalties upon conviction of any violation of the section. At page 3 of the bill will be found section 8 (b) which is a comparable provision relating to employees or former employees of the office of the Comptroller. Also at page 113, section 38 (i) contains a comparable provision with respect to employees or former employees of the Board of Governors or of any Federal Reserve bank. Likewise at page 200 section 19 (b) makes the same provision with respect to employees or former employees of the Federal home-loan bank and at page 240 section 21 (i) makes the same provision for any employees or former employees of the Bureau of Federal Credit Unions. We assume that these comparable provisions have been inserted as they have in order to achieve uniformity. We do not feel that any exception can be taken to this. We note, however, that at pages 248–249 of the bill, 18 United States Code section 217 is amended by adding thereto a provision which to me seems to be in direct conflict with the sections of the bill which I have referred to. As the advisory committee has not considered this new material. I am not in position to state its views. Speaking personally, however, I am constrained to think that the provisions at pages 248–249 of the bill are much too broad and should be removed from the bill. For the information of the committee, during the past few weeks I have had my attention directed to page 248 of the bill perhaps more than to any other of its provisions.

Recommendation 115F—Absorption of exchange as indirect payment of interest

The Board of Governors of the Federal Reserve System by their recommendation 77 suggested that the words "directly or indirectly by any device whatsoever" be removed from section 19 of the Federal Reserve Act and that it be made clear that the term "interest" should include only cash payments made or credits given by a bank for the account or benefit of a depositor and further that appropriate amendments be made to make certain that the same limitations as to the payment of interest should apply both to member and nonmember insured banks either by an explicit statement in the law as to both types of banks as to whether absorption of exchange charges shall be deemed a payment of interest or by a provision authorizing either the Board of Governors or the FDIC to define the term "interest" for both classes of banks. The FDIC made no specific recommendation on this subject but in the testimony given by its representatives in November it was stated that there is unfairness when one bank can absorb and another cannot depending upon whether or not it is a member of the Federal Reserve System. (See record, pp. 292–293.)

The advisory committee at page 30 et seq. of its report suggested that the Federal Deposit Insurance Act be amedned to read the same as the Federal Reserve Act with respect to the payment of interest on demand deposits. The reasons for this recommendation were that our committee thinks that the present lack of uniformity on this subject is deplorable; that uniformity should be achieved as we believe the Congress originally intended; that the direct or indirect payment of interest on demand deposits should be unlawful both as to nonmember insured banks as well as member banks; that the ruling as to the absorption of exchange constituting a prohibited payment of interest should be the rule.

Since the date of the advisory committee's report legal questions have arisen as to whether or not the implementation of our committee's recommendation will, as a matter of law, produce the result which our committee intended to achieve. In the light of this fact and for the reasons stated at length in the advisory committee report, I feel that this issue should be met squarely, to the end that absorption of exchange shall be outlawed and shall be outlawed for all insured banks alike, whether or not they are members of the Federal Reserve System. Thus, I urge that the committee print bill be amended as follows:

At page 163 of the bill strike out the first sentence of section 26 and substitute the following:

"No insured bank, whether or not it is a member of the Federal Reserve System, shall, directly or indirectly, by any device whatsoever, pay any interest on any deposit payable on demand except as now or hereafter may be permitted by law or regulation of the Board of Governors of the Federal Reserve System in the case of a member bank of the Federal Reserve System."

The result of this suggested change would clearly be that all insured banks, nonmembers as well as members, would be controlled by the regulations of the Board of Governors issued pursuant to section 41 at pages 117–118 of the bill. The Board consistently since September 1943 has ruled that absorption of exchange is an unlawful payment of interest. (See 1943 Federal Reserve Bulletin, page 817.)

In addition to the foregoing amendment, another might be made at page 118 of the bill. On that page the period at the end of section 41 (a) might be changed to a comma and the following added:

"*And provided further*, That within the meaning of the provisions of this section the absorption of exchange shall be deemed to be a payment of interest."

I urge that even though this last amendment is not made, that section 26 on page 163 be changed to read as I have suggested. If the only way to achieve uniformity is by the Congress forcing one agency to agree with another, then such action certainly should be taken here in order to eliminate the terrible inequity which has existed far too long.

I now want to mention a few of the important changes as relate to the Federal Home Loan Bank Act and Federal saving and loan associations.

Recommendations 118 through 140, except recommendation 121, have all been incorporated in the revision of the Federal Home Loan Bank Act as it appears from pages 181 through 202 of the bill. All of these are recommendations of the Federal Home Loan Bank Board which the advisory committee deemed to have merit and thus approved them. We have assumed that that Board will check the implementing language more closely than have I.

At page 203 of the bill, section 501 of the Home Owners Loan Act is amended to provide for a Federal Savings and Loan Association Act. While this was not the subject of a particular recommendation, I am pleased to see that this has occurred.

I note that recommendation 144 as made by the advisory committee at page 40 of its report has been implemented at page 207 of the bill by section 5 (d) (3) which is modeled after 12 Unted States Code, section 77, as it is revised at page 15 of the bill as relates to national banks and at page 101 as it relates to State member banks. This is in keeping with the thoughts of the advisory committee.

Recommendation 166C—Branches of Federal savings and loan associations

At page 211 of the bill, section 6 pertains to branches of Federal savings and loan associations and as we understand the situation it follows the language of H. R. 972 as passed by the Senate in the 84th Congress.

Recommendations 166F, 166G, 166H

I will comment on these in my oral testimony.

Recommendation 158 (1) Regulation of insured institutions

At page 221 of the bill, section 404 (e) implements this recommendation by providing that except with prior approval of FSLIC no insured savings and loan association shall be a party to a merger or consolidation or purchase assets or accounts from other associations. This is something comparable to section 23 of the Federal Deposit Insurance Act as it appears at page 162 of the bill. Our committee feels that these provisions are in the public interest.

Recommendation 166A—Holding companies

At page 227 of the bill, section 409 implements the recommendation which our committee made in regard to having holding company legislation relating to savings and loan associations. It is our understanding that the language employed is that which was used in the bill which Representative Spence, of Kentucky, introduced on this subject in the 84th Congress. While our committee did not consider this language, it strongly endorses the principle.

Title VII of the bill recasts the Federal Credit Union Act beginning at page 229 of the bill. All of the recommendations which were made as to Federal credit unions which were approved by the advisory committee have been implemented by the bill. We believe that as a result the practices and procedures of these worthy organizations will be vastly improved. I note particularly that recommendation 190 in regard to audits is implemented by section 7 (b) at page 231 of the bill. This provides that credit unions with assets of $50,000 or more shall have an annual audit by outside auditors approved by the Director of Federal Credit Unions and that unions with assets of less than $50,000 shall be audited annually by the Bureau of Credit Unions.

At page 235 of the bill, section 15 increases the size of unsecured loans which may be made from $400 to $500 and also provides that the Director may impose by regulation maximum loan limits for all credit unions or for any one or more classes provided the same is within the statutory limits. This last provision will provide a greatly needed safety factor in the operations of credit unions.

At page 241 of the bill section 25 of the Credit Union Act implements recommendation 173 of the advisory committee and amends section 21 of the old act so that a credit union "the membership of which is composed exclusively of persons who are either presently Federal employees or are retired Federal employees and members of their families" shall be eligible applicants for the allotment of space in Federal buildings.

In title VIII of the bill, which starts at page 242, various recommendations are implemented. I note, for example, that at page 251, section 803 (f) amends 18 United States Code, section 709, in conformity with S. 2891 of the 84th Congress as was suggested by the Comptroller in his recommendation 43 which was approved by our committee.

I now desire to speak briefly concerning the recommendations which were made by the advisory committee which have not been implemented in the committee print bill.

Recommendation 52—Service on Reserve Bank Board or Federal Advisory Council

At pages 74 and 85 of the bill will be found provisions which relate to the subject of this recommendation. Section 7 (a) at page 85 provides, among other things, that Federal Reserve bank directors, other than the chairman, shall be prohibited from serving more than 2 full consecutive terms of 3 years, each without an intervening period of not less than 3 years, and section 8 (a) at page 74 provides that members of the Federal Advisory Council shall be prohibited from serving more than 6 consecutive terms of 1 year each without an intervening period of at least 3 years.

It is the committee's opinion that advantages of preserving and promoting the autonomy of the Federal Reserve banks outweigh the possible benefits from rotation, that the present system has been beneficial and should be retained. Our report notes Professor Chandler's dissent on this recommendation.

Recommendation 79.—Reserves against deposit of public moneys

At page 120 of the bill will be found language which implements this recommendation of the Board of Governors, the first part of which our committee approved and the second part disapproved.

The second part, as provided for in section 42 (f) at page 120 of the bill provides that member banks shall maintain the same reserves against public funds as against other deposits.

Our committee does not recommend standby authority with respect to waiving reserves against public deposits in case of an emergency—authority can be readily provided in such case—but it based its recommendation primarily on the principle of giving the Board of Governors the broadest authority possible for the discharge of its monetary and credit control responsibilities.

Recommendation 115G—Increase in assessment credit; Recommendation 166K—With reference to the Federal Savings and Loan Insurance Corporation

Recommendation 115G of the committee was that a study be undertaken promptly and expeditiously to determine a reasoned formula for computing the proper premium cost to the insured banks for the risk involved, in the light of the present size of the FDIC deposit insurance fund supplemented by annual increases from income and assessments; and that, meanwhile, the Congress amend section 7 (d) of the Federal Deposit Insurance Act so as to provide that 1 year from the date of enactment of the act the annual net assessment income shall be credited pro rata to the insured banks.

Committee recommendation 166K was intended to treat the Federal Savings and Loan Insurance Corporation on a comparable basis, and accordingly the committee recommended that a similar change be made as regards FSLIC insurance, subject to the following:

"Further accumulations by FSLIC should be suspended pending the outcome of the study if the relationship which FSLIC's fund bears to its insurance liability is at least equal to that of FDIC."

These two important recommendations are not included in the bill; yet, as I am sure that this committee will want to consider them, I bring them to your attention.

To place the problem in the proper perspective it is first necessary to establish a common, proper concept of the purpose of the FDIC and the FSLIC. Our committee concluded that the only possible purpose these insurance corporations could serve was to insure depositors against losses resulting from the day-to-day institutional failures occasioned by mismanagement, inadequate capital, local disaster, defalcation, and similar institutional casualties. It is also quite apparent that it is completely unrealistic to believe that these corporations could possibly insure depositors and account holders against losses occurring on a major scale incident to economic or other disaster, any more than the private insurance industry could insure losses incident to an all-out atomic war. No insurance company, private or public, could provide any real protection against universal economic disaster, and it would be immoral to mislead the public that it could.

If this is a proper concept of the purpose of these insurance corporations, then the FDIC deposit insurance fund seems to be adequate at this time. Such fund now exceeds $1.7 billion, which is equal to 1.41 percent of insured deposits. In the 22 years that the FDIC has been in existence it has disbursed for working-capital purposes in the aggregate less than $290 million in connection with receivership and deposit-assumption cases. More particularly, of this amount actual losses during the entire period amounted to only $19 million and estimated possible future losses on cases that are still active amount to only $9 million. Thus, total actual or contingent losses of $28 million during the entire period are substantially less than the $39 million of income from investments accruing to the fund in the year 1955 alone. Furthermore, the fund was increased by more than $56 million in the year 1955 as a result of assessments.

While this record seems to be impressive, it is by no means conclusive because of the lack of comprehensive and acturial information. It is a bare, startling fact that, inconceivable as it may seem, no study has been made which would provide an actuarial basis for determining the underwriting liabilities of the FDIC and the FSLIC. At least, our committee could find none, nor was any made available to it.

It is essential that such a study be made. Our committee feels that such a study is feasible and this bill to amend and revise the statutes governing financial institutions and credit would be lacking if it did not provide for such a study. Our recommendation would, in effect, force the proper agencies to make such a study and give them 1 year in which to do it. Results of such a study would clearly point out the problems and give the Congress the kind of information it needs to provide insurance protection to the Nation's savers without misleading them and without creating too heavy a burden on the Nation's banks and savings institutions.

We recommend that the present assessment rate continue during the period of this study, but that if the study is not completed by the end of the time provided for, and a more scientific assessment rate is not established, then further accumulations should be dispensed with until such scientific assessment rate is established.

Probably the most important aspect of the committee's recommendation with respect to these two insurance corporations is that the study would afford a monetary and financial commission, should it be established, a place to start in reviewing the overall insured deposits program.

I am sure I speak for every member of our committee in strongly urging the Senate Banking and Currency Committee to consider these recommendations favorably.

Recommendation 166D—Prohibited practice

The advisory committee recommended making it unlawful for any institution organized under the laws of either the United States or a State which is not authorized to engage in the business of receiving deposits to represent or hold itself out in any manner that it is a bank. The committee print bill does not implement this recommendation because, as we understand it, within the time available it was impossible to work out proper implementing language. It would appear that the relevant language might be placed in the committee print bill as a further amendment to title 12, United States Code, section 378 at page 36 of the bill. I intend to suggest implementing language.

Recommendation 195—Monetary and Financial Institutions Commission

This recommendation was perhaps the most important one made by our committee. It was that the 85th Congress enact without delay legislation providing for the establishment of a commission for the purpose of making an objective study and appraisal of the use of monetary controls to stabilize the Nation's economy and the impact of such controls upon the American system of free enterprise, and of the adequacy and responsibility of all financial institutions as custodians of the Nation's savings, to provide, individually and collectively under existing laws, the State and National financial needs for the continuing growth of our dynamic economy, giving appropriate consideration to deposit and savings insurance programs, the essentiality of Government lending and investing, and the tax burden on debtors, creditors, and equity owners.

May I say at the outset that this is not a matter that should necessarily be brought before Congress by incorporating it in the bill to amend and revise statutes governing financial institutions and credit. Accordingly, we considered that it was appropriate to omit this particular recommendation from the bill. As a matter of fact, it is preferable to have it incorporated in a separate bill in order to expedite the consideration of the recommendation.

The urgent need for such a study can hardly be questioned, both from the standpoint of the great many years since we have had one and also because of the tremendous changes in our economy during the intervening period. The last such study was made by the National Monetary Commission in 1908 and it lead to the formation of the Federal Reserve System in 1913. The major economic and social changes which have occurred since 1908 have substantially altered the functions, types, and relationship of financial institutions to public need and the economy. Notwithstanding the new demands occasioned by these changes, all we have had is piecemeal legislation to meet the day-to-day needs of the economy.

We are indeed pleased to see the introduction of S. 599 to establish a National Monetary and Financial Commission, and we strongly urge the study and consideration of this bill. We favor, however, an amendment to the bill broadening the composition of the Commission to include adequate representation of the Congress as we originally recommended. The legislative branch should be represented by not less than 4 and not more than 6 members of the Banking and Currency Committees of the House of Representatives and the Senate, consisting of the chairmen and the ranking members.

Basically our committee felt the scope of such a Commission's functions should be stated in the broadest terms in order to avoid disputes in the initial stages over controversial issues and the Commission after an exploratory period would be in a better position to define its areas of study. Nevertheless, section 3 of S. 599 seems to be conclusive and adequate, but if I properly interpret the views of the members of our committee, I would have to take strong exception to section 3 (f) (3). Certainly our committee would want no legislation that in the remotest way would prejudice the independence of the Federal Reserve System. This particular section might possibly be interpreted as a mandate by Congress for the Commission to question the System's independence of structure and power. Personally I believe that section 3 (f) (3) adds very little and that it might possibly be misinterpreted. Thus I feel that it should be deleted from S. 599.

In conclusion, our committee recommendation 195 squarely supports the principle of S. 599 and we urge its speedy enactment.

Next I will briefly discuss matters included in the committee print bill which were not specifically covered by the report of the Advisory Committee.

See for example, the last sentence of section 35 (a) at page 27 of the bill. There it is provided in the section dealing with interest which may be charged by a national bank, that the purchase of evidence of indebtedness from the owner shall not be deemed to be a loan or discount except to the extent that "they" may be construed as loans or discounts under the laws of the State in which the bank is located. I am informed that the purpose of this provision is to legislate away the holding of the old case of *National Bank* v. *Johnson* (104 U. S. 271). This has not been considered by the Advisory Committee. Speaking solely for myself, I believe that this is a fair provision for national banks if my understanding of its purpose is correct. For example, in my home State the Supreme Court of Missouri has held that where paper is purchased from the payee or other holder at a discount, usury is not present whatever amount the purchaser pays, as it is a purchase not a loan even though the holder endorses with recourse. (See *Webster* v. *Sterling Finance*, 195 S. W. 2d 509, l. c. 514, Mo. Sup. 1946.) In any event, I suggest that the language be changed as suggested in the amendment which I will submit.

In recommendation 44 the Comptroller suggested the need for a statute providing that reports of examinations of national banks, etc., shall be deemed confidential and privileged against disclosure to unauthorized persons except with the consent of the Comptroller. Recommendation 115E of the FDIC was comparable. Both were approved by our committee. Section 50 at page 41 of the bill implements the former and section 10 at page 153 of the bill the latter. I believe that a comparable provision should be inserted relating to the Federal Reserve Board. I mention these sections at this point because each adds a provided however clause to the effect that the privileged documents shall be made available to the committees of the Congress upon request. The Advisory Committee report at page 30 states that our committee by its approval did not intend to take a position for or against disclosure by the executive branch to the legislative branch.

At page 183 of the bill, section 4 (d) of title IV makes it unlawful for any uninsured member of the Federal Home Loan Bank to advertise or represent that it is connected with the Home Loan Bank System except as may be authorized by regulation. While the advisory committee made no formal recommendation as to this, it was discussed informally and I feel certain that I properly sense the feeling of our committee when I express approval of its having been inserted in the committee print bill.

In my discussion of recommendation 115b I alluded briefly to the criminal provisions which appear at pages 248 and 249 of the bill. As I have stated, these are new provisions which were not considered by the advisory committee, thus my remarks represent only my personal views. It seems to me that these provisions at pages 248 and 249 as they relate to employees of the supervisory agencies becoming employees of any institution which they may have examined is much too broad and if enacted will produce results of as serious a nature as are the results which the provisions were designed to prevent occurring.

One of the big problems of banking today is the matter of obtaining qualified personnel. Without elaborating on the basic proposition, I want to say that the provisions of the bill I am referring to will for all practical purposes cut off one of the best sources of supply of qualified personnel for the banking system—the employees of the supervisory agencies. This of itself is not in the public interest, because for each instance which the provisions are designed to prevent occurring there are dozens of instances of honorable relationships which have arisen between banking institutions and former employees of the supervisory agencies. A great many leaders in banking are products of the examining agencies.

There is another harmful aspect which I think merits your consideration. Means should be found and employed to strengthen the quality of bank supervision, not weaken it. I feel that these provisions will inevitably make it more difficult for the agencies themselves to obtain the services of younger qualified personnel and conceivably can result in the rapid decimation of their present complements.

I therefore earnestly suggest that your committee find some way of achieving the purpose you have in mind without exposing both the banking system and its supervisors to the hazards I have mentioned.

Prior to concluding, I will mention two recommendations which were made by the advisory committee which have not been implemented by the committee print— and properly so—but which our committee hopes that your committee will pass along with your favorable recommendation for action by the appropriate committees of the Congress.

First, there is the matter of postal savings. Our committee believes that following the recommendations of the Comptroller General and the Hoover Commission, the Postal Savings System should be liquidated in an orderly fashion forthwith. It has outlived its original purpose and private enterprise provides adequate facilities for the savings of our people.

Second, all banks, State-chartered as well as National, should by law be permitted to establish adequate and realistic bad-debt reserves under statutory formula.

Reserves permitted by present Treasury regulations are inadequate on the basis of past experience and penalize prudent management. This inadequacy is even more pronounced if the banking system is to meet the huge and increasing demands for credit in a dynamic economy and protect the depositors. Our present economy requires the extension of many types of credit never before provided primarily by the banking system. As a result, the banking system must provide enormous amounts of consumer, mortgage, capital, and term credit, which types carry risks not present in banking in the historical sense.

Accordingly, a new concept of the adequacy of reserves for losses for eligible loans outstanding in the banking system must be forthcoming. Consideration of the risks and the inadequacy of capital in the banking system forcibly demonstrates that any reserve less than 5 percent of eligible loans outstanding is wholly inadequate and unrealistic. The banking system should therefore be permitted to accumulate reserves in excess of this amount.

Thus, the advisory committee recommends that commercial banks be permitted under the Internal Revenue Code to add to reserves for bad debts in any taxable year up to a percentage of not less than one-half of 1 percent and not more than 1 percent of eligible loans, provided that no addition under the formula to such reserves in any taxable year shall cause the aggregate thereof to exceed a percentage of not less than 5 percent and not more than 10 percent of the eligible loans.

In conclusion the advisory committee again thanks you for this opportunity to be of service and trusts that its work has been of assistance to you.

SCHEDULE 1 ATTACHED TO STATEMENT OF KENTON R. CRAVENS

Here follows list of recommendations (by their numbers) which were approved by the report of the advisory committee and which are implemented in the committee print of bill cited as "Financial Institutions Act of 1957," which recom-

mendations are referred to in part I of testimony given by Kenton R. Cravens on January 28, 1957, viz:

[Column A denotes number of recommendation; column B denotes page of bill where found]

A	B	A	B	A	B
1	2	85C		133	196
3	3	85D		134	197
4	18, 19	85E	84	135	197
8	43 et seq.	86	148	136	199
12	5, 6	87	148	137	200
14	243	88	148	138	200
18	243	89	148	139	202
19	243	90	148	140	202
20	13	91	148	142	203
22	31	92	149	143	203
27	69	93	149	146	209
30	54	96	157	148	214
31	55	98	160	150	214
32	56	100	150	151	215
38	247	101	150	152	215
39	246	102	154	153	216
46	70	104	152	154	216
47	88	105	150	155	216
48	102	106	168	156	218
49		107	170	157	218
50	70, 85	108	171	158	221
53	88	109	171	159	221
57	89	110	169	160	222
59	134	111	174	161	222
61	111	115D	169	162	223
62	111	117	181	164	250
63	146	118	182	165	250
64	71	119	182	166	251
65		120	183	166B	215
68	111	122	184	166H	213
70	80	123	186	166I	247
71	84	124	189	166J	250
73	145	125	190	167	233
74	120	126	192	169	234
75		127	192	170	234
76		128	193	174	251
78	117	129	193	175	229
80	99	130	195	180	236
82	123	131	195	181	242
84	101	132	196		

Senator ROBERTSON. For the benefit of the press and also of the witnesses, the Chair wishes to announce the program for this week. Tomorrow we will hear the American Bankers Association and we will have some very fine representatives, including the president of that association, Mr. Erle Cocke, of Atlanta, Ga.; Mr. Lee P. Miller, of Louisville, Ky.; Mr. Gibbs Lyons, of Stamford, Conn.; Mr. D. Emmert Brumbaugh, of Claysburg, Pa.; and Mr. Paul A. Warner, of Oberlin, Ohio.

On Wednesday, January 30, we will hear from Mr. Ben DuBois, Sauk Centre, Minn., representing the Independent Bankers Association; from Mr. William A. Lyon, New York, N. Y., representing the National Association of Mutual Savings Banks; and from Mr. J. A. Baker, Washington, D. C., representing the National Farmers Union.

On Thursday, January 31, we will hear from Mr. Sam M. Fleming, Nashville, Tenn., representing the Association of Reserve City Bankers; from Mr. Charles R. Howell, Trenton, N. J., representing the National Association of State Bank Supervisors; and from Mr. Henry A. Bubb, of Topeka, Kans., as we previously indicated, representing the United States Savings & Loan League.

On Friday, February 1, we will hear from Mr. James W. Grant and David R. Weinberg, representing the Credit Union National Association; from Mr. Henry H. Heimann, New York, N. Y., representing the National Association of Credit Men; from Mr. Donald E. Durick, Fort Wayne, Ind., representing the American Industrial Bankers Association; and from Mr. A. D. Shackelford, Wilson, N. C.

We also have witnesses scheduled for the 2 following weeks, but they will be announced later.

I have a number of letters sent in to the committee, and without objection they will be made a part of the record.

(The letters referred to are as follows:)

THE FIRST NATIONAL BANK,
LaJara, Colo., January 11, 1957.

HON. GORDON ALLOTT,
United States Senate Chambers,
Washington, D. C.

DEAR SENATOR ALLOTT: At present a national bank is permitted to borrow on its note obligation from a correspondent bank the amount of its capital stock without consideration given to its surplus and reserves and undivided profits. In our particular case, as you can see from the December 31, 1956, statement attached, this would mean only $50,000, or about one-seventh of the total shareholder investment of $351,500.

The current bulletin of A. S. Pratt & Sons, Inc., 815 15th Street, Washington, D. C., with the slogan "Serving bankers since 1867" states under proposed law revisions under recommendation of the advisory committee:

"*Increase in debt limit of a national bank.*—The committee proposes that the present limitation be increased to 100 percent of capital and surplus."

The new banking code under consideration by the Colorado Legislature endorsed by the Colorado Bankers Association provides that Colorado banks operating under State charter shall be limited to "two times its capital and surplus" and, further, "or in such larger amount as the banking board approves."

Under these circumstances, may I not kindly ask you to give this measure full support and to lend your influence with such Senate committee as may have it in charge?

Thanking you kindly and with personal wishes, I am

Very truly yours,

O. A. GARRIS, *President.*

THE FIRST NATIONAL BANK OF COLORADO SPRINGS,
Colorado Springs, Colo., January 16, 1957.

HON. JOHN CARROLL, SENATOR,
Senate Office Building, Washington, D. C.

DEAR SENATOR: This bank is greatly disturbed at the consequences should certain provisions of a bill to amend the statutes governing financial institutions and credit be enacted. The particular provision objected to concerns prohibitions and penalties levied in connection with bank examiners accepting employment in banks.

The various bank supervisory agencies have for years been a training ground for bankers. Many of the heads of leading banks of the country have been bank examiners. As such an examiner, I can visualize the consequences of the rash legislation contained in the proposed amendments to section 803 (a) section 217 of title 18, United States Code, now before the Congress.

The first effect of enactment of this legislation will be mass resignation of examiner personnel and a later effect will be an inability to enlist examiner personnel in the future.

I trust your action in connection with this proposed legislation will be toward its rejection.

Sincerely,

J. F. ANGELL, *Vice President.*

THE FIRST NATIONAL BANK OF COLORADO SPRINGS,
Colorado Springs, Colo., January 17, 1957.

HON. JOHN CARROLL,
Senate Office Building, Washington, D. C.

DEAR SENATOR: We call your attention to the bill to amend and revise the statutes governing financial institutions and credit. Under amendments to the Criminal Code we believe this new bill as written will be a strong deterrent to enlisting qualified men to serve as bank examiners and others entering the Government financial field.

Where one's freedom of motion of employment is restricted, such as this bill does, we believe it immediately sets up a barrier of employment.

You are aware of the general difficulty that now exists in the recruitment and development of qualified bank examiners by the Treasury Department, and this bill we feel will definitely further handicap their progress.

Thanking you for your consideration in this matter, and with my very kindest regards.

Sincerely,

H. CHASE STONE, *President.*

THE EXCHANGE NATIONAL BANK OF COLORADO SPRINGS, COLO.,
Colorado Springs, Colo., January 17, 1957.

Senator JOHN CARROLL,
Senate Office Building, Washington, D. C.

DEAR SENATOR CARROLL: It is my understanding that you now have, or will soon have, before you a bill to amend section 803 (a) section 217 of title 18 of the United States Code governing financial institutions and credit. I would like to express my very firm opinion that present legislation on this matter has appeared to be quite adequate, with few violations. The amendment if passed, I am inclined to believe, would discourage good men from entering the Federal services named in the amendment and could easily be the means of present good, able, and conscientious servants terminating their employment in those divisions.

One point specifically is that part making it unlawful to "employ or make an offer of employment to any officer or employee of the Comptroller of the Currency, etc. within a period of 2 years." Many good men go from the Federal services into banks. Many men go into the Federal service as a foundation for experience to qualify them for banking. If such a person cannot talk about a position within 2 years after he leaves the service, it might well be that he would not enter the Federal service for that very reason. I believe it is true that the Comptroller's office is having a hard time getting and keeping outstanding young men. The proposed amendment could very well aggravate that situation.

Most sincerely,

JASPER ACKERMAN, *President.*

THE FULLERTON NATIONAL BANK,
Fullerton, Nebr., January 21, 1957.

SENATE BANKING AND CURRENCY COMMITTEE,
Washington, D. C.

SIR: The text of the committee print bill has been reviewed by the writer and as a whole I believe the committee is to be commended for their sound views and proposals. There are some proposals, however, in which I do not concur and I am presenting my views and comments for your consideration:

TITLE 1, NATIONAL BANK ACT

Section 22 (b)

My objections to this proposed section are:

1. Further intrusion upon the rights of proprietorship, with increasing bureaucratic power and control of private enterprise.
2. The legislation is admittedly for the control of a very nominal number of banks and could easily unduly penalize the smaller banking institutions who have built up a large capital account. Present legislation covering removal of officers because of "unsafe and unsound practices" would seem to be adequate to provide control of the cases which were presented at the hearings.
3. In my opinion, this legislation would tend to discourage the retention of profits in the capital account and would be conducive to the reduction of earnings by excessive salaries, fees, etc.—at the expense of the shareholders.

4. In States where branch banking is permitted it would further enhance their expansion potential, as individuals would not be interested in the purchase of banking institutions with large capital accounts, if both the seller and the purchaser were prevented from making capital adjustments.

5. This section would, in my opinion, further lessen the attractiveness of investing in bank capital stock, when other industries would probably be more attractive and their operations under less governmental control.

6. It is my opinion that under the provisions of this section it would be more desirable to operate under a nonmember State charter and result in a decrease in national banks.

7. It would seem that this section would also create unfair competition of operations under a national charter as compared to that of a nonmember State bank, particularly with respect to stock ownership.

It was brought out in the hearings that banking institutions have paid dividends in excess of earnings for the current year and that such were paid from undivided profits. It is difficult to understand where there is anything wrong in making such payments from profits which have been accumulated during periods of more prosperity. Such savings of profits are often for use in less prosperous times. It seems to me that in biblical times surpluses were saved in lush periods for relief in times of famine.

Section 52

Do not concur in the requirement that the Comptroller of the Currency may require the publication of the report of payment of dividends. Some banks publicize such information but in smaller communities such a report might not be understood and have unfavorable public reaction.

TITLE III, FEDERAL DEPOSIT INSURANCE ACT

Section 301—chapter 3, section 6

In my opinion, the provisions of this section would invest too much power in one individual and tend to make the office dictatorial. Certainly the views of 3 men should be better than that of 1 individual; also, the proposed Advisory Board would not be invested with any power.

This recommendation does not seem consistent with the Federal Deposit Insurance Corporation's policies with respect to banks. They have been very critical of the one-man dominated banking institutions, and yet they recommend such powers over the majority of the banks in the United States. It would seem therefore that if a one-man operation is not good for banks it would be increasingly detrimental to the formulation of policies and operations, and supervision, of an agency as large and influential as the Federal Deposit Insurance Corporation; also, other governmental agencies in the financial field are governed by a Board. The Federal Reserve bank is governed by a Board and the advisory committee, to your committee, rejected recommendation 66 with respect to simple majority for all Board actions. It is my further opinion that the minority party should be represented in the formulation of policies, operations, and supervisory authority, of a corporation which directly or indirectly affects almost every individual in this United States. It is my belief that the number of directors should be increased from 3 to 5 members, instead of investing such great power in 1 individual.

Section 29

It is my opinion that the portion of this section which recites: "such shorter periods of time as the Comptroller of the Currency or State authority, or Board of Governors of the Federal Reserve System" is entirely out of line with justice. This again puts too much power in one individual or Board and could easily create an injustice. It is my belief that any accused should have ample time to prepare and present a defense under this proposed law, or any other law, and I do not see where such a time is provided—unless I have wrongly interpreted this part of the section. It is my opinion that a fair period of time would be 60 days.

The text of the committee print bill was presented to our entire Board of Directors and they were in full concurrence with the views and comments as expressed above.

Respectfully submitted.

C. H. Hosler, *President.*

THE INDIAN RIVER CITRUS BANK,
Vero Beach, Fla., January 21, 1957.

HON. GEORGE SMATHERS,
United States Senator,
Washington, D. C.

DEAR SENATOR: I enclose for your information excerpts from the Robertson bill to revise the Federal banking laws.

Particularly I want to call to your attention the changes as they relate to the employment of examiners by banks. With all due respect to the person or persons who are responsible for this bill, I believe that the changes would be very detrimental to the banking system. Again, I repeat, I am referring only to the section regarding the employment of examiners.

I speak from experience when I make these comments as I was associated very pleasantly with the Federal Deposit Insurance Corporation as an assistant examiner and later as an examiner for a period of about 10 years. I do not believe that the position would have been nearly as attractive to me if I had known I would have to be governed by the drastic measures contained in this proposed Robertson bill.

I believe I am correct when I say that the Federal supervisory agencies recognize that they run a training school for future bankers. I further believe I am correct when I say that they are very happy to conduct such a program for they feel that the returns come back to them by way of better management and fewer problem banks.

Unfortunately the newspapers played up the banking case in Illinois and I believe there were times when they were ill-advised as to the actual facts in the case.

Please give every consideration to having the employment feature of the bill struck out for certainly it can do nothing but create a very difficult situation for supervisory agencies for the hiring of new personnel.

Yours very truly,

L. S. TILLER,
Executive Vice President.

A BILL TO AMEND AND REVISE THE STATUTES GOVERNING FINANCIAL INSTITUTIONS AND CREDIT

(Excerpts)

AMENDMENTS TO CRIMINAL CODE

SEC. 803. (a) Section 217 of title 18 of the United States Code is amended to read as follows:

"SEC. 217. Whoever, being an officer, director or employee of a bank which is a member of the Federal Reserve System or the deposits of which are insured by the Federal Deposit Insurance Corporation, or of any land bank, national farm loan association or other institution subject to examination by a farm credit examiner, or of any savings and loan, building and loan, or homestead association, cooperative bank or other institution the accounts of which are insured by the Federal Savings and Loan Insurance Corporation, or of a Federal credit union, or being a stockholder of such a bank, corporation, association or institution holding directly or indirectly 10 per centum or more of the stock thereof—

"(i) gives or grants any gratuity or gift to any examiner or assistant examiner who examines or has authority to examine such bank, corporation, association, or institution, or to any other officer or employee of any Federal or State agency having supervisory authority over such bank, corporation, association, or institution, or

"(ii) makes or grants any loan to, or employs or makes an offer of employment to, any examiner or assistant examiner or to any other officer or employee of any Federal or State agency having supervisory authority over such bank, corporation, association, or institution who is examining or is employed or performing duties in connection with such bank, corporation, association or institution or who in the two years preceding the making or granting of the loan or the employment or offer of employment examined or was employed or performed duties in connection with such bank, corporation, association or institution, or

"(iii) in a case not falling under (ii) above makes or grants any loan to or employs or makes an offer of employment to, any officer or employee of the Comptroller of the Currency, of the Board of Governors of the Federal Reserve Bank, of the Federal Deposit Insurance Corporation, of the Farm Credit Administration, or of the Federal Home Loan Bank Board or of the Bureau of Federal Credit Unions, unless the written approval of the governing body (in the case of an agency having a board of directors or comparable body) or the principal official (in the case of an agency having a single administrator) of the agency in which the officer or employee is appointed or employed has first been obtained,

shall be fined not more than $5,000 or imprisoned not more than one year, or both, and may be fined a further sum equal to the money so loaned or gratuity given or granted.

"The provisions of this section shall apply to all public examiners and assistant examiners who examine, and other officers and employees of public agencies which supervise, member banks of the Federal Reserve System or insured banks, or from land banks or national farm loan associations, or insured savings and loan associations, whether appointed by the Comptroller of the Currency, by the Board of Governors of the Federal Reserve System, by a Federal Reserve agent, by a Federal Reserve bank, by the Federal Home Loan Bank Board, by the Farm Credit Administration, or by the Federal Savings and Loan Insurance Corporation, or by the Bureau of Federal Credit Unions, or appointed or elected under the laws of any State; but shall not apply to private examiners or assistant examiners employed only by a clearinghouse association or by the directors of a bank."

(b) Section 218 of title 18 of the United States Code is amended to read as follows:

"SEC. 218. Whoever, being a member, officer, or employee of the Board of Governors of the Federal Reserve System, of the Comptroller of the Currency, of the Federal Deposit Insurance Corporation, of the Federal Home Loan Bank Board, or of the Farm Credit Administration, or the Bureau of Federal Credit Unions—

"(i) accepts any gratuity or gift from any bank, corporation, association, or other institution over which the agency employing such member, officer, or employee has supervising authority, or from any officer, director, or employee, or stockholder holding directly or indirectly 10 per centum or more of the stock of such institution, or

"(ii) applies for or receives a loan, or accepts or agrees to accept an offer of employment, from any bank, corporation, association, or other institution which he is examining or in connection with which he is employed or is performing duties, or in the two years preceding the application or acceptance of the loan or the acceptance or agreement to accept the offer of employment has examined or has been employed or performed duties, or from any officer, director, or employee, or stockholder holding directly or indirectly 10 per centum or more of the stock of such institution, or

"(iii) in a case not falling under (ii) above, applies for or receives a loan, or accepts or agrees to accept an offer of employment, from any bank, corporation, association, or other institution which the agency employing him has authority to supervise, or from any officer, director, or employee, or stockholder holding directly or indirectly 10 per centum or more of the stock of such institution, without first having obtained the written approval of the governing body (in the case of an agency having a board of directors or comparable body) or the principal officer (in the case of an agency having a single administrator) of the agency in which he is appointed or employed,

shall be fined not more than $5,000 or imprisoned not more than one year, or both; and may be fined a further sum equal to the money so loaned or gratuity given."

THE FIRST NATIONAL BANK OF STEVENS POINT, WIS.,
January 24, 1957.

HON. ALEXANDER WILEY,
The United States Senate,
Washington, D. C.

MY DEAR SENATOR: The unnumbered Senate bill introduced by Senator Robertson, entitled "Financial Institutions Act of 1957," which is set for a hearing before the Banking and Currency Committee on January 28, 1957, has several features that would be detrimental to banking and to the supervisory authorities.

I specifically refer to the amendment to section 217 of title 18 and section 218 of title 18 of the United States Code, wherein any officer of a financial institution would be subject to a fine or imprisonment if he granted a loan to any examiner or any officer of a supervisory agency or offered employment to any examiner, officer, or employee of a Federal or State supervisory agency. And any examiner, officer, or employee of a Federal or State supervisory agency would be subject to a fine and imprisonment if he accepted a loan from a financial institution or accepted an offer of employment from any financial institution in the 2 years preceding the approval or acceptance of the loan or offer of employment.

The most objectionable part of the amendment pertains to the offer of employment to an examiner, officer, or employee of an agency. Supervisory authorities are continually seeking young men to enter the service of an agency with the hope that they will make it their career. However, most men enter the service in order to gain the experience and banking background necessary to obtain a position in the banking field. Banks are continually looking for men with such backgrounds, and if this amendment were passed it is my opinion that it would be extremely difficult to obtain men to go into service as any examiner seeking a position in a bank would have to resign from the service and wait 2 years before accepting employment. I know that the salaries paid to men in the service are not sufficient to keep them or their families for 2 years while waiting to obtain employment.

There are a number of bank executives in our State at the present time who were former examiners and who would not hold their present position had it not been for their experience and background as an examiner. I speak from experience as I was an examiner with the Federal Deposit Insurance Corporation for 14 years prior to my return to the banking business.

I sincerely hope you will use every effort to defeat this portion of the act.

With best regards, I am,

Sincerely yours,

JOSEPH R. HARTZ, *President.*

THE FIRST NATIONAL BANK,
Pueblo, Colo., January 24, 1957.

HON. GORDON ALLOTT,
United States Senate, Washington, D. C.

DEAR SIR: It has come to my attention that there is now a bill before Congress to amend certain sections of the United States Code. I specifically refer to section 803 to amend sections 217 and 218 of title 18, United States Code, in reference primarily to examiners and assistant examiners of the various Federal agencies supervising lending institutions.

As a former examiner for the Federal Deposit Insurance Corporation, I would like to go on record in opposition to the proposed amendments, as I believe that the amendments would be to the ultimate disadvantage of the Federal supervisory authorities, as well as to the lending institutions covered by the amendments.

As you know, sections 217 and 218, Title 18, United States Code, are rather comprehensive and limiting in their present form and as such it would appear to me that they are adequate. The proposed amendments concerning an offer of employment to an examiner or assistant examiner being classed as a criminal violation appear to be without constructive foundation and with several serious detriments.

It is presently difficult for the supervisory authorities to attract capable men to serve as examiners and assistant examiners. If the new amendments are passed into law it would, in my opinion, be much more difficult to attract competent men into this field. It might also result in the resignation of many capable examiners and assistant examiners in that the passage of the amendments would be interpreted by the men to mean that for practical purposes they are tied to their present jobs without the opportunity as freemen to make employment changes when they could, in their opinion, better themselves.

As a former examiner, it is difficult to understand what possible benefit is expected to accrue by forbidding a lending institution under criminal penalty to consider the employment of experienced examiners or assistant examiners who supposedly have been conservatively trained in lending activities by the United States Government. Instead of forcibly retaining examiners and assistant examiners in the Government services, I fear such action may have the opposite effect.

In the past the various Federal agencies supervising lending institutions have taken the position that the valuable experience gained while a member of the examining force would be beneficial to lending institutions as a whole should some of their members decide to leave the force and become employed by a bank or other lending institution. In short, although the agencies prefer not to lose trained men, they feel that the banking profession as a whole will ultimately benefit making the job of the examining agency less difficult in the long run.

Your cooperation and careful consideration of the possible results of such legislation before action is taken will be greatly appreciated by the undersigned.

With kindest personal regards.

Very truly yours,

D. W. CALDWELL, *Vice President.*

Senator ROBERTSON. The committee will now stand in recess until 10 a. m. tomorrow morning.

(Whereupon, at 12:15 p. m., the committee recessed until 10 a. m. the following day, Tuesday, January 29, 1957.)

STUDY OF BANKING LAWS

(Financial Institutions Act of 1957)

TUESDAY, JANUARY 29, 1957

UNITED STATES SENATE,
COMMITTEE ON BANKING AND CURRENCY,
SUBCOMMITTEE ON BANKING,
Washington, D. C.

The subcommittee met, pursuant to recess, in room 301, Senate Office Building, at 10:05 a. m., Senator A. Willis Robertson (chairman of the subcommittee) presiding.

Present: Senators Robertson, Frear, Clark, Bricker, and Bennett.

Senator ROBERTSON. The subcommittee will be in order.

The chairman of this subcommittee did not appreciate what a big organization the American Bankers Association was until a few years ago, when it was his privilege to speak at one of their annual meetings in Atlantic City. He was on the morning program and a Cabinet officer was ahead of him, and 2 or 3 other experts ahead of him, so they did not reach him on the program until nearly noon. Before he started speaking there seemed to be a great exodus from the hall, and he remarked to the man next to him, "My goodness, everybody is leaving." He said, "Oh, no. There will be some 4,000 left to hear you." I said, "In Virginia that is considered a very satisfactory audience."

We are pleased to have with us this morning the representatives of such a fine group of bankers. They extend from Maine to Florida and from Virginia to California. I am particularly glad to see heading the group a friend from Atlanta, Ga., an outstanding banker and civic leader, one of the real leaders of the South, who was at your Los Angeles convention this year elected president of this great organization. That is Mr. Erle Cocke.

He informs me, however, that he would like one of our Kentucky neighbors to start the testimony.

Mr. COCKE. That is right, sir.

Senator ROBERTSON. We feel very kindly toward Kentucky, because after all, the county I live in, Rockbridge County, was cut from Augusta County. Before that Augusta County ran to the Mississippi River and Kentucky was a part of it.

We are proud of Kentucky and glad to have Mr. Miller as our first witness.

We will be glad to hear from you.

STATEMENT OF ERLE COCKE, PRESIDENT; ACCOMPANIED BY LEE P. MILLER, CHAIRMAN OF THE COMMITTEE ON FEDERAL LEGISLATION; GIBBS LYONS, PAST PRESIDENT OF THE NATIONAL BANK DIVISION; FRANK L. KING; D. EMMERT BRUMBAUGH, CHAIRMAN OF THE COMMITTEE ON FEDERAL DEPOSIT INSURANCE; AND PAUL A. WARNER, CHAIRMAN OF THE COMMITTEE ON FEDERAL LEGISLATION OF THE SAVINGS AND MORTGAGE DIVISION, AMERICAN BANKERS ASSOCIATION

Mr. MILLER. Good morning, Mr. Chairman.

My name is Lee P. Miller. I am president of the Citizens Fidelity Bank & Trust Co., of Louisville, Ky. I appear here today as chairman of the committee on Federal legislation of the American Bankers Association.

I should like to say at the outset that the American Bankers Association recognizes the monumental task undertaken by Senator Robertson and the members of your committee in the preparation of this Financial Institutions Act of 1957—we would like to call it the Robertson Act, if you do not mind—and desire to compliment the committee on its accomplishment.

We have four witnesses whom I should like to introduce, each of whom will present in brief form our association's position on different provisions of the bill. I shall also introduce the president of the American Bankers Association, who will make a short closing statement. Before introducing the witnesses, Iwould like to call the attention of the committee to a recommendation which we submitted previously relative to bank bad-debt reserves. Although recognizing that our recommendation covers a subject which could not appropriately be included in the bill before you, we believe that it is germane to consideration of any legislative program involving the banking system of this country.

Provision for adequate bank reserves out of current earnings to meet future loan losses contributes to the safety of depositors' funds and the availability of credit so necessary to provide employment and business activity in periods of economic recession. For these reasons all banks should be encouraged to establish and maintain such reserves. We believe our proposal will accomplish this objective.

We propose that the Internal Revenue Code be amended to adopt an industrywide basis for reserves for bad debts of banks under which an annual addition to reserves of a percentage of total eligible loans would be permitted as a current deduction from income each year until the accumulated reserve reaches a limit also calculated as a percentage of total loans outstanding. The maximum amount so allowed should be adequate to absorb the losses that past experience demonstrates may be sustained in a period of economic recession.

The proposal should not result in any ultimate loss of tax revenue as it amounts to a deferment of tax since all bad debt losses on loans must be charged to the reserve. We hope that this committee may give consideration to the merits of our proposal and will refer it with favorable recommendations to the House Committee on Ways and Means and the Senate Committee on Finance.

Senator ROBERTSON. Let me interrupt to say that I have requested Chairman Fulbright, as I mentioned yesterday, to bring it before our committee. I am sure we will endorse it and submit our recommendation to the tax committees of the Congress.

Mr. MILLER. Thank you.

Senator ROBERTSON. It would be in line for the American Bankers Association to submit its recommendations both to the tax committees of the Congress and to the Secretary of the Treasury.

Mr. COCKE. Thank you, sir.

Mr. MILLER. We hope we may be able to do that. However, one phase of the matter I should like to call attention to is the American Bankers Association made this survey of all the banks of the country to determine how many were using this bad debt reserve. We found that about 50 percent of the banks in the country were not on a reserve basis, and that that 50 percent happened to be primarily the smaller banks, as, in effect, 90 percent of the total banking resources are in the hands of the banks that are on the reserve method. The method up to this point has been a 20-year moving average, and later in 1954 it was amended, so that you could freeze the 20 years to get your experience on any consecutive 20-year period, beginning in 1928.

The smaller banks on this survey took the position that the method was so complex that they just did not care to worry with it and had no records of what their losses were, and so on and so forth. So we think it would be a very helpful thing, particularly for the smaller banks of the country, which did most of the closing back in the thirties, to get them on a reserve method, as well as the larger banks.

It is with that objective in mind that we have proposed this industrywide basis on a simple percentage per annum would be permitted to be deducted as a reserve for bad debts. The result of that survey I thought might be interesting to you to hear about, Senator.

Mr. Chairman, I should like now to introduce our witnesses: Mr. Gibbs Lyons, who will testify regarding the National Bank Act; Mr. Frank L. King, whose testimony will relate to the Federal Reserve Act; Mr. D. Emmert Brumbaugh, who will testify concerning the Federal Deposit Insurance Act; Mr. Paul A. Warner, who will deal with provisions relating to the Federal Home Loan Bank System; and Mr. Erle Cocke, president of the American Bankers Association, who will present a general statement at the conclusion of our testimony.

Our first witness, Mr. Gibbs Lyons, of Connecticut.

Senator ROBERTSON. The committee will be glad to hear all of these witnesses, but the chairman must call your attention to the fact that the Senate meets today at 12 o'clock and we will have to recess today at that time. Therefore the witnesses will bear that in mind in giving their testimony. I would assume we can finish your testimony, though, in that time.

Mr. MILLER. We will be well within that time limit, sir.

Senator ROBERTSON. You may proceed.

Mr. LYONS. Mr. Chairman and members of the Senate Banking and Currency Committee, my name is Gibbs Lyons. I am president of the First-Stamford National Bank & Trust Co. of Stamford, Conn., and immediate past president of the national bank division of the American Bankers Association.

The American Bankers Association believes that title I of the Robertson bill amending and reenacting the National Bank Act is an excellent and much needed legislative proposal.

In my statement I shall discuss those changes in the law contained in the National Bank Act which are of particular interest to our association. Most of these changes are desirable and are supported by the American Bankers Association. I shall explain our reasons for belief that a few are inadvisable and also suggest some addtional amendments which we consider to be desirable.

SECTION 8. CONFLICTS OF INTEREST PROHIBITED (P. 3)

We are in agreement with the purpose of section 8 of the bill which prohibits conflicts of interest. We think it is desirable for the Comptroller of the Currency to have regulatory authority to disapprove the employment of his office personnel by banks under his supervision. However, we suggest that the regulatory authority to supervise former employees should be limited to a period of not more than 2 years after termination of employment with the Comptroller's Office.

Senator ROBERTSON. I may interrupt to say that on yesterday I indicated I felt that the provision in the tentative bill was too harsh and I would recommend to the subcommittee when we draft the official bill that we soften that up and revise it. We will be glad to hear your views.

Mr. LYONS. Thank you.

This regulatory authority over the employment by banks of persons in the Office of the Comptroller of Currency and comparable authority in section 38 (i) of the Federal Reserve Act, section 40 (d) of the Federal Deposit Insurance Act, section 19 (b) of the Federal Home Loan Bank Act, and section 21 of the Federal Credit Union Act, afford the needed protection against possible abuses arising out of the employment of supervisory employees by the supervised financial institutions.

SECTION 803 OF TITLE VIII (P. 247)

It is our view, therefore, that the additional provisions relating to the employment of supervisory personnel in section 803 of title VIII amending sections 217 and 218 of the Criminal Code are unnecessary. We urge that all such provisions in those sections be eliminated in the best interests of the public, of the banks and other financial institutions, and of the supervisory agencies.

In view of your statement as to your recommendation, I will not read the rest of that section, but I would like to add a paragraph to my written testimony, and I shall leave a copy of it with the reporter.

Senator ROBERTSON. All that you have here in your written statement will, without objection, appear in the official record.

Mr. LYONS. Thank you, sir. I will read it.

In connection with section 803, the American Bankers Association also believes that the prohibition against loans is too restrictive. The present proposed language of sections 217 and 218 of the Criminal Code would seem to prevent any employees of one of the supervisory agencies from obtaining a loan from a federally supervised or insured financial institution, at least without obtaining the written approval of the agency in which he is employed. We recommend that the prohibition against loans be limited to a financial institution which the office of the employee has the primary responsibility for examining.

Senator FREAR. That would then permit the auditors or agents of the State banks to borrow from a member bank?

Mr. LYONS. Generally speaking, I would say that the agency that would seem most restricted is the Federal Deposit Insurance Corporation. Under our suggestion a Federal Deposit Insurance Corporation examiner would be permitted to borrow from a national bank, because the Federal Deposit Insurance Corporation has not the primary responsibility for the examination of national banks.

Senator FREAR. Yes. That normally is a member bank, is it not, with one exception?

Mr. LYONS. Yes.

Mr. KING. With one exception.

Mr. LYONS. Excuse me.

SECTIONS 20 AND 21. PREFERRED STOCK. CAPITAL NOTES AND DEBENTURES (PP. 9 AND 10)

The American Bankers Association approves the authority to issue preferred stocks on a nonemergency basis with the approval of the Comptroller of the Currency contained in section 20 and also the authority on the same basis to issue capital notes and debentures incorporated in section 21. National banks should have greater flexibility in meeting their capital requirements. At certain times it may be preferable to obtain capital by other means than by increasing common stock. These sections would permit capital expansion by means of preferred stock or capital notes and debentures if warranted.

SECTION 22 (B). EXCESSIVE DIVIDENDS (P. 11)

The Comptroller has reported that under the present law there is a risk that a self-serving bank ownership could deplete a bank of an unduly large part of its capital funds by an excessive dividend or dividends.

The American Bankers Association agrees that this is a danger which should be guarded against, but in a manner which does not interfere with or complicate the declaration of normal and usual dividends.

We believe that the protection of capital funds is assured by this section. It would require the Comptroller's approval before directors of national banks may declare and pay to stockholders cash dividends which exceed the current year's net profits plus the retained net profits of the 2 preceding years. We, therefore, recommend favorable action on section 22 (b)

SECTION 23. SHAREHOLDERS' LIST (P. 12)

The American Bankers Association favors the elimination from the present law of the right of creditors to inspect the list of shareholders of a national bank as provided in section 23 (a) of the Robertson bill. The abandonment of the principle of double liability and the fact that individual shareholders are no longer personally liable for obligations in the event of a bank failure make this provision unnecessary.

Our association recommends one modification of this section to provide that the list of shareholders of a bank may be inspected by shareholders only for a proper purpose not inimical to the interests of the bank. The absolute right of inspection is both unnecessary and a source of abuse. In some instances individual stockholders have obtained and used the shareholders' list to promote private business interests not related to the bank.

Section 23 (b) adds a new provision requiring a report to the Comptroller of any purchase or sale of 10 percent or more of outstanding shares. Although we are not clear whether this provision will be effective in accomplishing the purpose intended, we have no objection in principle. We do suggest, however, that the report be made within 10 days rather than immediately and that it be limited to purchases and sales of voting stock recorded on the books of the bank, so that the reporting obligation will be manageable. We recommend that the same changes be made in the comparable provisions of section 23 (i) of the Federal Reserve Act (p. 95) and section 27 of the Federal Deposit Insurance Act (p. 164).

Mr. Rogers. May I ask a question?

Mr. Lyons. Yes.

Mr. Rogers. Mr. Lyons, on your recommendation to report within 10 days, when would the 10 days start running?

Mr. Lyons. From the recorded transfer on the books of the bank.

Mr. Rogers. Thank you.

Mr. Lyons. Section 26 (c) on the question of cumulative voting of shareholders:

ELECTION OF DIRECTORS (P. 13)

The American Bankers Association supports this section which would permit cumulative voting of shares of stock for the election of directors of national banking associations when authorized in the articles of association of the bank.

In view of the favorable action by the Senate on S. 256, I shall not read the rest of the detail on that subject.

Senator Robertson. I may point out that the Senate bill received a large majority of the votes when it was voted on, but it was brought up under the suspension of the rules, so it required a two-thirds majority. It just failed of getting the two-thirds majority, or else that would now be the law.

Mr. Lyons. Yes, sir.

Senator Robertson. You may proceed.

Mr. Lyons. Thank you, sir.

SECTION 31. CORPORATE POWERS (P. 18)

The American Bankers Association favors the enactment of section 31 (a) (8). This section clarifies the authority of national banks to make contributions. Existing law provides that national banks may make contributions to "charitable, philanthropic, or benevolent instrumentalities."

The Comptroller has ruled that this statute permits contributions to nonprofit educational institutions. Since this result is clearly desirable, but the interpretation is not completely free from doubt, legislative confirmation would be helpful.

It has been ruled, however, that contributions to chambers of commerce or local industrial development organizations for the purpose of civic improvement are not permitted. We approve the proposal that such contributions should be permitted. National banks as well as State-chartered banks have an interest in the industrial betterment of the communities in which they are located. They should be able, if they so desire, to contribute to programs designed to make the local community more enterprising and prosperous.

The American Bankers Association is in favor of section 31 (a) (9), which authorizes a national bank to grant options to purchase, and to issue and sell shares of its common stock to its officers and employees. The requirement for approval of both the Comptroller and two-thirds of the shares of the bank adequately protects the interests of existing shareholders.

Stock option and stock purchase plans are designed to attract and retain personnel. They also give employed personnel an added incentive to produce. Banks have had difficulty in competing with industry for managerial personnel.

Industry and business have been giving increased attention to stock option and stock purchase plans because of today's highly competitive labor market. In those States where State banks may adopt such plans, there has been considerable interest in stock option and stock purchase plans. National banks without similar authority are at a disadvantage.

Mr. ROGERS. May I interrupt there?

Mr. LYONS. Yes, sir.

Mr. ROGERS. Mr. Lyons, in reference to the contributions to chambers of commerce or local industrial development organizations, yesterday the advisory committee recommended that the word "nonprofit" be deleted.

Mr. LYONS. I noticed that and I see no objection to their recommendation in that regard. The purpose of the contribution is the controlling factor, I should think, whether it is to a nonprofit corporation or one that was organized for profit.

Mr. COCKE. There are cases that could be desirable.

Senator BENNETT. Could you give me an example of a profitmaking corporation to which you would want to contribute?

Mr. LYONS. At the moment I cannot.

Senator BENNETT. I could not think of any yesterday, so I am wondering if we are not straining at a gnat here, because business generally cannot make a contribution to another corporation if it wishes a tax deduction. The fact that the recipient of the contribution is nonprofit is usually the controlling factor. So I have been puzzled about it. If anybody can give me an example, I would appreciate it.

Mr. KING. May I give an example of that, Mr. Lyons and gentlemen?

We had in Los Angeles a parking corporation, which was organized for badly needed parking in the downtown area. A certain amount was contributed and then the banks, among others, were asked for contributions to support the additional capital required. Banks did contribute to that. That was a profitmaking organization, but the banks felt that in order to get it started it was worth a contribution on the part of the banks.

Senator BENNETT. Well, just to argue with you for a second, the banks did it because they assumed it would have a specific value to their depositors and thus might improve their business relationships. So it was done on a different basis than the basis on which you would contribute to the community chest, or some community funds.

Mr. KING. That is true, but this was done for the benefit of the public, and really not for the customer relationships of that particular corporation.

Senator BENNETT. I think you might be opening a door if you permit the banks to contribute to profitmaking corporations. It is hard to know where to draw any line. But I think the matter has been sufficiently discussed, Mr. Chairman.

Mr. LYONS. Thank you.

SECTION 32. DEALING IN SECURITIES (P. 20)

This section contains authority for a national bank, with the approval of the Comptroller, to acquire, for a period of 90 days, stock in another bank as a step in a proposed merger or consolidation. As the Federal Reserve Board has stated in recommendation 60 relating to State member banks, such action is sometimes desirable as one step in the takeover process. The American Bankers Association approves the inclusion of this authority for both national banks and State member banks.

SECTION 33. TRUST POWERS (P. 20)

We believe that the proposal in section 33 carrying out advisory committee recommendation 34 to transfer from the Federal Reserve Board to the Comptroller of the Currency the power to grant national banks the right to act in fiduciary capacities but leaving with the Board the authority over common trust funds of both National and State member banks, is appropriate. The regulation, supervision, and examination of national banks is the responsibility of the Comptroller of the Currency. This includes supervision and examination of trust departments. Through the performance of his regular responsibilities the Comptroller has available the information needed to decide which national banks should be permitted to operate trust departments. We would like to add that the Federal Reserve Board has performed its function with regard to trust powers in a fine manner and that this change is supported only as a more logical allocation of responsibilities.

SECTION 34. MAXIMUM LOAN LIMITATIONS (P. 25)

The American Bankers Association favors the changes made in section 34 with respect to the exceptions to applicable loan limitations. Both subsections (b) (6) (B) and (b) (7) (B) would afford additional desirable credit facilities for agricultural purposes.

Under present law national banks are permitted to acquire obligations secured by shipping documents or warehouse receipts evidencing title to insured, refrigerated, or frozen readily marketable staples up to 10 percent of capital and surplus. In view of the great improvements made by frozen-food processors in methods of processing, freezing, shipping, and storing such foods, the association favors the provision of this section to permit national banks to make loans for this purpose up to 25 percent of capital and surplus.

The association also approves section 34 (b) (7) (B) to permit national banks to make loans up to 25 percent of capital and surplus to dealers in dairy cattle when the obligations arise out of the sale of dairy cattle and bear a full recourse endorsement or unconditional guaranty of the dairy cattle dealer.

Subsection 34 (b) (12) provides that installment consumer paper which bears a full recourse endorsement or unconditional guaranty of the endorser may be acquired up to 25 percent of capital and surplus. However, the limitation of 10 percent of capital and surplus as to the maker will be the only limitation if the bank has evaluated and is relying primarily on the responsibility of the maker and a certification to that effect is retained in the records. This is a desirable amendment to clarify the status of consumer installment paper.

SECTION 36. REAL-ESTATE LOANS (P. 28)

Section 36, title I of the Robertson bill, makes six important improvements to the present Federal law affecting real-estate loans of national banking associations.

1. Under existing law real-estate loans are limited to combined capital and surplus or 60 percent of time and savings deposits, whichever is greater. These limitations are unduly restrictive on the amount of permissible real-estate loans, particularly in some areas of the country where, because of local conditions, time and savings deposits are very low. Therefore, we believe that some additional alternative aggregate limitation is desirable. The additional alternative of 20 percent of demand deposits contained in the bill is helpful, but we think that 20 percent of all deposits would be preferable. We suggest that this alternative be so changed.

2. The revision as to leaseholds permits a national banking association to make a loan where a building is situated on leased property and there is the assurance that the real estate itself is leased for a time which will permit the orderly liquidation of the mortgage indebtedness. Ample time is provided if the lease runs for a period of time 10 years beyond the maturity of the loan. This is a more realistic approach than the time limits contained in existing laws.

3. The authority to make construction loans on industrial or commercial buildings for 18 months where there is a valid and binding agreement entered into by a financially responsible lender to advance the full amount of the bank's loan upon the completion of the buildings will also assist national banks to meet legitimate credit needs arising under modern commercial and business practices. The Federal laws already provide for national banking associations to make construction loans for 9 months on residential and farm buildings. It is equally important that there be some arrangements whereby construction on commercial and industrial properties can be financed until such time as the definitive financing is consummated. Because of the size of the commercial buildings more time is needed and 18 months is considered to be more reasonable. The bank is protected in that upon completion of the building the construction loan will be liquidated by the proceeds of the permanent mortgage. Similar arrangements are permissible under the laws of many of the States and, therefore, this

amendment would put the national banking associations on a comparable basis with State-chartered banks in such States.

4. This section would also increase the aggregate amount of construction loans which a national banking association can hold from 50 percent of its actually paid-in and unimpaired capital to 100 percent of such capital plus 100 percent of its unimpaired surplus funds. The present limitation has been found to be too restrictive under the existing authorization to make construction loans on residential and farm buildings. This difficulty will be made more serious by the new authority for 18-month construction loans on industrial and commercial buildings. We recommend that the increase in the limitation provided in this paragraph be approved.

5. We believe it is reasonable to consider loans to industrial and manufacturing business where payment is expected from the operations of the business to be excluded from the limitations on real-estate loans even though a mortgage on the industrial or manufacturing plant is taken as additional security. In such situations the real estate usually has a relatively small intrinsic value apart from the operation of the manufacturing or industrial enterprise. The real estate does not constitute the primary security for the loan.

Moreover, many State-chartered banks can take a blanket mortgage on real estate and machinery and equipment in connection with such industrial loans without the loans being subect to the strict limitations on real estate loans. This change will, therefore, tend to make national banks competitive with the State-chartered banks.

6. We also believe it is reasonable to except from the limitations on real-estate loans, loans financing the construction of buildings under the Public Buildings Purchase Act of 1954 and under the Post Office Department Property Act of 1954.

We recommend, therefore, that favorable action be taken on all the amendments contained in this section, changing only the alternative aggregate limitation to 20 percent of all deposits.

SECTION 37. LIMIT ON BANK'S INDEBTEDNESS (P. 31)

This section would increase the aggregate permissible amount of a bank's indebtedness from 100 percent of capital to 100 percent of capital and unimpaired surplus. This is a helpful amendment which the American Bankers Association supports. Experience has demonstrated that the present limitation is too restrictive. For example, it prevents banks in a seasonal period of high-credit demands from obtaining sufficient funds from their correspondent banks to meet temporary local needs. This is often true in farm areas where there is a substantial need for credit to finance the marketing of crops.

SECTION 38. HOLDING OF REAL ESTATE (P. 32)

We approve section 38. Under present law, if a bank invests in bank premises more than its capital stock, it must have the permission of the Comptroller of the Currency. This places banks with a small amount of capital stock and a large surplus at a disadvantage when compared with banks with a large amount of capital and a small surplus. Under the amendment, if the bank's surplus exceeds its capital, it can invest in bank premises 50 percent of its combined capital and surplus without securing the permission of the Comptroller. This will permit banks freedom to invest in bank premises an amount which is more in keeping with the total capital investment in the bank.

SECTION 44. ENGAGING IN THE SECURITIES BUSINESS (P. 36)

The American Bankers Association recommends the addition of a new paragraph to section 44 of title I of the draft bill to provide that it shall be unlawful for any institution organized under the laws of the United States to represent that it is a banking institution unless the law under which it is organized expressly authorizes it to engage in the business of receiving deposits or expressly authorizes the use of the word "bank" in its corporate or business name.

The purpose and function of banks have been clearly defined in laws and regulations. In recent years careless advertising and other practices by some nonbank institutions have tended to confuse public understanding. While these practices have not attained general usage, their continuance and spread could result in a loss of public confidence in both the banking system and in other financial institutions.

I might say at that point we have examined the language of Chairman Cravens and his suggested change in this paragraph (b), and we recommend the adoption of the language he submitted.

SECTION 45. ACTING AS INSURANCE AGENT OR BROKER (P. 37)

Section 45 permits national banks to act as an insurance agent or real-estate broker to the same extent as local State banks. At the present time national banks may act as such an agent or broker only in towns of less than 5,000. In many States the State banks are not so limited and it is reasonable to provide that national banks should have the same powers in those States. The section also permits banks originally acting as agents or brokers in towns of less than 5,000 to continue so to act if the town later exceeds 5,000. We recommend favorable consideration of this section.

SECTION 50. CONFIDENTIALITY OF EXAMINATION REPORTS (P. 41)

In order to remove any doubt as to the confidential nature of examination reports and to discourage future attempts at disclosure, the confidential and privileged nature of the reports should be made statutory as provided in section 50 of the National Bank Act and in section 10 of the Federal Deposit Insurance Act. In the interests of uniformity, we believe a similar provision should be in the Federal Reserve Act.

The courts generally have recognized that reports of examinations by national bank, Federal Reserve and FDIC examiners are confidential documents privileged against disclosure except with the consent of the Comptroller of the Currency, the Federal Reserve Board or the Federal Deposit Insurance Corporation Board of Directors. This is sound because the information is given to or obtained by the examiner in confidence and its disclosure would often adversely affect the operations of the bank and the interests of its customers.

In recent years there has been an increase in the number of instances wherein litigants sought through subpena or other means to compel disclosure of these confidential documents. Generally, the litigant has been motivated by a desire to ascertain whether the examiner's report contains criticisms of the management of the bank which might serve the litigant's purpose. This is an obvious violation of the purpose for which examination reports are prepared.

SECTION 51. STATE EXAMINATION OR LICENSE PROHIBITED (P. 41)

Section 51 carries out a recommendation of the Comptroller of the Currency relating to the exemption of national banks from State licensing and examination in connection with carrying on its authorized banking business.

The Comptroller takes the position that this provision is merely declaratory of existing law since he maintains that any attempted State restrictions or limitations on national banks are clearly unconstitutional. Nevertheless, the question is a recurring one which has sometimes required negotiation with State authorities.

Senator BRICKER. There was some trouble in Andrew Jackson's time on that question.

Mr. LYONS. Yes, sir.

The American Bankers Association approves this section of the bill, because the clarification obtained by its enactment should remove any doubts as to the Comptroller's interpretation and minimize the possibility of these difficulties and disagreements from arising in the future.

We are pleased to note that the draft bill does not include the Comptroller's Recommendation No. 45. This would have authorized the Comptroller to permit one national bank to acquire another national bank in the same county if it were in precarious financial condition and continue the absorbed bank as a branch, even though State law would not permit the establishment of such a branch. This would have been, in our opinion, a serious breach in the principle of equality between State and national banks with respect to the establishment of branches.

In conclusion, let me repeat that title I, the National Bank Act, of the Robertson bill is an excellent bill for which the committee is to be commended. I trust that our suggestions for amendments will not serve to obscure our firm belief in the merits of this legislation. We urge its favorable consideration with the few changes we have suggested.

Senator ROBERTSON. We appreciate your endorsement of title I of the bill, subject to the changes that you have suggested.

Are there any questions?

If not, we will be glad, Mr. Miller, to hear your next witness.

Mr. MILLER. Mr. Frank L. King is the next witness, Senator.

Senator ROBERTSON. Mr. King is recognized.

Mr. KING. My name is Frank L. King. I am president of the California Bank, Los Angeles, Calif. My bank is a State member bank of the Federal Reserve System. I am appearing today on behalf of the American Bankers Association to discuss the provisions of title II of the Robertson committee print bill which contains a recodification of the Federal Reserve Act.

We approve generally the provisions of the Federal Reserve Act as set forth in title II of the bill. We believe that it provides a simplified and more workable statute with changes which give recognition to present-day conditions affecting the Federal Reserve System.

We are pleased with the decision of the Banking and Currency Committee not to follow certain recommendations made by the Board of Governors of the Federal Reserve System; specifically, the recommendations of the Board of Governors to subject dividends on Federal Reserve bank stock issued before the effective date of the Public Debt Act of 1942 to Federal income taxation and to provide authority for the revocation of the exercise of trust powers by national banks. We opposed these recommendations in the supplemental statement submitted to your committee on November 28, 1956, and we are glad to see that they are not included in the bill.

We likewise approve the omission from the recodification of the Federal Reserve Act of the authority now contained in section 13 (b) of the act for the Board to make working capital loans to industrial and commercial enterprises. The repeal of this provision is in accord with recommendation 85F of the advisory committee and was also recommended by the American Bankers Association in its supplemental statement.

There are two provisions of the act, however, on which we have specific proposals for changes. These are as follows:

First, reports by State member banks and national banks. We believe that section 23 (b) of the Federal Reserve Act, on page 92 of the committee print, relative to reports by State member banks, should be clarified to make clear that in requiring the publication of reports, the Board may not require the publication of reports of earnings or dividends, and in requiring the publication of reports of condition, such publication shall be required from all State member banks on the same date. We believe that similar clarifying changes should be made in the National Bank Act, section 52, on page 41 of the committee print, relating to reports by national banks.

Earnings and dividend reports should be considered a confidential matter between the supervisory authorities and the individual bank and it should be made certain that the publication of such reports is not authorized. We believe also that a bank could be adversely affected if it were required to publish its report of condition on a date other than that required for the publication of reports by other banks. It would be clearer if the act specifically states that the publication of reports of condition by all banks shall be on the same date, and we so recommend.

We feel that the adoption of the sampling technique, under which the Board or the Comptroller, as the case may be, would have the power to prescribe different forms for reports from various groups of State member banks or national banks, according to their size, location, or other reasonable classification, could be effective, and would serve to cut down the work of some banks, particularly the smaller banks.

Mr. Rogers. Could I ask you a few questions on that part, Mr. King?

Mr. King. Yes.

Mr. Rogers. You see, the law now provides exactly the same as the first three sentences of that section. I wonder if what you are proposing is a change in the present law rather than a change in our proposed bill.

Mr. KING. Our particular concern is that the earnings and dividends report could be published. We think that that might harm the bank and not be in the interests of the public. We think if a small bank in a town were required to report publicly its condition, and a bank that may be larger, or may be smaller, may not be required to report on the same date, that it might be harmful.

Mr. ROGERS. I must reiterate that it is exactly the same. At the present time the Federal Reserve Board requires reports on condition and payment of dividends, and it has authority to publish them. That is exactly what we carried over here. We apply that to national banks also. The language is new as to national banks but as to member banks it is exactly the same. The only new thing we have added, and which you apparently do not question, is the provision for reports on a sample basis.

Mr. KING. We think even reports on a sample basis, if they were required to be published for the smaller banks all at one time, and if the larger banks were not to be published on the same date, or vice versa, that we would recommend against that. We do not object—we think there are advantages in having different kinds of reports and maybe a more simplified report for smaller banks, provided they are not published.

Mr. ROGERS. I would appreciate it if you would have your lawyer look over that section.

Mr. KING. I will ask him to perform that assignment.

Mr. ROGERS. Check it again and give us some language on it.

Mr. KING. We will be very glad to do that, Mr. Rogers. Secondly, in connection with Title II: Service on Federal Reserve Bank Boards and Federal Advisory Council, we recommend the elimination of the limitation on the tenure in office of members of the boards of directors of the Federal Reserve banks to 2 consecutive terms of 3 years each, provided in section 17 (a), on page 85 of the committee print, of the Federal Reserve Act, and the elimination of the limitation on the tenure in office of members of the Federal Advisory Council to 6 full consecutive terms of 1 year each, provided in section 8 of the act, on page 74 of the committee print.

It is believed that any advantage that might be gained by requiring a degree of rotation in the directorates of the Reserve banks is outweighed by the need for preserving the freedom of choice as to the individuals who should serve as directors and the right to continue in office those who are best qualified.

The individual Federal Reserve banks now may place limitations on the tenure in office of their directors. We believe the autonomy of the banks in this respect should be preserved and that the tenure in office of their directors should not be arbitrarily limited by statute. It is likewise deemed desirable that the autonomy of the Federal Reserve banks be preserved in the selection of individuals to serve as members of the Federal Advisory Council.

That completes my testimony, Mr. Chairman.

Senator ROBERTSON. We thank you, sir. Are there any further questions?

Senator BENNETT. May I ask one question, Mr. Chairman?

Senator ROBERTSON. Certainly, Senator Bennett.

Senator BENNETT. Have there been outstanding examples where this privilege of maintaining tenure has been abused?

Mr. KING. I think some districts have different customs. I know in the 12th district, in which I reside, that we have a rule which everybody agrees to that the member of the Federal Advisory Council—and I happen to be a member of that at the moment—is limited to 3 years. When I was appointed the first year I was told that, and that is customary there.

In the past we have had longer tenure of office in the directorate, and I think that is not strictly observed in the 12th district. I think perhaps in some of the other districts, for instance I believe the seventh district has had a member of the Federal Reserve Advisory Council until recently, who happened to be chairman for many years, Mr. Ned Brown, who served more than the 3 years—a good many more than 3 years. So I think it varies from district to district.

Senator BENNETT. I am curious. Do you know why this proposal was included in the bill? Is there any history which would suggest that it is necessary?

Mr. KING. Well, I do not know of any history. I do know that when the Reserve Board submitted their recommendations to this committee, each member of the Federal Advisory Council of 12 unanimously recommended against the matter. The Board did not tell me, and I do not believe they told the Council, why they recommended it.

Senator BENNETT. Usually when a recommendation of this kind comes up there may be behind it an example of an abuse of the unlimited privilege, and I am just wondering whether there was any history in this case.

Mr. KING. I do not know of any.

Senator ROBERTSON. The chairman will say to his distinguished colleague, while we did not go into great detail at the hearings in November, it was naturally assumed when the Federal Reserve Board asked for this change they had a good and sufficient reason for wanting the change to be made. So we put it in the tentative bill.

Senator BENNETT. So there must be some history.

Senator ROBERTSON. When the Federal Reserve Board testifies, we can ask about the history.

Senator BENNETT. Fine.

Senator ROBERTSON. Thank you. Who will be your next witness, Mr. Miller?

Mr. MILLER. Mr. Chairman, our next witness is Mr. D. Emmert Brumbaugh. Mr. Brumbaugh.

Mr. BRUMBAUGH. My name is D. Emmert Brumbaugh. I am president of the First National Bank, Claysburg, Pa.—a bank with resources of $6 million. For many years I have been directly interested in matters of bank regulation and supervision, particularly as they relate to State banks. I served for 4 years as commissioner of banking of the State of Pennsylvania, and while in that capacity also served as chairman of the Federal legislative committee and president of the National Association of Supervisors of State Banks.

I am appearing today as chairman of the committee on Federal deposit insurance of the American Bankers Association to present its testimony on title III of the Robertson bill, dealing with the Federal Deposit Insurance Corporation.

Sections 6 and 7 of the bill (pp. 151–152) provide for a change in the management of the Corporation from the present board of three directors to a single Administrator, and for the creation of an Advisory Board composed of the Comptroller of the Currency, the Chairman of the Board of Governors of the Federal Reserve System, and a State officer exercising functions relating to the supervising of State banks. Other sections of the bill also take account of this proposed change.

If the statute is amended to vest the management of the Corporation in a single Administrator, we believe that a Board of some nature should be established which would have general authority with respect to policies and operations of the Corporation and to which the Administrator would be accountable. We believe further that consideration might be given to the establishment of a bipartisan Board of five members to be appointed by the President subject to confirmation by the Senate, which Board should be constituted with proper authority over the Corporation's policies and operations.

Mr. ROGERS. May I ask a question there?

Mr. BRUMBAUGH. Yes, sir.

Mr. ROGERS. The effect of your recommendation would be to expand the present 3-man board to a 5-man board and eliminate the Comptroller of the Currency. Is that it in a nutshell?

Mr. BRUMBAUGH. That was not our thought at all. The thought of the American Banker's Association was that a Board of this type might be a lot more desirable than to have a Board constituted of the three named members before. Of course, we would have no objection to the Comptroller of the Currency being on that Board as far as the American Bankers Association is concerned.

Mr. ROGERS. Would you consider having a representative of the Federal Reserve Board on that group?

Mr. BRUMBAUGH. We would have no objection to that.

Mr. ROGERS. Should there be a representative of the State supervisory authorities?

Mr. BRUMBAUGH. That is right. We think there should be. This Board should be made up of men of that type, and holding those responsible positions in a bipartisan Board with authority to have some say-so to the management rather than have a manager who would have no one that would have any control over him.

Mr. ROGERS. Under the bill as it now stands the Administrator would have complete policymaking authority.

Mr. BRUMBAUGH. That is right.

Mr. ROGERS. Your thought is to vest in the Administrator just the management functions, and have this Board make the policy for the Administrator. Is that correct?

Mr. BRUMBAUGH. That is correct.

Senator FREAR. May I ask a question?

Senator ROBERTSON. Yes, Senator Frear.

Senator FREAR. Would this contemplated or suggested five-member Board be a full-time Board?

Mr. BRUMBAUGH. This Board would be a full-time Board. The other Board of three would be subject to call. This is a full-time Board.

Mr. ROGERS. In the present bill the Advisory Board is just subject to call.

Senator FREAR. The Advisory Board is subject to call.

Mr. BRUMBAUGH. That is right.

Senator FREAR. But the present Board is certainly full time.

Mr. BRUMBAUGH. Yes.

Senator FREAR. One, the Comptroller of the Currency, is certainly full time, and the other two members are on a salary and work full time and do form the policy of the Federal Deposit Insurance Corporation. They also execute that policy. As I understand it, this Administrator, as far as your recommendations are concerned, as suggested by our counsel, the Administrator will carry out the policies as laid down by this five-man Board?

Mr. BRUMBAUGH. That is correct, as to the three-man Board.

Senator FREAR. Thank you.

Senator BRICKER. Then you distinguish entirely between the Advisory Board and the Board of Management which you recommend?

Mr. BRUMBAUGH. That is correct.

Senator BRICKER. Do you envision that Board of five which you recommend would be constantly in session, giving full time to the affairs of the Insurance Corporation?

Mr. BRUMBAUGH. That is correct. Yes.

Senator BRICKER. If that were true then you would not want to exempt the Comptroller of the Currency and the Chairman of the Board of Governors of the Federal Reserve.

Mr. BRUMBAUGH. We do not exempt them. We said we have no objection to them being appointed by the President.

Senator BRICKER. But they cannot give full time.

Mr. BRUMBAUGH. And we have not been thinking of them as members of that Board, but nevertheless we have no objection to them.

Senator BRICKER. If they were members of the Board you would not have the kind of Board you envision here in your recommendation.

Mr. BRUMBAUGH. That is correct.

Senator ROBERTSON. The chairman would like to point out if the Federal Deposit Insurance Corporation as constituted carries out the study recommended by our advisory committee yesterday, and tries to find out what is the basis of the liability they are going to assume and how much it is going to amount to with respect to assessments, the board will have in the first year plenty for all of them to do.

Mr. BRUMBAUGH. That is right.

Senator ROBERTSON. Are there any other questions?

Mr. BRUMBAUGH. Section 9 (b), page 153, relates to submission and publication of reports of condition by insured State nonmember banks. We propose an amendment to provide that any publication so required be on the same date for all such banks. This will make it consistent with our recommendations with respect to reports of condition by national and State member banks.

Section 10, page 153, provides that Corporation records pertaining to any insured bank may not be disclosed without prior consent of the Corporation.

This provision corresponds to section 50 of title I as relates to national banks. As stated in our testimony with respect to the national bank provision, we favor this protection of confidential records.

Section 16 (b), page 157, provides that any insured bank need not maintain records pertaining to its assessment computation for a period in excess of 5 years.

We favor this provision because we believe that 5 years is a reasonable period for the Corporation to verify the correctness of assessment computations. The insured banks should be free thereafter to dispose of detailed records which would serve no other purpose than verification.

Section 18, page 159, sets forth the basis for determination of assessment credits to insured banks. The bill retains the existing provision that 40 percent of the Corporation's "net assessment income" be transferred each year to the deposit insurance fund and that the balance be credited pro rata to the insured banks. We favor an amendment to change from 40 percent to 20 percent the portion of "net assessment income" to be transferred to the fund.

This would enable the Corporation, under prevailing conditions, to cover its expenses and losses and make an annual addition to the fund of about $70 million. The Corporation would receive about $40 million from investment income and $30 million from the 20 percent of "net assessment income." This $70 million annual addition to the fund is equal to 3½ times the net insurance losses sustained by the Corporation in its entire history.

Testifying in 1950 on the Deposit Insurance Act, which set up the present basis of assessment credits, the association recommended that when the surplus reached $1.5 billion, provision should be made for adjustment of the percentage of "net assessment income" to be credited to the banks. That point was reached in 1954. The fund has since continued to grow, currently at a rate of about $100 million annually, and now approximates $1¾ billion.

We reiterate the view expressed in 1950 that—

> the deposit insurance fund should not be permitted to grow indefinitely at more than a nominal rate.

The first line of defense for the protection of bank deposits is the capital investment in our banks. A moderation of assessments will help to build up capital funds. We feel that the strength of our banks—indeed of the deposit insurance fund itself—is better served by adding more funds to bank capital, which can help to make the Federal Deposit Insurance Corporation assistance unnecessary.

Section 23, page 162, provides that there must be prior written consent by the appropriate Federal bank supervisory agency to any proposed merger, consolidation, or assumption transaction between insured banks.

The association supports this section of the bill which contains the substance of the Fulbright-Capehart bill, S. 3911, 84th Congress, approved by the United States Senate in 1956. We supported S. 3911. In the statement to the Senate Banking and Currency Committee on November 7, 1956, we recommended inclusion of this provision. We believe that the authority over bank mergers is properly within the jurisdiction of the bank supervisory agencies and that the law should be specific to that effect.

Section 29 (a), page 165, provides for a shortening to 20 days of the existing 120-day period now permitted for the correction of unsafe or unsound practices by an insured bank, in cases where it is determined that the insurance risk is unduly jeopardized. It is further provided that any hearing subsequent to the 30-day notice of intention to terminate the insurance status of a bank shall be held in accordance with the Administrative Procedure Act, and that the review by the court shall be upon the weight of the evidence.

We believe that this amendment to existing law would strengthen the power of the Corporation to act promptly and decisively in the public interest.

Section 30 (b), page 168, prescribes that payment of deposits of a closed insured bank shall be made by the Corporation either by cash or by a transferred deposit payable on demand in a new bank or another insured bank.

We believe that this provision should be amended to eliminate the phrase "payable on demand" and to provide instead that the transferred deposit be payable on the same basis as called for in the original arrangement between the closed bank and the depositor. We do not consider it either practical or appropriate to change the status of any class of accounts, as for example savings deposits or time certificates of deposit, to the demand category.

Section 2 (1), page 149, should accordingly also be amended to eliminate the word "demand" from the definition of "transferred deposit." That is the end of my testimony. Thank you.

Senator ROBERTSON. Are there any questions?

We thank you. May we have your next witness, Mr. Miller?

Mr. MILLER. Our next witness is Mr. Paul A. Warner, Mr. Chairman.

Senator ROBERTSON. We will be glad to hear you, Mr. Warner.

Mr. WARNER. Mr. Chairman and members of the committee, I am to testify with respect to the Federal Home Loan Bank System.

My name is Paul A. Warner. I am president of the Oberlin Savings Bank Co., Oberlin, Ohio, which is a small commercial bank. We have slightly over $5 million of deposits, roughly half of which are savings deposits. Some years ago, I served as savings and loan supervisor for the State of Ohio, and subsequently as chief examiner of the Federal Home Loan Bank Board. I appear today as chairman of the committee on Federal legislation of the savings and mortgage division of the American Bankers Association.

Speaking as a country banker, and from legislative experience in the State of Ohio, while I was superintendent of the savings and loan association there, I commend your committee for the fine work it has done.

The first thing I want to take up is something that is not in the committee print of the bill, but it is called to attention by the hearings where it was brought up, and that is with respect to title IV, the Federal Home Loan Bank Act.

Near the close of the hearings before this committee on November 10, 1956, Everett Reese, president of the Park National Bank, Newark, Ohio, and a member of the Advisory Committee, made the following observation:

> Senator Robertson, I would just like to say the banks and savings and loan associations have been competing with each other for many years, and they will continue to do so. It seems to me this creates a great opportunity for these two industries or professions to begin to do constructive thinking, to have a recognition of the qualities of the other and an understanding that each of us is going to continue to function and to develop a greater respect for each other in the different industries and not begin to hash over and regurgitate things that have happened in the last 50 years. It seems to me this study gives us a great opportunity to try to do some things immediately in line with Senator Robertson's suggestion that we stay within the field where that can be done.
>
> Of course, there will be competition. There will be overlapping. But as near as we can, we must try to do constructive things in the banking business and

try to get constructive legislation in both fields so that we have a clear line of demarcation. The word "bank" means something to people in the United States and it means to a great extent a commercial bank.

We have in the Federal Home Loan Bank Board the word "bank" right in the name of the central institution. We used the word "bank," and it is probably a misnomer right at the start.

Immediately following this statement, Albert Robertson and Ira Dixon, chairman and member, respectively, of the Federal Home Loan Bank Board, stated that they agreed with Mr. Reese.

The next statement was made by Mr. Bubb, chairman of the savings and loan subcommittee of the Advisory Committee and president of the Capital Federal Savings & Loan Association, Topeka, Kans. Mr. Bubb stated:

I think we can bring about very easily what Mr. Reese has in mind, what comes out of this committee hearing and the Senators' interest, together with the fact that we have a Home Loan Bank Board of which we can all be very proud—I don't think they care whether the name "bank" is in it or not. We can all come out under your line of reasoning, Mr. Reese. I know we will all be very happy, and I will certainly do my part, for one.

In view of the unanimity of opinion expressed by these men—and in line with the idea that you accomplish things by doing things with people and not to them—we strongly urge the change in the name of the Board to the "Federal Home Loan Board," a change which we deem fundamentally important. It would follow that individual associations would be members of the "Federal Home Loan System." This would be parallel to the terminology used in the Federal Reserve Act and avoid a great deal of confusion.

Mr. Rogers. Mr. Warner?

Mr. Warner. Yes, sir.

Mr. Rogers. Have you considered what you would call the Federal home-loan banks—the regional banks?

Mr. Warner. There would be no objection to calling the regional banks, "regional banks."

Mr. Cocke. "Regional units" has been suggested.

Mr. Rogers. Pardon me.

Mr. Cocke. Federal home-loan regional unit.

Mr. Warner. The difficulty arises out of a number of things. One is that the Federal savings and loan associations are Federal instrumentalities under the way it is set up now. There is a great deal of confusion in the public's mind and often in the minds of the operators of these institutions. I have one very fine and unstanding competitor who constantly refers to his institution as a bank, and he does it 5 or 6 times in 3 minutes when you are talking to him. Also I have a niece who worked in one of the building and loan associations in Columbus and she always says "the bank." It is quite natural that that should come about because of this confusion which arises. Maybe it is semantics, but it is awfully confusing.

Mr. Rogers. Do you not think this proposal would only be the very beginning if you want to change that situation? Is not the answer to it really education campaigns by the American Bankers Association?

Mr. Warner. I think when we are working together here we had better stay a working group rather than to start out trying to start something that may be construed as being "anti," because essentially we are not against an industry that has done a good job.

Mr. Rogers. Thank you.

Mr. WARNER. Title V, Federal Savings and Loan Association Act:

SECTION 5. FEDERAL SAVINGS AND LOAN ASSOCIATIONS

Paragraph (g) of this section, page 209, reads in part as follows:

> * * * and all shares of such associations shall be exempt both as to their value and the income therefrom from all taxation * * * now or hereafter imposed by the United States; * * *

Although this provision is the same as in the present law, its reenactment as a part of this recodification could have the effect of repealing the provisions of the Public Debt Act of 1942 which subject dividends on the shares of Federal savings and loan associations issued after the effective date of that act to Federal income taxes. Therefore, appropriate language should be included in paragraph (g) of section 5 to make it clear that the provisions of the Public Debt Act of 1942 continue in effect.

SECTION 6. FEDERAL SAVINGS AND LOAN BRANCHES

The committee print of the omnibus bill, page 211, includes the language of S. 972, as passed by the Senate in the last session.

Inasmuch as there is at the present time no statutory provision for branches of Federal savings and loan associations, we would rather see this provision enacted than no provision at all.

However, we believe it would be in the public interest for Congress to espouse the principle of a dual savings and loan industry just as Congress has espoused the dual banking system of national and State-chartered banks. Nearly a century of administration of national banks and the much longer experience of balancing States' rights and Federal prerogatives, have proved eminently successful. Under this principle a national bank has the same branch powers as a State-chartered back. By the same token, we believe, Federal savings and loan associations should have the same branch powers as State-chartered savings and loan associations.

In some States the savings and loan branch powers are greater than the powers of commercial banks; in some States the powers are the same; and, in other States the branch powers are less. It certainly is not proper to give Federal savings and loan associations the most favored treatment with respect to branch powers of State-chartered savings and loan associations, mutual savings banks and commercial banks, particularly where by law or practice the State has established different branch requirements for the different types of financial institutions organized under its laws.

We, therefore, recommend that the States rights principle be observed by giving to Federal savings and loan associations the same branch powers as are given to State-chartered savings and loan associations in each State.

SECTION 7. RESTRICTIONS ON ASSOCIATIONS, DIRECTORS, AND OFFICERS

The law prohibits Federal savings and loan associations from accepting deposits. Therefore, the word "deposits" should be deleted from paragraph (c) of section 7, page 213, which reads as follows:

> No Federal savings and loan association shall pay to any director, officer, attorney, or employee a greater rate of return on the shares, deposits, or other

accounts of such director, officer, attorney, or employee than that paid to other holders of similar accounts with such association.

With the deletion of the word "deposits" we could approve this section.

Title VI, Federal Savings and Loan Insurance Corporation Act:

SECTION 406. PAYMENT OF INSURANCE

This section, page 223, provides that in the event of a default by any insured institution, the Federal Savings and Loan Insurance Corporation could make payment either in cash or "by making available to each insured member a transferred account payable on demand in another institution." The American Bankers Association believes that where a transferred account is made available in another institution it should be in the same type of account as in the defaulted institution. This is consistent with our recommendation concerning payment of insurance by the Federal Deposit Insurance Corporation. The words "payable on demand" should be deleted from this section.

That is the end of my testimony, sir.

Senator ROBERTSON. We appreciate very much your endorsement of our proposal to codify the banking laws, and we are very happy to have both of your fine Ohio Senators on this committee. Are there any questions?

Senator BRICKER. No, except to say Paul Warner is a great favorite of the State of Ohio, and I well remember him at the time I was the attorney general of the State.

Senator ROBERTSON. I am sure he was because as I say this American Bankers Association is a great association and he would not have been picked if he had not been good.

Mr. MILLER. Mr. Chairman, our concluding statement will be made by the president of our association, Mr. Erle Cocke.

Senator ROBERTSON. We will be glad to hear from him.

Senator FREAR. May I just ask one question of Mr. Brumbaugh, Mr. Chairman?

Senator ROBERTSON. Yes, sir.

Senator FREAR. When were you bank supervisor of the State of Pennsylvania?

Mr. BRUMBAUGH. 1947 to 1951.

Senator ROBERTSON. Mr. Cocke.

Mr. COCKE. I want to express the appreciation of the American Bankers Association for the opportunity afforded by the committee to present the testimony which you have heard this morning.

Our presentation will fulfill its purpose if it proves helpful to the committee in your further consideration of the proposed legislation.

This bill is a landmark in our Nation's financial history. It will rank in importance, upon passage, with such fundamental improvements as the National Bank Act and the Federal Reserve Act.

Because it seeks to make our banks more useful to the public by modernizing the laws governing them and thus providing them with greater flexibility, we stand firmly and squarely behind the objectives of this committee print of the bill.

As you have observed in the testimony presented this morning, we are in agreement with almost all of the proposals contained therein. Still, as you gentlemen are greatly aware, on any piece of "omnibus" legislation, perfect agreement never can be achieved. The legislative process itself is naturally a process of compromise. We have found it necessary, therefore, not to agree with a few provisions of this committee print. We believe that whenever particular provisions appear to interfere with the historical intent of the Congress to guard the soundness of the banking system in the public interest, it is our duty—as representatives of the banking industry—to make our position clear.

It was the wise intent of the authors of this bill, furthermore, to confine its scope to a largely technical recodification of the financial laws. Since financial legislation covers so wide and detailed an area, it would not have been possible, in a relatively short time, to develop a thorough discussion of views regarding broad questions of financial policy on which there might be broad and important differences of opinion.

This effort to recodify and modernize existing statutes will make a positive contribution to a smoother functioning of our financial system and we, therefore, urge its speedy enactment. Nevertheless, it is evident from the record already presented to the committee by various groups that more remains to be done beyond the scope of this bill.

The financial system in recent decades has become very complex. The development of various institutions, the use of Government credit in different ways, and the evolution of the concept of monetary management are just three examples among many factors in recent years which have reshaped our financial system and which suggest the desirability of a reexamination or study of public policies with respect to financial institutions.

We believe that an objective study by a qualified commission would help to develop a clearer understanding of the system and, therefore, we would favor the creation of such a commission to cover the ground not contained in this, the Robertson bill, as we know it.

Let me again emphasize, however, that the American Bankers Association heartily and enthusiastically supports the committee print under consideration, with the amendments proposed by us, and hopes that the Congress will see fit to enact it without waiting for the findings of a longer-range study commission, if one should be established.

Mr. Chairman, again we want to thank you and say that if any further questions develop in the minds of any members of this committee we will attempt to give you our thinking to the best of our ability. It is a privilege to have been before you.

Senator ROBERTSON. We thank you, Mr. Cocke. Your name is a very ancient and honored one in Virginia. I would like to flatter Virginians by saying that I hope you are kin to some of them.

Mr. COCKE. Well, the rich part of the family lives in Virginia.

Senator ROBERTSON. I read a little preview of what we are trying to do here, in the January 18 issue of my friend David Lawrence's fine magazine, U. S. News & World Report. He said:

> The plan is to rewrite and modernize the country's banking laws. Offered by Senator A. Willis Robertson, Democrat, of Virginia, the effort is presented in what is expected to be one of the biggest and most controversial bills of this session of Congress.

That may be true, but it certainly gratified me and other members of this subcommittee who want to put this thing through to know that we have behind us in this effort an organization like the American Bankers Association.

Mr. COCKE. We are at your service, sir.

Senator BENNETT. May I ask another question or two of Mr. Warner particularly?

Mr. WARNER. Certainly, Senator.

Senator BENNETT. I was interested particularly in the fact that you included in your testimony this statement of Mr. Reese, and you are interested in removing the word "bank" from the name of the Federal Home Loan Bank Board. Are we to assume that the American Bankers Association is anxious to maintain the identity of these two loaning systems and at the same time anxious to eliminate overlapping, or what they might consider to be unfair competition?

I am going to ask you a general question. You have suggested one very minor approach to what might be a complete separation of these two systems—the elimination of the word "bank" from the name of the Board. I am facing a problem in my own State in which a bank is advertising that it will accept not deposits, but investments from people who are members of a savings association. It projected an ad in 2 parallel columns saying, in effect, "We can get you 3 percent interest on money deposited in our bank and we will accept money for a building and loan association and get you 3½ percent." The two are published parallel to each other.

Would you be interested in legislation which would make that kind of a thing impossible and which would separate the operation of the two systems in the mind of the public to that extent?

I have another instance in my own State where a building and loan association operates in the banking room of a bank so that when a person comes into that room he may go to one window as a bank depositor, or another window as a member of a Federal—or at any rate a savings and loan association. I do not know whether it is Federal.

It is raising a great question in my mind as to the extent to which we should go in this legislation to separate these two systems of savings. Does anybody have any comment on that?

Mr. WARNER. Well, Senator Bennett, I have had a little experience along that line. When I was a State bank examiner in Ohio; that is, before I was the superintendent of loan associations for the State, I had assigned to me as one of my duties the examination of the banks which were affiliated, in the manner that you speak, with the building and loan associations. It was very confusing because there were a good many things that could and did happen as a result of those close affiliations and those confusing circumstances.

I believe that it is a good thing to have them clearly defined. It is good for both institutions. One of the reasons why it is good is that, for instance, as supervisor of the building and loan associations I had many people come into my office—this was in 1933 and 1934, and you know the situation where everything was frozen up—and they wanted to know, "Why it is that the legal authorities permitted me to be deceived in this manner? I thought that I was diversifying my investment." And they were crying about things that, to a great extent, I thought they should have known about.

On the other hand, when we examined the advertisements in the newspapers in the city of Dayton, we found "deposits" and "shares" used without any regard to which they were. They used "interest" and "dividends" in their advertisement without any regard to what they were. So how could the public help being confused. And believe me, they were confused.

I think it is a good thing to have both industries kept in such a position that they are not confused.

There are other reasons for that—and I will use the city of Dayton again as an illustration. We have building and loan associations which paid 6 percent interest on deposits—our associations in Ohio—and some of them will accept deposits. We had other large and good building and loan associations which paid dividends on shares in that city. They attracted money from other associations from over the State who were only, perhaps, paying 4 percent, and they got a large concentration of money.

Then they went on notice in 1930 and they proved a burden in taking care of the fellow who thought what he had was a savings account to take care of him in an emergency. That burden was thrown on to the banks. Then the city correspondents of the banks, and city banks who had, to a large extent, the advising of national accounts, said, "Look, that situation in Dayton is getting bad. You had better pull your deposit out of there before it gets worse." And it did get worse and they did pull their deposits out. Then we had more frozen assets in the building and loan system there than we had in the banks to take care of it. Much more. It was just a situation that was really terrible.

Senator BENNETT. That was related to a situation that was terrible wherever people made deposits or purchased shares.

Mr. WARNER. That is true.

Senator BENNETT. But I am interested in terms of this bill, and I would be grateful—probably you would not want to make a statement on it at this time—but I would be personally grateful to have a statement from the American Bankers Association on the extent to which these two systems should be separated.

This current situation is an interesting twist in my State because it is the banker who has moved into the building and loan field and is apparently willing to accept building and loan deposits, or contributions, or payments for investment through his teller banking wicket.

Senator ROBERTSON. If the Senator will yield there. You referred to an advertisement in your State that would "give you 3 percent in our bank or 3½ percent in our savings and loan"?

Senator BENNETT. That is right. Parallel, in the same ad in the same paper.

Senator ROBERTSON. Are those advertisements published by a bank holding company?

Senator BENNETT. Yes.

Senator ROBERTSON. The Senator from Utah was a patron of the bill last year known as the Bank Holding Company Act of 1956.

Senator BENNETT. That is right.

Senator ROBERTSON. After a little effort and a little delay we got it enacted into law and put the supervision under the Federal Reserve Board. The coauthor of that bill, the acting chairman of this investigation, has called on the Federal Reserve Board to investigate what this bank holding company is doing out there and report to us.

Senator BENNETT. I realize this is a specific and single instance, but I also realize there may be a question here that should be gone into while we are working on this general problem of the recodification of the banking laws.

Mr. WARNER. May I say it would be very helpful to spell out, if possible, in this bill just what each of these institutions is, so that it can be explained to the public. It is very difficult under existing conditions.

Senator ROBERTSON. Off the record.

(Discussion off the record.)

Senator ROBERTSON. Gentlemen, we want to thank you for your appearance here and thank you for the cooperation you have given us. And, as I call to your attention the estimate that this might be a controversial bill, we hope to have your continued cooperation until we get it through the Senate.

Mr. COCKE. We are subject to your call.

Senator ROBERTSON. The next witness tomorrow will be a representative of the Independent Bankers Association, another fine banking group.

The committee will stand in recess until 10 a. m. tomorrow.

(Whereupon, at 11:35 a. m., the subcommittee recessed until 10 a. m. the following day, Wednesday, January 30, 1957.)

STUDY OF BANKING LAWS

(Financial Institutions Act of 1957)

WEDNESDAY, JANUARY 30, 1957

UNITED STATES SENATE,
COMMITTEE ON BANKING AND CURRENCY,
SUBCOMMITTEE ON BANKING,
Washington, D. C.

The subcommittee met, pursuant to recess, in room 301, Senate Office Building, at 10:05 a. m., Senator A. Willis Robertson (chairman of the subcommittee) presiding.

Present: Senators Robertson, Frear, Bricker, and Bennett.

Senator ROBERTSON. The subcommittee will please come to order.

The first witness today is Mr. Ben DuBois, who will testify on behalf of the Independent Bankers Association.

The Chair is pleased to recognize Mr. DuBois at this time.

STATEMENT OF BEN DuBOIS, SECRETARY, INDEPENDENT BANKERS ASSOCIATION

Mr. DUBOIS. Mr. Chairman, it will be necessary to use the committee print in following my testimony, and I assume that the committee members have it before them.

Senator ROBERTSON. That is correct.

Mr. DUBOIS. As the chairman stated, my name is Ben DuBois. I am secretary of the Independent Bankers Association, and our office is in Sauk Centre, Minn.

The executive council of the association recently had a meeting for the purpose of making a study of the proposed legislation that is being formulated by your committee.

We believe that this banking study being carried on by your committee is timely and of great importance. You, Mr. Chairman, your committee, your staff, and the advisory committee that was appointed have all done an excellent job. In general, we are in favor of the legislation proposed in the committee print.

With few exceptions, the membership of our association is composed of the Nation's small banks. We have as members a few large banks—banks that believe in our old system of independent banking. We do not, however, have any members in the billion dollar class.

The association, therefore, is obligated to its grassroot membership to oppose any proposals that might be detrimental to either independent banking or to the dual system of banking.

Of late, it seems to many of us that the three Federal supervisory agencies have become friendly to what we might call system banking—big organizations with many branches or subsidiaries.

We think the record shows that the Comptroller of the Currency is quick to grant branch-banking permits and slow to curtail bank mergers. The workable relationship that formerly existed between the Comptroller's Office and the supervisors of State banks has undergone a change.

The Comptroller appears to have encroached upon the prerogatives of State supervisors. He has construed State statutes in a way that gives national banks permission to branch, a change from the procedure of the past. Where a State supervisor has prohibited a State institution from merging with a national bank, the Comptroller has been quick to permit the State institutions to nationalize.

At the present time, two States, New York and Massachusetts, are attempting to secure stopgap legislation that would prevent mergers. In Massachusetts, legislation is proposed with support of both the Governor and the commissioner of banks that would prevent mergers of national or trust banks across county lines without State approval.

Since I wrote this, Mr. Chairman, the State of Massachusetts did pass legislation that stopped the First National Bank of Boston and the Granite National Bank of Quincy from merging. It was a night session. I understand that the legislation was passed after midnight.

Mr. ROGERS. Mr. DuBois, I think New York yesterday passed the other bill.

Mr. DUBOIS. Well, I am a little behind. Thank you.

In New York State, legislation is proposed, supported by the Governor and the superintendent of banks, that would stop the proposed holding company of the First National City Bank of New York from stepping across bank district lines and securing in Westchester County what is now a State bank but with the aid of the Comptroller to be changed into a national bank.

As Mr. Rogers said, the laws in New York and Massachusetts have passed.

Bankers in Pennsylvania are in a tumult due to conflicts between the Comptroller's office and the State banking department.

Those who want a change in our banking system, those who feel that great financial empires should be established, those who desire monopoly in banking find it more practical to proceed by piecemeal legislation, knowing that if they asked directly for what they really want, what they hope to ultimately secure, their ambitions would meet with failure.

This country has been well served by its unique American system of banking—a diffused ownership of banks, management by people of the community, responsive to the needs of the community, part and parcel of the community and directed by a sovereign board of directors.

We firmly believe our old system of banking is much preferable to any multiple system of banking where large numbers of banks or offices are under the control and direction of a distant head office.

Without protective legislation, our old system of banking will gradually be taken over by some form of monopolistic banking. This, we believe, would be extremely detrimental to the well-being of our people and would foster an undemocratic economy that might seriously affect our political democracy.

With what we have just said as a background to our banking philosophy, we would like to proceed to suggest some changes in the committee print.

On page 4 of the committee print, chapter 3, section 12, we quote:

> Associations for carrying on the business of banking under this title may be formed by any number of natural persons, not less in any case than five.

This language was contained in the National Bank Act as passed in 1863. In that act, each national bank was to be a unit bank, a community bank, owned and operated by people of the community. We would not want the statement we quoted to be changed, but we desire to call your attention to the fact that the spirit, at least, of the original National Bank Act has been seriously violated.

It has been the practice for a bank holding companying seeking a national bank charter to get five natural persons to make application for a charter and the charter is usually granted. The Comptroller of the Currency knows that these five individuals are requesting the charter for the holding company and that the holding company will own practically all of the stock of the bank. In some instances there may be strings on the stock of the applicants.

We understand the Comptroller is loath to charter a national bank if control is in 1 or 2 individuals. Why should a corporation have advantage over individuals?

At the time the National Bank Act was passed, the sponsors of this legislation remembered well the First and Second Bank of the United States, how the Second Bank became a central bank with branches and became abusive of its power. The framers of this legislation wanted to produce a system of diffused banking, each national bank independent and operating under its sovereign board of directors within the law and framework of regulations.

In 1911, Frederick W. Lehmann, the then Solicitor General of the United States, prepared an opinion that stopped a national bank in New York City from forming an investment corporation. Unfortunately, this opinion was buried in the Comptroller's office. We do not hold Mr. Gidney responsible for this burial.

Senator Carter Glass unearthed this opinion in 1932. He referred to it as having been suppressed at the time it was rendered and ordered it printed in the 1932 Congressional Record. If this opinion had not been suppressed, it is doubtful if the trend toward banking monopoly would be as pronounced as it is today.

Page 15, section 28, "Oath of Directors," we quote:

> * * * and that he is the owner in good faith, and in his own right, of the number of shares of stock required by this act, subscribed by him, or standing in his name on the books of the association, and that the same is not hypothecated, or in any way pledged, as security for any loan or debt.

We believe this statement is intended to convey the fact that the qualifying shares are fully owned by the directors and that the Comptroller of the Currency should see to it that these qualifying shares are not covered by any option agreement.

We would like to see this language changed to read as follows: After the word "hypothecated," there should be added:

> in any manner whatsoever, and that no agreement exists between the director and any person or corporation limiting his right to sell or dispose of such stock and said qualifying shares of stock be in his possession.

For the record, we are handing you a reprint from the Independent Banker of an article by Emil E. Placek, our State director in Nebraska, containing an option agreement that has been used and probably is still used by one of the bank holding companies. We believe that the last phrase of our proposed change—that the stock must be in the possession of the director—is pertinent,

(The article referred to follows:)

Legality of Chain Bank Stock Option Deals Challenged

By Emil E. Placek, chairman of the board, First National Bank, Wahoo, Nebr.

(Editor's Note.—Challenged in this provocative article by Mr. Placek is the legality of stock option agreements signed by directors of holding company banks. He urges independent bankers to back the Burdick bill requiring that at least two-thirds of the outstanding shares of stock in a bank be owned by natural persons. Mr. Placek is Nebraska director of the Independent Bankers Association.)

The National Banking Act was passed in 1863 and created the office of the Comptroller of the Currency. The act authorized the organization of a local national bank by any number of natural persons, but not less than five in number, to engage in the business of banking in any State or Territory. No bank so organized could issue or circulate currency unless it was secured by Government securities.

Banks created by the National Banking Act were designed to be local institutions and independent of each other, but under the control and supervision of the Government.

The United States Compiled Statutes of 1901, section 5133, provide for the formation of national banking associations by natural persons and specifies that articles of organization were to be signed by the persons uniting to form the association.

If only "natural persons" can organize a national bank, the logical presumption is that only natural persons can operate a bank.

Section 5134 of the 1901 compilation provides necessary requisites of organization such as name of bank, place of business, location, name and place of residence of each stockholder and number of shares held by each.

Section 5140 specifically provides that every director must own, in his own right, at least 10 shares of the capital stock of the association. Without such ownership, he cannot be a director. The director, too, must take an oath that the stock is not hypothecated in any manner whatsoever.

FALSE SWEARING CHARGED

My contention is that a director in a bank owned and controlled by a bank holding company, to whom stock is issued under an option agreement, is guilty of perjury when he swears his stock is not hypothecated in anyway.

Bank holding companies were organized to evade and circumvent the National Banking Act and the laws of the various States which prohibit branch banking. A bank holding company buys all of the stock of a bank and then issues qualifying shares to dummy directors with an option agreement giving the holding company the right to repurchase the stock.

Such stock must immediately be endorsed by the dummy director and be delivered to a bank owned and controlled by the holding company. There the stock is held in escrow, so the dummy director never has possession of the stock certificate.

If the holding company chooses to exercise its option to purchase, it may do so simply by mailing or delivering to the bank having the stock in escrow a notice of intent to purchase, accompanied by payment of the purchase price.

The stockholder, or dummy director, is not even notified, except that his services are no longer required. For his stock he receives only the amount originally paid in. He gets none of the accumulated profits earned during the period of his employment. He does not even get the money he paid in until he surrenders his copy of the option agreement.

If the stockholder dies while the stock still is held in escrow, the stock does not become part of his estate. The holding company exercises its option and returns the purchase price to the estate.

OPINION BURIED

On November 6, 1911, Frederick W. Lehmann, in his capacity as Solicitor General of the United States, delivered an exhaustive opinion and held that holding companies are illegal. For some unknown reason, the opinion was pigeonholed. Finally, after 20 years, the opinion was ordered printed in the Congressional Record at the request of Senator Carter Glass of Virginia.

Since Congress recently passed legislation regulating bankholding companies, it may be necessary to pass further legislation requiring that at least two-thirds of the outstanding shares of stock in a bank shall be owned by natural persons.

Such a bill has been introduced in the House by Representative Burdick of North Dakota. The bill is H. R. 7056. It is up to the independent banks of the Nation to press for passage of such a bill.

The only other alternative is to bring an action charging that directors in banks owned by a holding company are not qualified directors, because they do not own the stock in their own right under the option agreement they are required to sign.

The proper procedure would be for the Comptroller of the Currency to have the Department of Justice bring such an action.

The Comptroller and the Attorney General take the position, however, that the question was settled in the Federal case of *Transamerica Corporation* v. *Parrington, et al.* In this case, the stockholder had possession of the stock, which is not true in the option agreements being signed now. Furthermore, the case was not appealed to the United States Supreme Court, which should pass on the whole matter.

After reading the *Transamerica* v. *Parrington* case, I am firmly convinced it was a friendly suit, and for that reason there was no appeal.

> (EDITOR'S NOTE.—Reproduced below is a copy facsimile of the agreement cited by Mr. Placek in his article. The copy was obtained from the office of J. L. McLean, director of banking, Lincoln, Nebr., where it is a public record. The italic, for emphasis, was supplied by Mr. Placek.)

THIS AGREEMENT, made and entered into this ______ day of ________________, 19____, by and between NORTHWEST BANCORPORATION (hereinafter called the "Company"), party of the first part, and ________________________________ (hereinafter called the "Shareholder") party of the second part,

WITNESSETH THAT:

WHEREAS the Company is the owner of a substantial amount of the common stock in ____ (hereinafter called the "Bank") and has this day agreed to sell and assign to the Shareholder certain shares of said stock (Said shares hereby so sold being hereinafter sometimes called "Shares of Stock"), for the consideration hereinafter set forth, and

WHEREAS as an inducement to the Company to sell said Shares of Stock to the Shareholder and as a part of the consideration for the sale thereof to him, the Shareholder is willing to make the agreements and promises hereinafter contained,

NOW, THEREFORE, in consideration of the premises and other good and valuable considerations, the receipt and sufficiency whereof are hereby acknowledged, IT IS AGREED by and between the parties hereto as follows:

1. The Company does hereby sell and assign to the Shareholder ________ shares of the common stock of the Bank and contemporaneously herewith has delivered to the Shareholder stock certificate No. __________ issued by said Bank for said Shares of Stock.

2. The Shareholder does hereby purchase said Shares of Stock and contemporaneously herewith has paid to the Company as the purchase price thereof the sum of ____ Dollars ($____________________).

3. (*A*) *The Shareholder does hereby give and grant unto the Company an absolute option to repurchase said Shares of Stock*, together with any and all Additional Shares (as hereinafter defined) and together with all rights appertaining to said Shares of Stock and Additional Shares, whether in the nature of subscription rights or otherwise, for a purchase price to be determined in accordance with the provisions of subparagraph (B) of this paragraph 3. The term "Additional Shares" as used in this Agreement shall include all shares purchased by the Shareholder pursuant to preemptive rights arising by reason of his ownership of the original Shares of Stock hereby sold and of any Additional Shares and all shares received by the Shareholder as stock dividends from time to time upon said Shares of Stock and upon any Additional Shares, it being the intention of the parties hereto that said option shall cover and include all shares in the Bank owned by the Shareholder from time to time in any manner derived from the

original Shares of Stock hereby sold and representing the proportionate interest in the Bank which on the date hereof is represented by said original Shares of Stock.

(B) The *aggregate purchase price for the original Shares of Stock and all Additional Shares, however acquired by the Shareholder, to be paid upon the exercise of said option by the Company shall be the sum of* (*a*) *$--------------, being the amount paid by the Shareholder for the original Shares of Stock,* and (b) the issue or subscription price paid by the Shareholder for the additional Shares, if any, which he shall have purchased pursuant to preemptive rights arising by reason of his ownership of the original Shares of Stock or of any Additional Shares and shall then own.

(C) Said option may be exercised by the Company upon or within six (6) months after

(a) the date upon which the Shareholder shall for any reason cease to be a director of the Bank,

(b) the Shareholders of the Bank shall have voted to authorize the consolidation or merger of the Bank with any other financial institution, the assumption by any other financial institution of the deposit liabilities of the Bank, or the voluntary liquidation of the Bank, or

(c) the date upon which the holdings of the Company in the common stock of the Bank shall be reduced by sale or otherwise to an amount representing less than 51 percent of the outstanding common shares of the Bank.

The Shareholder may at any time make written request that the Company exercise said option and the Company may upon or within thirty (30) days after the receipt by it of such written request exercise the same but, unless theretofore exercised by the Company, said option shall terminate and become null and void thirty (30) days after receipt by the Company of such written request.

Any exercise of this option may be made by the Company by mailing or delivering to Northwestern National Bank of Minneapolis, Minneapolis 2, Minnesota, a notice of the Company's intention to exercise the same accompanied by the payment of the amount of the purchase price determined in accordance with the provisions of sub-paragraph (B).

(D) The Shares of Stock and any Additional Shares shall be registered in the name of the Shareholder upon the stock books of the Bank and at all times prior to the exercise of this option the Shareholder shall have, enjoy and exercise with respect thereto all the rights, privileges, powers and duties of a shareholder of the Bank, subject only to the terms of this agreement.

(E) *The Shareholder agrees that so long as the option in this paragraph 3 granted shall continue in force and effect he will not sell or assign to anyone other than the Company, or pledge, hypothecate, or otherwise dispose of the Shares of Stock or* Additional Shares and that he will continuously remain the owner thereof in his own right. In order to prevent possible loss of the Shares of Stock or Additional Shares, the certificates representing the *Shares of Stock hereby sold shall be endorsed in blank by the Shareholder and delivered to Northwestern National Bank of Minneapolis for safe keeping and all certificates representing Additional Shares shall forthwith upon issuance be likewise so endorsed and delivered for safe keeping. Said Northwestern National Bank of Minneapolis is hereby directed to hold and safely keep said certificates and upon the exercise of said option by the Company as provided in subparagraph (C) above, to deliver said certificates to the Company and to deliver to the Shareholder upon surrender by him of his copy of this agreement, the purchase price received by Northwestern National Bank of Minneapolis.*

4. The Shareholder agrees that any preemptive rights to purchase shares of the Bank to which the Shareholder may from time to time become entitled by reason of his ownership of the original Shares of Stock or of any *Additional Shares shall, if not exercised by the Shareholder, be assigned by the Shareholder to the Company.*

5. This agreement constitutes the only agreement between the Company and the Shareholder with respect to any of the Shares of Stock or Additional Shares and supersedes any and all prior agreements or obligations of either party to the other, howsoever arising or expressed, with respect to such stock, the dividends thereon, or any other rights derived therefrom.

6. This agreement shall inure to the benefits of and be binding upon the parties hereto and their respective heirs, personal representatives, successors and assigns.

7. This agreement has been signed in triplicate, one copy thereof to be delivered to Northwestern National Bank of Minneapolis and one copy to each of the parties hereto.

IN WITNESS WHEREOF the Company has caused this instrument to be executed by its proper officers thereunto duly authorized and the Shareholder has hereunto set his hand, all as of the day and year first above written.

NORTHWEST BANCORPORATION.
By ________________________________
Vice President.
and ________________________________
Assistant Secretary.
____
Shareholder.

Northwestern National Bank of Minneapolis hereby acknowledges receipt of Certificate No. ______________ for ______________ Shares of Common Stock of ____, which it agrees to hold in accordance with the provisions of the foregoing agreement

Dated ________________, 19____.

NORTHWESTERN NATIONAL BANK OF MINNEAPOLIS.
By ____
An Authorized Official.

Mr. DUBOIS. The option agreement might be discontinued and in lieu thereof the holding company could require the director to hand over and assign to the corporation his stock in the bank of which he is a director. The holding company might hold this stock until the director ceases to be a director and then have the transfer made in the stock register of the bank to a new director.

The qualifying shares of a director should be in his possession, a strong indication of true ownership. We are sure there is no question in the minds of any of the committee but that a director should absolutely own his qualifying shares.

Section 39, "Branch offices," paragraph (c), page 33, line 10 of that paragraph: We would like to suggest a change in the wording of the last part of the sentence. Here is our suggested substitution:

* * * and subject to all the restrictions imposed by the law of the State on State-chartered commercial banks.

In the committee print, the verbiage is a bit loose, and the Comptroller of the Currency will give it a liberal interpretation in permitting a national bank to branch.

Mr. ROGERS. Mr. DuBois, may I ask you a question at that point?

Mr. DUBOIS. Yes, sir.

Mr. ROGERS. The language in the bill is the language——

Mr. DUBOIS. That language is in the statute now.

Mr. ROGERS. Yes; that is right. I wanted to make that clear for the record. We did not change it in the bill.

Mr. DUBOIS. Yes.

Section 39, "Branch offices," page 34, paragraph (f): At the end of that paragraph, we believe these words should be added:

* * * if not contrary to the laws of the State concerned.

Page 54, chapter 9, section 58, paragraph (a), on the sixth line of the paragraph, put a period after "stock" and delete—

unless an emergency exists and the Comptroller of the Currency specifically waives such requirement for shareholder approval.

It is hard at times to properly appraise emergency. It gives the Comptroller discretionary power, something that we fear. In small banks the supervisory authorities have for all practical purposes more power than was ever written into the book.

Title II, Federal Reserve Act, page 93, section 23, paragraph (d), starting with the words "provided, however," we believe the paragraph that follows should be stricken. This wording constitutes a scheme to make mergers easier. The wave of mergers in this country is appalling and should not be aided and abetted but must be curtailed.

Chapter 9, "Regulation of Bank Holding Companies," page 140, section 54: There should be an addition to paragraph (d) on line 7 after the word "operations." Place a semicolon, strike out the balance of the paragraph, and then this language:

* * * any bank holding company or any subsidiary thereof to acquire, directly or indirectly, any voting shares of, interest in, or all or substantially all of the assets of any additional bank, except (i) within geographic limitations that would apply to the establishment of branches of banks under the statute law of such State, or (ii) unless such acquisition is at the time authorized by the statute law of such State by language specifically granting such authority affirmatively, and not merely by implication.

The recommendation we are making was contained in the House version of holding company legislation, H. R. 6227, passed by a vote of 371 to 24. If this proposed addition had been contained in the Bank Holding Company act of 1956, the Federal Reserve Board would not be in the sweatbox it is. New York State would not have found it necessary to pass stopgap legislation.

This intrastate clause would have saved the Federal Reserve Board from the embarrassing position it now finds itself in.

If the application of the First National City Bank is approved, and I do not think the Board will approve it, it will start a chain reaction that might change our whole banking system.

Right there I would just like to make a statement. I do not think the Federal Reserve Board should be in a position where it could change the whole banking system. If there is to be a change in the banking system, it should be done by the Congress of the United States.

If the Board turns down this application, one of the biggest banks in the country will be offended. The discretionary authority that the Board now has under the act will torment it as long as this discretionary authority lasts. Legislation delegating discretionary authority should be as limited as possible.

Title III, Federal Deposit Insurance Act, section 18, "Assessment Credits," page 159: Our association agrees with the recommendation of the American Bankers Association to prorate back to the banks 80 percent of the assessment, rather than 60 percent. Then, following, the rest of the language contained in that section.

Section 23, "Mergers and Consolidations," page 162: The Independent Bankers Association prefers legislation that would place the administration of antimerger legislation in the Department of Justice. We do not believe that the three supervisory agencies really desire any antimerger legislation. We do not believe that they have used the tools that they now already have to stop mergers.

Section 26, "Payment of Interest": For years there has been disagreement between the Federal Reserve Board and the Federal Deposit Insurance Corporation as to what constituted interest on demand deposits. Now these two agencies seem to be of the same mind.

We doubt if there is much absorption of exchange. We wonder if this is an indirect way of forcing par clearance. We do not care to argue the issue involved, but we do believe that eventually State legislation will bring about par clearance and then this matter of absorption will be out of the picture.

Mr. ROGERS. Mr. DuBois, would you clarify your position on that? Are you opposed to the provision we have in here to provide for a uniform interpretation on this question of absorption of exchange?

Mr. DUBOIS. I would like to say that I do not believe it is very pertinent legislation, that it is coming about anyhow.

I think there is only one section of the country where there is any absorption to amount to anything, and that is in the Southeastern States. In the section of the country I come from, in Minnesota, we have more nonpar banks than any other State. I think we have 408. But the correspondent banks are all member banks, and, as far as I know, there is not a nickel's worth of absorption.

So, it is what I would call minor. It does not amount to very much.

Mr. ROGERS. I think that is true in your State of Minnesota.

Mr. DUBOIS. It is just the Southeastern——

Mr. ROGERS. It involves perhaps 2,000 banks, which includes their branches.

Mr. DUBOIS. There are only about 1,600 or 1,700 nonpar banks in the country.

Mr. ROGERS. About 2,000 altogether—banks and branches.

Mr. DUBOIS. Is that right? Thanks for the information. Of course, when I think of banks I think of an independent bank, sir, and not a branch.

Section 29, "Termination of Insured Status," page 165: The Illinois debacle gives some grounds for an argument that the Administrator of the FDIC in his discretion can shorten the period in which bad practices in a bank must be eliminated. We doubt the wisdom of shortening the period to less than 120 days. As we have before stated, supervisory authorities have more power than is contained in the statute, and 20 days would be too short a period for most banks to remedy a bad situation.

I thank you, Mr. Chairman.

Senator ROBERTSON. Are there any questions?

If not, we thank you very much for your testimony.

The next witness will be Mr. William A. Lyon, of the National Association of Mutual Savings Banks.

I believe Mr. Lyon has with him another witness.

STATEMENT OF WILLIAM A. LYON; ACCOMPANIED BY MORRIS CRAWFORD, NATIONAL ASSOCIATION OF MUTUAL SAVINGS BANKS

Mr. LYON. With your permission, Mr. Chairman, I would like to have Mr. Morris Crawford, vice president of the Bowery Savings Bank of New York, sit with me. He is a member of the legislative committee of our national association.

Senator ROBERTSON. The committee will be glad to extend that privilege and to hear from both of you.

Mr. CRAWFORD. Thank you.

Senator ROBERTSON. You may proceed.

Mr. LYON. My name is William A. Lyon. I am chairman of the executive committee of the Dry Dock Savings Bank, New York City. I am appearing on behalf of the National Association of Mutual

Savings Banks, a trade association made up of 527 mutual savings banks located in 17 States. The largest number of these savings banks and the preponderance of their deposits are concentrated on the east coast of the United States. They are particularly strong and numerous in the States of New York, Massachusetts, Connecticut, New Jersey, and Pennsylvania.

As of December 31, 1956, these mutual savings banks——

Senator BRICKER. I think we only have three in Ohio; is that right?

Mr. LYONS. Yes.

Senator BRICKER. One big one and two small ones.

Mr. LYON. Yes. You have a very big one in Cleveland, Senator.

Senator BRICKER. Thank you.

Mr. LYON. As of the end of last year these mutual savings banks had $33,382 million in assets and $30,030 million in deposits belonging to approximately 21 million depositors. All of these savings banks are mutual institutions without stock or other proprietary interests.

With your permission, I should like to address myself to the following specific provisions of the tentative bill entitled "Financial Institutions Act of 1957."

The first provision I would like to speak on is the form of organization of the Federal Deposit Insurance Corporation.

The advisory committee has proposed, and the new bill includes, a change in the form of organization of the Federal Deposit Insurance Corporation. It is proposed that the Board of three which now directs the Corporation's affairs be replaced with a single administrator. Here we believe that the bill goes beyond technical statutory changes and gets into substantive changes of great importance.

The change from a board of shared responsibility to a single administrator is a step that would be taken against the trend of supervisory agency development since around the time of the banking holiday. It is the older established agencies, such as the Comptroller of the Currency, that go in for a single administrator, and the Comptroller, it might be recalled, has Treasury officials immediately available, down the hall, for consultation and advice. The Federal Home Loan Bank Board, which is one of the newer agencies in the supervisory field, has three members. The Federal Reserve Board has seven members. The trend in the States over the last 25 years has been toward the creating of banking boards, not merely to advise but also to share responsibility with the supervisory authority.

The Federal Deposit Insurance Corporation has spent all of its days in a rising price level and, more recently, in a time of extraordinary prosperity. It is yet to go through a period of declining business which would create greater stresses for insured banks than they have had to face in the years that the Corporation has been in existence.

Of course, we all hope that any troubles that may develop for banking will be little troubles. It would be a great mistake, however, to assume that banking will never again know times of genuine strain. If those times ever come again, a single administrator might have to deal with more problems than any one person should be expected to handle efficiently and wisely. It would not take much of a setback in business to keep a three-man board pretty busy.

It is readily agreed that the Comptroller of the Currency should no longer sit on the Board of the FDIC. Before cutting the Board back to the direction of a single man, however, the prudent course would be to wait to see how the Corporation made out after business and banking had faced declining trends in activity and prices for a time.

Senator ROBERTSON. If you would not object to a question at that point?

Mr. LYON. Not at all.

Senator ROBERTSON. We would like to know your definite recommendation, whether you favor a 3-man board without the Comptroller, a 3-man board with the Comptroller ex officio as under the existing law, or a 5-man board without the Comptroller as recommended to us yesterday by ABA.

Mr. LYON. The first of your alternatives, Senator—a 3-man board without the Comptroller.

Senator ROBERTSON. A three-man Board without the Comptroller?

Mr. LYON. Yes. I doubt the need has yet been demonstrated for a larger board than three. I think that it provides some power and means of consultation among the members of the Board. And five, with the present duties of the Corporation, might be an excessive number.

Senator ROBERTSON. Mr. Brumbaugh suggested it would be agreeable if we had a five-man board: the Comptroller and the Chairman of the Federal Reserve Board ex officio members, and some State examining official—rather, an ex officio member to be selected from that group. That would leave only two men to be selected solely from the standpoint of who is best qualified to administer FDIC. You wouldn't favor that change?

Mr. LYON. We would not favor that, Senator.

Senator ROBERTSON. You would definitely favor a three-man board, but let them all be full-time employees and hove no ex officio member?

Mr. LYON. That is right.

Senator ROBERTSON. Thank you.

Senator BRICKER. What would you recommend for the tenure?

Mr. LYON. I think the term should extend over the term of an administration. I think on the order of the Comptroller of the Currency, whose term is 5 years, I believe. I think it should at least extend a year beyond the 4-year term.

Senator ROBERTSON. Any other further questions on this one point?

Senator FREAR. Senator Bricker just brought up a question in my mind. I thought the term would be 4 years. But would you or your association favor staggering terms?

Mr. LYON. I think that is useful, too. It provides for some continuity in experience that is, in times when the going is rough, extremely valuable. To expect a whole new board to start off from scratch and try to familiarize itself with the problems of the Corporation when the sailing is not exactly smooth is expecting too much.

Senator FREAR. Thanks.

Senator ROBERTSON. You may proceed.

Mr. LYON. The second point has to do with the investment power of Federal savings and loan associations, page 204, paragraph (c).

Near the end of the paragraph it is provided that these associations may make investments "insured as provided in the Servicemen's Readjustment Act of 1944." It would appear that there should be inserted the words "or guaranteed" after the word "insured." This would supply an apparently inadvertent omission on the part of the drafters of the bill.

Senator ROBERTSON. I will ask Mr. Rogers if that is correct.

Mr. ROGERS. I cannot give you an offhand answer to that. I will check it.

Mr. LYON. Mr. Crawford points out that was in the law as it now stands before your draft appeared.

Senator ROBERTSON. And it was not carried on?

Mr. LYON. That is right.

Mr. CRAWFORD. No; the omission was carried forward, I believe.

Mr. ROGERS. The present law has an omission in it.

Mr. CRAWFORD. I believe, sir, that this omission was in the original law. It was not a fault of the draftsman of this particular bill. We are merely pointing it out because it does appear to be an omission that should not exist, since these——

Senator ROBERTSON. I am glad to have that testimony, because I got a letter yesterday from one of the outstanding banking lawyers of New York, a member of what is probably the largest, certainly the most prominent, law firm of that city, in which he said he thought we had done a very good job. He pointed out that we had used an adjective when we should have used an adverb in one place, a typographical error that we had already caught. He pointed out that in referring to the new setup of FDIC we had in one place referred to the Board when it should have been the Administrator, but we had already caught that. And then he said that we had eliminated in the National Banking Act a reference to Treasury notes and had not used the same language in the Federal Reserve Act. Our reply to that was that if that was a fault it was a fault of the Federal Reserve Board because the Comptroller had recommended that the words be eliminated from this statute, the Federal Reserve Board had not made the recommendation, and so the drafters just followed the recommendation of both agencies.

Personally, the chairman thinks that the lawyer in New York was correct—that the same language should be applied to both. It is an obsolete provision, in other words, but we think the Federal Reserve Board just overlooked it.

Mr. LYON. Yes.

Senator ROBERTSON. But I thought it was a right good tribute to the work of the Federal agencies, our advisory committee, and our staff that we have put together a 253-page bill and one of the best lawyers in New York, probably as good as any of the oldtime "Philadelphia lawyers," who are supposed to be the best, could find only those three errors in it.

This error that you refer to now was the error of those who first drafed this and not those who carried it forward.

Mr. LYON. I am glad Mr. Crawford made that clear, Mr. Chairman.

Senator ROBERTSON. You may proceed.

Mr. LYON. The third point has to do with branches of Federal savings and loan associations outside of the State of the head office. This provision appears on page 211 of the bill.

This provision of the new bill permits the retention of branches when there is a consolidation or merger of State or Federal savings and loan associations, but there is no restriction prohibiting the merger or consolidation of such associations located in different States.

The tentative bill does provide that no branches of any Federal savings and loan associations shall be established outside the State in which the home office is located, but this prohibition does not cover the situation where two savings and loans located in different States are merging. In order to prevent cross-State establishment of savings and loan branches, it is urged that the language near the bottom of page 211 be amended to read:

No branch of any Federal savings and loan association shall hereafter be established or operated outside the State in which its home office is located.

The next point concerns Federal savings and loan branch powers generally, page 211, paragraph (c).

The savings banks have long believed that Congress should itself decide what branch powers Federal savings and loan associations should have instead of, by keeping silent, creating a vacuum which the Federal Home Loan Bank Board would feel obligated to fill by regulation.

Some savings and loan branch bills would be more desirable than others, but it may fairly be said that most any bill would be better than no bill at all. The proposed bill is, in our opinion, clear of any criticism when it grants to Federal savings and loans the same branch powers in any State that the State-chartered savings and loans have. A case may be made for granting them also the branch powers that mutual savings banks have, though, strictly speaking, savings and loan associations are not banks of deposit and a true analogy with savings banks does not exist. It is when the bill goes beyond this point and extends to Federal savings and loans in addition the branch powers available in any State to the State-chartered banks and trust companies that its workability and its fairness to the States become more open to question.

Senator ROBERTSON. You recall that the Senate passed a provision about branches at the last session.

Mr. LYON. Yes.

Senator ROBERTSON. And that is the reason we decided to put the same language in that bill.

Senator FREAR. That was an amendment accepted on the floor, Mr. Chairman.

Mr. ROGERS. To your bill.

Senator FREAR. Yes.

Senator ROBERTSON. But anyway we passed——

Senator FREAR. It did not come out of the committee.

Senator ROBERTSON. No, but the Senate passed it.

Senator FREAR. Yes.

Senator ROBERTSON. But it got tied up in the House committee. They never acted on it.

Senator FREAR. Yes.

Senator ROBERTSON. Of course, we realize the provision does not go as far as the savings and loan associations want. They want, when a savings and loan association is in a bank holding company State, to have all the branch provisions that the bank holding company has. That would enable them to go into some cross-State lines.

Mr. LYON. Yes.

Senator ROBERTSON. You may proceed.

Mr. LYON. We praised the action of the committee on the bill last year over what the Senate itself did.

Branch powers, under the dual banking system, are applied with the greatest equity and logic when the powers are directly related to those of the same type of institution and are not derived indirectly from the branch powers of another type. This is so because the derived powers, by their very nature, trample on the safeguards that a good many States have set up in their branch laws.

Banks and trust companies in New York State and Connecticut, to take two examples, are not permitted to establish branches by application in communities other than their head office communities where the other communities have their own independently operated institutions. The laws of these States and various other States have placed this limit to branch powers for the very good reason that they wish to give local institutions, which are usually of a smaller size, endurable competitive conditions. There is no better way to thin out the ranks of the small independent institutions, locally owned and operated, than to give supervisory agencies and institutions complete freedom to roam at will in authorizing and opening up branches.

The great weakness that has been shown to exist in the branch provisions of the National Bank Act is with the derived powers. The National Bank Act says that the national banks can have not merely the branch privileges extended to banks and trust companies under State laws but also the branch powers granted by the States to savings banks. The Comptroller of the Currency has taken the position that the limitations under the direct grant of branching power do not extend over into the derived powers. For that reason he holds that he would be able to use the savings bank parallel to permit branches, in contravention of State policy, even in those communities where head offices of local commercial banks exist. I do not believe that Congress intended that the Comptroller should have this power. It scarcely seems fair or desirable that a State should be unable to permit savings banking to come to a community which has its own commercial banks, but lack a savings bank, without laying that community open to invasion by national banks from other cities and towns.

If the Congress wishes to reduce the number of competitive units in commercial banking rapidly and to concentrate banking power in fewer and fewer hands, it could not have chosen a better way to do it than with the derived-power provision in the 1927 amendment. If and when Congress takes up again for serious consideration the whole large issue of branch powers under the dual-banking system, I feel sure that it will have to conclude that State policy designed to protect local institutions should be respected and the Comptroller should be required to abide by the branching patterns which the States believe to be suitable. For this reason we think that a branch bill which said merely that Federal savings and loans may have the same branch powers as State savings and loans would be the best bill of all.

We repeat, however, that it is most earnestly to be hoped that the Congress will no longer leave Federal branching to the unstable foundations of agency regulations and interpretations but will rest it clearly and firmly in the statutes.

The fifth point has to do with payment of insurance by Federal Savings and Loan Insurance Corporation.

In section 406, page 223 of the proposed bill, it is provided that in the event of a default by any insured savings and loan association, the FSLIC shall pay each insured account either by cash or by making available a transferred account payable on demand in a new insured institution in the same community or in another insured institution. The proposal to create a new class of shares for savings and loan associations, payable unconditionally on demand, is, we believe, more than a technical amendment to the laws.

As the committee is aware, a savings and loan which invokes its rights to withhold full payment on shares for a time is not considered to be in default. The provision that transferred accounts would be payable on demand, however, would create a new and specially privileged type of share. Such a proposal would go a long way toward removing one of the distinctions between banks of deposit and savings and loan associations.

There is good reason to believe that the public would be better served if the lines of distinction between different types of financial institutions were more clearly drawn instead of being blurred, as the proposal in section 406 would result in.

In any case, before any such proposal is seriously considered for inclusion in the statutes, it should be studied with the kind of care and with the eye toward the complete banking picture that a monetary commission could give it.

Mr. ROGERS. Mr. Lyon, are you aware that we put a like provision in the Federal Deposit Insurance Corporation Act?

Mr. LYON. Yes.

Mr. ROGERS Is that satisfactory there?

Mr. LYON. Yes. I think that is a desirable amendment to make. I believe that restores the Federal Deposit Insurance Act to the form in which it existed prior to 1950. I think that it is only reasonable that a transferred deposit which is not transferred with the precise consent of a depositor to another institution should be immediately available to transfer to some other institution at the depositor's option. I think that is fair.

Mr. ROGERS. Why does not the same philosophy apply to this case?

Mr. LYON. Because in any going Federal savings and loan association the unconditional right of immediate withdrawal of shares does not exist. This would create for the first time that unconditional right. And it would prejudice the interests of the other shareholders in a savings and loan association.

Those transferred shares which went to another association would, if withdrawn immediately or presented for withdrawal, use up the liquid resources that were available to all the customers of the association that were doing business with it before the transfer took place.

Mr. ROGERS. Well, in a bank your time deposits would be in the same situation, where you are supposed to give 30 days' notice.

Mr. LYON. Yes.

Mr. ROGERS. If they are transferred, then they are payable on demand under the new provision.

Mr. LYON. Yes; but there is in a commercial bank always the right to withdraw on demand, and that is not an unconditional right of a savings and loan association.

Mr. ROGERS. Well, there can be a 30-day period. They can require it.

Mr. LYON. There can be a period that can extend for a long while before an association is considered to be in default.

Mr. ROGERS. No; I am referring to a bank. They can require in their contract with a depositor a 30-day waiting period, or a 60-day or a 90-day.

Mr. LYON. Yes; that is true, Mr. Rogers. The fact is that that power has not been invoked in many years. And I would say for practical purposes it must be assumed not to exist as a reliance for banks of deposit with demand deposits.

Mr. ROGERS. I would agree with you more if you would be opposed to both changes.

Senator FREAR. Do you know of any bank that is enforcing the 30-day withdrawal of time deposits?

Mr. LYONS. No; I do not. I do not remember in the——

Senator FREAR. Was there not established also, primarily, the fact that the bank would not have to pay the time depositor the interest on that 30-day period?

Mr. LYON. I do not know about that, Senator, but I do know that in an earlier era in banking 50 or more years ago it was not uncommon for a notice of withdrawal privilege to be invoked. But since the establishing of the Federal Reserve that power I would say had not in any instance known to me ever been resorted to.

It becomes impossible to use a power to require notice of withdrawal for time deposits and savings deposits while you continue to pay out your demand deposits. That would be prejudicial to the savings depositor and is, for practical purposes, not available as a result.

Mr. ROGERS. In reality, do not savings and loans pay on demand?

Mr. LYON. Well, they do; yes; that is correct. Now they do. But it is no statutory privilege of the shareholder to require payment on demand.

Senator FREAR. I do not want to get into debate with the counsel for this committee. However, going back to a statement you made a little earlier in your testimony when questioned, that in case of default of a Federal savings and loan association that this proposed legislation would give to the FSLIC the authority to transfer those funds to another organization, presumably another Federal savings and loan association, it also could be that it would have some prejudice in the defaulted shareholders' organization going into the new one whereby they would have a right that the shareholders of the institution to which they were transferred did not have also.

Mr. LYON. That is precisely the point, Senator. Of course, too, if you pursue this thing to the end, it would become of interest to any large shareholders in an institution that was getting on the ragged edge to see it go over the edge, because then their shares would have the right of transfer to a going institution and be unconditionally payable on demand under this bill.

The next point that we would like to bring up for your consideration has to do with amendments to the Criminal Code, on pages 247 to 249.

It is highly desirable that the bill not go any further than necessary in its effort to prevent conflicts of interest between supervisory personnel and the institutions under supervision of Federal or State agencies.

No one will contend for a moment that the moral position of the supervisory agencies should be undermined by permitting institutions with disciplinary problems pending before an agency to hire agency personnel to represent them in the proceedings. Banking supervision, including examiners, has enjoyed a splendid reputation for the high ethical standards on which its dealings with banking institutions have been conducted. The lapses have been rare. The honor and fidelity of the supervisory staffs have been models in Government service. Most of the supervisory personnel is not even bonded. The traditions of the service are so high and firmly set that it has not been considered necessary by a great many, perhaps a majority, of the supervisory agencies to obtain surety bonds covering their examiners and their staffs. The cases that are known of any shadow of unethical conduct falling on supervisory staffs are so few as to be insignificant.

In view of this record, legislative bodies are justified in proceeding with great caution in adopting laws which would make the already difficult problem of recruiting and retaining examining personnel harder to live with.

Years ago the task of hiring examiners of suitable ability and experience was manageable. In recent years the comparison between the pay of examining personnel and the pay of banking staffs has become steadily more unfavorable for the former. The usual practice is to find additions to the examining staffs from bank clerks and junior officers. Some of the most able young examiners have taken, in effect, leaves of absence as bank employees so that their careers might be broadened and deepened by at least a few years' experience as examiners. These intended from the start to go back to banking. This free flow of bank clerks into supervisory agencies and back into banking has been good for both supervision and banking.

It would be most regrettable if a dead end should in effect be placed in the way of a bank examining career by encumbering the examiner's return to banking with a mass of redtape and statutory restriction. We do not believe that there is any problem here which cannot safely be left to the agencies' regulatory power.

Senator ROBERTSON. Do we understand then that you endorse the recommendation made to us by ABA yesterday that the criminal provisions with respect to future employment in banks and the lending provision be completely eliminated from the bill?

Mr. LYON. Be completely eliminated and the right to control that by regulation would still remain.

Senator ROBERTSON. Yes.

Mr. LYON. Yes. I speak—excuse me.

Mr. ROGERS. I wanted to make this clear. As I understood it, you would go along with a provision such as in title I which provides for each agency by regulation to control the situation?

Mr. LYON. That is right.

Mr. ROGERS. At the present time the law does not so state, and some agencies do not have any regulations.

Mr. LYON. If it did so state, I think that would be completely——

Senator BRICKER. Why would you think the regulatory agencies could properly handle that, when you would not put it in the statute?

Mr. LYON. I think, Senator, that it becomes an impossible thing for a statute to be so worded that it can contemplate any of many situations that may arise.

An examiner, for example, may have completed, as 1 of a group of 20 or 30, an examination of an institution and to have been in such a minor capacity in the examination and to be of such limited influence, shall we say, in the supervisory agency, that the hiring of him, by that institution which he had reecntly been part of the examining staff of, would be a matter of absolutely no importance.

And I think there, if the supervisory agency could inquire into the facts and establish that there was nothing out of the ordinary in this request for permission to accept employment, it should be within the power of that agency to give him——

Senator BRICKER. But that power and authority ought to be granted in the law, even though you leave it to the supervising agency. It ought to be pretty well prescribed by the law.

Mr. LYON. Granted to the agency to issue the regulation. I speak on that subject with a great deal of feeling, I may say. I spent some years in the banking department of New York State, I was for some years the superintendent of banks of New York State, and I understand firsthand the seriousness of the problem that the supervisory agencies have in recruiting and maintaining staffs of adequate quality and adequate numbers.

Senator BRICKER. I agree with all that, but what I am getting at is whether or not that authority should be left to the supervising agency or whether it should be prescribed by law, although it not be a strict statutory prohibition or anything of that kind. If it could be determined by the regulatory agency, why could it not be determined by the Congress in the statute, even though it not be a strict requirement?

Mr. LYON. Senator, I find it not possible to say that nobody could come up with a combination of words that would permit respect for prohibition of conflict of interest and the opening up of reasonable inflow and outflow of personnel in banking and supervision and back again. But I think it would test the ability of the most skillful drafters of legislation to draw up a bill that would not set rules that would go too far in preventing this irregularity which everyone is interested in preventing.

I think that if the statute said that the power is left to the supervisory agencies to issue regulations prohibiting conflicts of interest that would express the policy of the Congress and put the agencies on notice that they must be more than ordinarily careful to prevent such conflicts. I feel that it would accomplish every purpose that you have in mind.

Senator BRICKER. I hesitate, with the responsibility that we have here, to say to you as a supervising administrator that you could do something for one man that you would not do for another, if there were any way that the law could be definite on the subject.

In other words, you might favor one examiner and say to another one, "No, yours transgresses the conflict of interest, while the first one does not."

If there were any way of being definite about it in the law, I would like to see it done rather than leaving it up to the supervising agency to favor one that he likes and maybe penalize one that he does not who has been working under him. That is the only thing I fear, and I have seen a lot of favoritism in the administration of law.

Mr. LYON. I would just like to say again that I believe it would be desirable for the committee not to use the test of recency of examination of an institution, of participation in an examination of an institution, as the main test.

Senator BRICKER. In other words, the degree of authority in supervision ought to be a determining factor?

Mr. LYON. Oh, by all means that should be taken into account. And that, I would submit, could be left only to the discretion and judgment of the agency. After all, Senator——

Senator BRICKER. You have got to lodge authority some place.

Mr. LYON. Yes. Yes. And the agencies should be exceedingly vigilant about it too.

Senator BRICKER. The trouble is we too often emphasize the indiscretions to the detriment of those who are perfectly honest and straightforward, who would handle either of the jobs, in the regulatory authority or in the bank, with perfect honesty and integrity.

Mr. LYON. Senator, do not the lawyers say that bad cases make bad law?

Senator BRICKER. I think that is right.

Mr. LYON. I think it would be good to be on guard against that in a matter of this importance.

The seventh and last point that we would like to make has to do with a comprehensive study of the banking laws.

It is noted that the bill does not include the recommendation of the advisory committee that a Monetary and Financial Institutions Commission be appointed. In the memorandum which savings banking filed with the committee on December 13, 1956, the recommendation was made that a sweeping and exhaustive study be made of the Federal laws relating to banking and credit.

We in our association still believe that such a study should be authorized forthwith by the Congress.

Senator ROBERTSON. I may ask there, Who should make the study? Whom do you favor making it?

Mr. LYON. Senator, my belief is that you would get a better study if the commission were composed both of Members of Congress and public representatives.

Senator ROBERTSON. That is the recommendation of our advisory committee.

Mr. LYON. Yes.

Senator ROBERTSON. There are a lot of political issues that have got to be solved there.

Mr. LYON. Very decidedly.

Senator ROBERTSON. I would personally prefer for them to be handled by someone who does not have to answer politically to any constituency.

Mr. LYON. I think you are completely correct.

Senator ROBERTSON. And there is another thing. The majority might come up with proposals that Members of Congress did not approve of. Would they not be more or less committed to such a finding if they were a member of such a commission and be less free to criticize it?

Mr. LYON. It would save valuable time, it seems to me, for the public members, lacking the knowledge of the congressional questions that they do, to have as members of the committee the responsible Members of Congress having to do with banking and currency matters. But I do believe at the same time, Senator, that public members in an advisory capacity are much less effective than they are as full-fledged members of the committee where they can take part in the——

Senator ROBERTSON. We have had a lot of commission reports in recent years. Some people think we have referred too many problems to agencies of that kind. Some of them have been independent of Congress, and some have had congressional members on them. But, after all, the report of any commission does not rise above the status of a report until Congress takes it up and decides whether or not to legislate on the subject.

Mr. LYON. That is correct.

Senator ROBERTSON. So the final decision has to be with Congress in any event.

Mr. LYON. Quite correct.

Senator ROBERTSON. But you would prefer——

Mr. LYON. I would combine them.

Senator ROBERTSON. To combine them?

Mr. LYON. Yes.

Our country is greatly in need of a study by experts, objectively carried out, which would consider, among other things, the adequacy of our banking and financial structure and the allocation of responsibilities in it. There has never been a time when greater competition existed between the different types of financial institutions, including commercial banks, savings banks, and savings and loans. The role that each type should play has not been clearly marked out. It is high time that we knew whether savings banking, for example, had anything unique and of value to offer to our economy. Savings banking has a different effect on the country's economy from what commercial banking has. It attracts the savings of the people and invests those savings, not in short-term loans and investments, in the manner of commercial banks, but in the long-term capital market—in the financing of homeownership, in mortgages on commercial properties, and in the long-term obligations of the public-utility companies, railroads, industrial companies, turnpikes, States, and municipalities, and so forth.

In the last few years a number of commercial banks have decided that they were part of the thrift machinery themselves. They have been going out more and more aggressively to draw in the public's savings.

Commercial banking does not, however, as a general thing, employ the savings that it attracts from the public in long-term investments. It uses these savings in the customary commercial banking fashion—that is to say, to extend short-term credit to business and industry and to finance purchases of consumer goods by the public. When commercial banking gets its hands on a dollar of savings, it uses only a few cents of that dollar to close the gap between the demand for long-term capital and the supply. It is no secret that some of the commercial banks, both large and small, which have savings departments make no mortgage loans at all.

The use of savings, the very stuff and fiber of the long-term capital market, to make short-term loans, including personal loans and loans to finance purchases of consumer goods, can hardly be regarded as the best use of our national resources.

We believe that the time is at hand when we should turn our best legislative and public minds to work of appraising the component parts of our financial and banking structure, and to decide whether the manner in which we have built that structure is the best for the public.

I wish to thank the committee for permitting me to express the views of the savings banks on these subjects.

Senator ROBERTSON. Mr. Lyon, since you have demonstrated a commendable grasp of banking and credit matters, we would welcome an expression of your views on the subject of the absorption of exchange.

Mr. LYON. Senator, in my State, my part of the country, I have not come across this problem. There are no nonpar banks up through New York and through New England. That, as has been said, is largely a southern and a middlewestern problem.

I myself believe that there is some good to be got from uniformity of practice on this subject. I would say that it would be quite harmful though to the nonpar banks to change their status on exchange overnight.

If you will look at the figures in any of the compendiums of commercial banking statistics of how nonpar banks conduct their operations, you will see that this matter of collecting exchange is a major reliance for income. They have by far the largest cash reserves, cash resources, of any commercial banks in the country. You cannot say to them overnight, "You must change; you must look elsewhere for your source of income and not look any longer to exchange. You must, in other words, become makers of loans and investors in securities exclusively as the par banks do."

That, I submit——

Senator ROBERTSON. If I may interrupt, in drafting the tentative bill we took the position that we just could not say categorically to some 4,000 banks including the branches, "You must be a par bank; you cannot be a nonpar bank."

Mr. LYON. Yes.

Senator ROBERTSON. All we did in our tentative bill was not to give to the FDIC—and we do not think it has it anyway and we did not give it to them—the right to pass on what is and what is not interest. We merely wrote into the FDIC section the same definition of interest that has been in the Federal Reserve, thinking that if FDIC did undertake to make a ruling on this subject it would have to be in conformity with the ruling of the Federal Reserve Board.

But on yesterday you may remember we had the recommendation of the advisory committee that we should definitely write into this final bill a provision that no bank should absorb exchange.

Mr. LYON. I think if you were working with a clean sheet of paper and there were not these longstanding differences in this matter you could come up with the ideal solution so much more easily. I would think that it would be better for trade and commerce and for banking in the country if the trend were toward par collection rather than preserving indefinitely the present divided practice.

Senator ROBERTSON. Certainly we would not want anybody, if we gave them a hundred dollar bill, to say that one-tenth of 1 percent comes off for the trouble of changing it for you. You'd like checks to be handled on the same basis as currency?

Mr. LYON. No question about it. But, Senator, if the decision is to move toward uniformity and achieving of complete par status, I submit that the progress should be gradual and not overnight. You cannot tell banks not accustomed to lending money on the scale that others do, "Tomorrow morning you must have a good and experienced loan man and you must find sources of loan demand that you can accommodate to replace the income that you have lost."

Senator ROBERTSON. I was under the impression that the approach that I decided to put in the tentative bill was a gradual approach.

Mr. LYON. If that is the case, Senator—and I have not made a close study of that part of the bill—it seems to me——

Senator ROBERTSON. In fact, we will have one witness here, on Friday, from North Carolina, if he comes who says it is too gradual.

Mr. LYON. Well, that is fine.

Senator BENNETT. You mean that any approach is too gradual or too fast?

Senator ROBERTSON. He wants it spelled out. He wants it spelled out in the bill that nobody can absorb it, Senator.

Mr. LYON. Well, you would cause some serious dislocations in that event. You can merely look at the statistics, without going to talk to a single banker, and see that that would be so.

Senator ROBERTSON. Are there any further questions of this witness? We have got to hurry along. Any further testimony from this gentleman?

Mr. LYON. Thank you very much for both of us.

Senator ROBERTSON. Thank you both.

The next witness is Mr. Baker, who will speak for National Farmers Union.

We are glad to have you, Mr. Baker. You may proceed.

STATEMENT OF J. A. BAKER, COORDINATOR OF LEGISLATIVE SERVICES, NATIONAL FARMERS UNION

Mr. BAKER. Mr. Chairman, for the record I am J. A. Baker, coordinator of legislative services, National Farmers Union.

We appreciate this opportunity to present our views concerning the recodification of Federal laws regulating the private and semiprivate nonfarm financial institutions of our privately and publicly managed free enterprise system.

There is, of course, nothing in the proposed Financial Institutions Act of 1957 that will help materially to raise farm family income toward the position of a fair parity in our economy that it should occupy. Nor is there anything in the proposed bill that will immediately improve the chronically weak bargaining power and disadvantaged position of family-farm operators in the commodity and money markets of the Nation.

Nevertheless, if enactment of the proposed legislation should operate to make our publicly controlled private financial institutions more effectively responsive to our constitutional democratic political institutions, more observably honest in their financial manipulations and more fully competitive in rates and efficient in management costs, these gains would be of great general importance and interest to farm people even if it did nothing directly and immediately to improve the current depressed economic lot of farm people.

No known improvements in the Nations credit system can improve the financial aid of farmers unless the legal and institutional conditions surrounding the production and pricing of farm supplies and of farm products are such that farmers can make enough income above conservation needs and living costs to repay such loans as they are able to obtain from financial institutions.

Moreover, we do not believe that the publicly controlled private financial institutions of the Nation can, whatever laws you may improve and adopt, ever become fully adequate to serve farmers' credit needs in the absence of expansion and revitalization of the Farmers' Home Administration to transform that agency into a fully adequate Federal yardstick family farm credit agency.

However, adequate provision to care for the needs of credit adapted to family farm needs is not the central purpose of your hearing today. Therefore I shall merely point out to you that the credit needs of the 22 million people on farms are, measured in human terms, about 13 percent of the subject matter of your hearings.

The 22 million people on farms are more than 50 times the approximately 400,000 children and wives and husbands of families who depend on banking for a livelihood. The family incomes of the latter greatly exceed the family incomes of the former. And the basic underlying reason for that condition is that bankers possess, under Federal and State law, and farmers do not, the right and power to withhold what other people want and need but cannot have unless the fixed price is paid.

Without taking your time at this point to discuss either the need to greatly strengthen the Farmers' Home Administration or to explain out deep disagreement with the existing hard-money policy, I request that you place the attached legislative analysis memorandum on yardstick family farm credit in the record of your hearings at this point in my statement.

Senator ROBERTSON. Without objection, that will be done.

(The statement referred to follows:)

YARDSTICK FAMILY FARM CREDIT LEGISLATION

(Legislative Analysis Memorandum No. 56–17, Revision No. 1, August 30, 1956)

Alone among the farm organizations, Farmers Union invited the attention of the 84th Congress to the credit problems of family farmers. Our efforts resulted in significant improvements in the credit programs provided by Farmers' Home Administration and succeeded in blocking the destruction of the yardstick 5-percent interest rate set up in existing law. Its repeal was repeatedly recommended and demanded by the Eisenhower administration.

LEGISLATIVE DEVELOPMENTS IN 84TH CONGRESS

Improved yardstick family farm credit legislation (H. R. 11544) was adopted by Congress. Farmers Union made a big push to obtain enactment of legislation that would rehabilitate the Farmers' Home Administration and reestablish it as a comprehensive fully effective yardstick family farm credit agency. The Eisenhower administration fought our efforts, putting their main emphasis on eliminating the 5-percent interest rate yardstick in existing law. Under existing law, a farm family that cannot obtain adequate needed credit from usual commercial and cooperative sources at not more than 5-percent interest is eligible to receive a loan from Farmers' Home Administration. Farmers Union urged this yardstick rate be dropped to 3 percent. Eisenhower recommended that the "5 percent" be changed to "a reasonable rate." Administration witnesses testified in both House and Senate that the words "reasonable rate" would be interpreted to mean the "prevailing rate in the local community, 6 percent, 8 percent, 12 percent, whatever it is." Adoption of such language would have completely destroyed the yardstick feature of the Farmers' Home Administration and the laws it seeks to administer.

A yardstick family farm credit bill (S. 3790) more nearly adequate to the current needs than H. R. 11544 was introduced in the Senate on May 7, 1956, by

Humphrey, George, Hennings, Kerr, Clements, Lehman, Mansfield, Morse, Murray, Neely, Neuberger, Scott, and Sparkman. Companion bill in House was introduced by Polk, Metcalf, and Knutson.

H. R. 11544 as enacted by Congress reflects Farmers Union recommendations as somewhat watered down by Eisenhower administration recommendations. Farm Bureau did not appear at the hearings on this important subject. The net result is to have obtained some quite significant improvements in the way of yardstick farm credit. Major among these are full authority for Farmers' Home Administration to make loans to refinance existing indebtedness, somewhat larger appropriations or authorizations for various types of loans, direction to the executive branch to tailor repayment schedule to fit characteristics of such needed credit as frozen-out prune orchards and the like, and specific mandatory expansion of real estate loan authority to include existing as well as prospective farmowners. Applicants to be eligible would not have to show that more than half of their income came from farming.

FARMERS UNION RECOMMENDATIONS

There is a developing farm credit crisis out in the country. We are in another of those eras that have come twice in the past 50 years when the Nation will and must make a major reform in its farm credit policy.

Growing awareness in the period 1908–14 of the basic disadvantage of farmers in the Nation's money and capital markets led to the establishment of the Federal land bank system.

Later, the total failure of the then existing farm credit institutions to cope with the 1921–33 farm depression led to the complete reform and improvement of national farm credit policy and institutions in 1933–34.

NEED NEW CONCEPT OF YARDSTICK FARM CREDIT

Now in 1956, we seem to be in the middle of another era of broadening farm credit concepts, an awareness brought on by the apparent inability of the now existing institutions and policies to cope with the problems of the growing farm depression and recurrent droughts, dust storms, floods, and falling farm income.

National Farmers Union continues to urge enactment of a comprehensive "yardstick" family farm credit bill, incorporating the good features of the bills that have been referred and expanding and extending the excellent features of existing Federal "yardstick" family farm credit laws.

EXISTING LAW

Existing legislation covering direct and insured general family farm credit loans is incorporated mainly in the Bankhead-Jones Farm Tenant Act, as amended; the Water Facilities Act, as amended; Public Law 38 (emergency loans), as amended; and Public Law 727 (emergency credit), as amended.

RECOMMENDED AMENDMENTS TO WATER FACILITIES SOIL CONSERVATION LOAN ACT

The Water Facilities and Soil Conservation Loan Act of August 28, 1937, as amended (16 U. S. C. 590r–x), needs to be improved and modernized.

This act has provided very much needed loan facilities during its nearly 10 years of operations. Its scope was broadened several years ago to cover the entire United States. It authorizes the Secretary of Agriculture to make direct and insured loans to farmers and stockmen and reclamation, irrigation and grazing associations for soil and water resource improvement and conservation purposes.

However, with increased costs of such measures, the loan limitations have gotten out of date. We recommend raising the limitation on indebtedness of drainage, irrigation, and grazing associations and other corporations and agencies, as provided in section 8 from $250,000 to 1 million.

We also urge that the maximum rate of interest chargeable under this program be set at 3 percent per annum. If this should require Federal subsidy in a period of a general hard-money policy, we feel the difference is justified both by the generally deflated condition of the farm economy and by the general public welfare benefits derived from increased soil and water conservation on the farms of the Nation.

RECOMMENDED AMENDMENTS TO DISASTER LOAN ACT OF 1949, AS AMENDED

Public Law 38 of the 81st Congress, as amended, is the act of April 6, 1949, as amended (12 U. S. C. 1148a). This act makes provision for 3 percent interest on production disaster, economic disaster, and special livestock loans.

We recommend striking out both termination dates so the programs can be continued, where needed, beyond July 14, 1957, the termination date in existing law. We continue to urge removal of the words "for $2,500 or more" from the language of the act since this provision was repealed by Congress in Public Law 175 within a month of its original passage. We find the idea of a minimum loan as repugnant now as did the Congress in 1953. This language should be cleared up.

We also urge the following amendments to this act:

Provision should be made in subsection 2 (c) to authorize the expenditure of the proceeds of these special livestock loans to repay existing indebtedness.

The repayment period should be made "10 years" instead of "3." The existing congressional limitation of not more than 3 percent per annum interest on these special livestock loans should be made explicit in the language of subsection 2 (c), as it is in subsections 2 (a) and 2 (b). This would mean deletion of the fourth and fifth sentences of this subsection.

RECOMMENDED AMENDMENTS TO EMERGENCY LOAN ACT OF AUGUST 31, 1954

This is the Emergency Loan Act of August 31, 1954. Except for the new legislation, it would expire on June 30, 1957. The new law extends it to June 30, 1959.

We recommended the following amendments to this Act:

1. Remove the prohibition against the refinancing of existing indebtedness in section 1.
2. Eliminate the termination date in section 1 and thus establish a permanent authorization for the program.
3. Eliminate the requirement for proclamation of emergency area in section 1.
4. Eliminate the size of loan limitation in section 2.
5. Eliminate the limitation on amount of total indebtedness in section 2.

In our considered judgment, there are a great many individual emergency situations outside of areas of widespread emergency. Moreover, when a fully adequate family farmer is in an emergency situation a loan no larger than $15,000 is often not enough to get him out of his trouble and enable him to get into a position to overcome his temporary emergency financial difficulty.

AMENDMENT TO BANKHEAD-JONES FARM TENANT ACT, AS AMENDED

Suggested extension and expansion of the Bankhead-Jones Farm Tenant Act, as amended consist of suggested additional titles, and suggested amendments to titles I, II, and IV.

RECOMMENDED FAMILY FARM DEVELOPMENT ACT

A crash program to eliminate farm and rural poverty in the United States is provided for in H. R. 4300 introduced by Mr. Wright Patman.

We strongly urged that Mr. Patman's bill, in its entirety, be included in the comprehensive new law as a new title to the Bankhead-Jones Farm Tenant Act. This new title was not adopted.

RECOMMENDED TITLE V ECONOMIC EMERGENCY REFINANCING LOANS

We pointed out the need for a new title to provide a specific program of constructive rehabilitation credit to farmers, ranchers and farm-related small businesses in rural areas who are heavily indebted as the result of the farm depression that is no fault of their own. This new title was not adopted but several of its provisions were incorporated in the new law.

H. R. 11544 COMPARED WITH FARMERS UNION RECOMMENDATIONS AND ADMINISTRATION POSITIONS

Using Farmers Union recommendations as a measuring stick of relative adequacy, the following paragraphs set forth the major provisions and omissions of H. R. 11544 as adopted by Congress and compares them with the positions taken by the Eisenhower administration on the proposed legislation.

Farm ownership and real estate loans.—H. R. 11544 adopts Farmers Union proposal to authorize insured as well as direct loans for purpose of making "improvements needed to adjust farming operations to changing conditions." Adopts Farmers Union proposal to make existing farm owners clearly eligible for such loans, and to allow such loans to be made to farm owners and tenants who have had to seek outside sources of income to augment dwindling farm income (which must still be a "substantial portion" of the family income rather than "major portion" as in existing law).

Does not adopt Farmers Union recommendation to reduce interest rates on loans and eligibility requirements from 5 to 3 percent. Nor does bill eliminate the 5 percent limitation as recommended by the administration.

H. R. 11544 does not change the limitation in existing law that units financed must be of smaller value than "average value of efficient family-type farm units * * * in the county." Both Farmers Union and the administration urged elimination of this limitation.

Bill does not raise the authorized annual appropriation from $50 million to $150 million as recommended by Farmers Union; nor is amount appropriated for insured-loan revolving fund raised as recommended by Farmers Union. However, limitation on outstanding indebtedness in any one fiscal year on insured loans is raised as Farmers Union recommended.

Elimination of 10 percent equity requirement as recommended by Farmers Union is not included in H. R. 11544, except for refinancing loans. Administration recommended keeping equity requirement for all loans.

Payment by borrower of special fees and mortgage insurance premiums are not eliminated as recommended by Farmers Union.

"Until June 30, 1959," direct and insured FHA real estate or farm ownership loans may be made or insured, as recommended by Farmers Union, "for refinancing secured and unsecured indebtedness of eligible farmers on farms of not larger than family size who are presently unable to meet the terms of their outstanding indebtedness and are unable to refinance such debts" through private commercial channels "at rates and terms which they could reasonably be expected to fulfill."

This is done in H. R. 11544 by means of a new section 17 added to title I of the Bankhead-Jones Farm Tenant Act rather than as a new title V as proposed by Farmers Union, but with following exceptions it does provide the real estate refinancing lending authority recommended by Farmers Union. Farmers Union proposed that, in addition to individual farmers, the following also be made eligible for refinancing loans: "farm partnerships, grazing associations, irrigation companies, and the owners of farm-related small businesses in rural areas;" these were omitted in H. R. 11544.

Refinancing loans secured by farm real estate, under H. R. 11544, can be made up to the amount certified by the county committee to be the "value of the real estate" plus the "reasonable value of the applicant's livestock and farm equipment;" this is in substantial agreement with Farmers Union recommendation, if administered according to intent of the House. (Farmers Union has suggested a limitation of not less than $50,000 per farm.)

Eisenhower administration has steadfastly opposed the provision of authority for refinancing of existing indebtedness as an approved purpose of any type of FHA loan.

Operating loans (production and subsistence and rehabilitation loans).—Existing law sets 5 percent maximum interest rate for loans and eligibility. Farmers Union recommended cutting rate to 3 percent. Eisenhower administration recommended eliminating maximum. H. R. 11544 leaves 5 percent as the maximum rate chargeable.

Accepts Farmers Union proposal to allow borrowers to substantially augment from outside sources their dwindling farm income without losing eligibility for these loans.

Raises maximum size of initial loan from then-existing $7,000 to $20,000 rather than to $25,000 recommended by Farmers Union; maximum allowable total outstanding indebtedness is raised from $10,000 to $20,000 rather than to $40,000 as recommended by Farmers Union.

Farmers Union recommended elimination of 7-year repayment maximum: H. R. 11544 continues this provision but softens it by extending the 7-year period to "7 years plus number of years the area in which the borrower is located has been designated as a disaster area by the President," for such existing borrowers as may now be located in such a disaster area or who in the past had been a recipient of a disaster loan.

Recommendations by Farmers Union to simplify and improve efficiency of administration of uncollectible accounts are incorporated in H. R. 11544.

Authority for making refinancing loans secured by chattel mortgages as recommended by Farmers Union is included in H. R. 11544 as a new section 51, to title II of the Bankhead-Jones Farm Tenant Act, rather than as a new title V as recommended by Farmers Union. However, Secretary of Agriculture is authorized to make use of "operating loans" funds for "the refinancing of existing indebtedness." Such loans would be limited to $20,000 per borrower rather than $50,000 per borrower as recommended by Farmers Union. The loans would be at 5 percent interest rather than 3 percent, and the maximum repayment period would be 7 years rather than 15 years as recommended by Farmers Union. Such loans would be available only to farmers and stockmen; Farmers Union recommended that farm partnerships, grazing associations, irrigation districts, and "farm-related small businesses" also be made eligible to obtain these refinancing loans. Bill does not provide that such loans could be made to assist "eligible farmers and stockmen to purchase stock in irrigation companies or grazing associations." In fact such loans appear to be expressly forbidden by language elsewhere in the bill.

The Eisenhower administration opposed authorizing loans of any kind for refinancing of existing indebtedness.

OTHER SPECIFIC OMISSIONS OF H. R. 11544

H. R. 11544 as passed by the Congress includes no change in Water Facilities and Soil Conservation Loan Act.

No changes were made in disaster loan act, except to include in the report of the House Agriculture Committee Farmers Union recommendation to direct the Secretary of Agriculture to make orchard disaster loans (such as for Oregon prune orchard freeze) with reasonable repayment terms.

Farmers Union-recommended farm-loan and technical-assistance programs to assist low-income farm families to develop "economically adequate full-time and part-time" farms are, with exception of extremely long-term farm forestry loans, incorporated in the title I and title II revisions of the Bankhead-Jones Farm Tenant Act that are included in H. R. 11544. Maximum interest rates on such loans is set at 5 percent in the bill rather than the 3 percent recommended by Famers Union and the "no maximum" recommended by Eisenhower administration.

H. R. 11544 has no provisions for aid to low-income farmers respecting employment services for off-farm employment, no provisions for additional vocational education services, and no provisions for industrial dispersion to low-income farming areas.

However, provision for these latter were incorporated in a separate bill which passed the Senate and favorably reported by the House Banking and Currency Committee. Unfortunately, this bill died when House floor consideration was blocked by Executive Branch pressure. This bill would have designated rural-redevelopment areas as a section of a general depressed areas redevelopment program for both urban and rural areas of chronic unemployment and underdevelopment.

Economic disaster loans.—Farmers Union recommended that authority for this type of loan be made permanent legislation. H. R. 11544 extends the program through June 30, 1959. Interest rate is continued at 3 percent as recommended by Farmers Union. However, H. R. 11544 does not eliminate need for area to be "designated" before loans can be made; does not eliminate maximum size of $15,000 and maximum indebtedness of $20,000 as Farmers Union had recommended. H. R. 11544 increases from $15 million to $65 million the total amount of such loans that may be made. Farmers Union recommended no maximum limitation. H. R. 11544 does not permit such loans to be made for refinancing of existing indebtedness; Farmers Union had recommended that such be permitted.

VOLUNTARY FARM-DEBT ADJUSTMENT

H. R. 11544 includes Farmers Union recommendation for increased emphasis to Secretary of Agriculture to reactivate the voluntary farm-debt adjustment program that was so helpful to debt-ridden farmers in their attempts to climb out of the farm depression that started in 1920 and hit bottom in 1932. Eisenhower recommendations did not mention farm-debt adjustment as a needed activity.

REESTABLISHMENT OF FULLY EFFECTIVE VARIABLE REPAYMENT PLANS

H. R. 11544 does not authorize reestablishment of authority for utilization of a fully effective variable repayment plan, without regard to previous excess payments. Farmers Union recommended that the Secretary be authorized to adjust repayments on all types of FHA loans to the new earnings and ability of the borrower to repay from year to year. Existing law, left unchanged by H. R. 11544, allows such variable repayment adjustments only in cases where the borrower has gotten ahead of schedule in previous years.

OPPOSITION ARGUMENTS

Following is the official executive branch recommendation opposing enactment of S. 3790 which would greatly improve the "Yardstick" family farm credit program of Farmers Home Administration.

JULY 3, 1956.

Hon. ALLEN J. ELLENDER,
Chairman, Committee on Agriculture and Forestry,
United States Senate.

DEAR SENATOR ELLENDER: This is in reply to your request of May 9 for a report on S. 3790, a bill to strengthen the Nation by providing auxiliary credit resources required to preserve the family-size farm, providing additional credit for farm enlargement and development, refinancing of existing indebtedness, expansion, and simplification of farm ownership and operations credit programs by amendment of the Bankhead-Jones Farm Tenant Act, and extension and simplification of emergency and disaster farm credit by amendment of the Acts of April 6, 1949, as amended, and of August 31, 1954, and for other purposes.

The Department recommends that the bill not be passed.

The bill would amend the Bankhead-Jones Farm Tenant Act, the Water Facilities Act of 1937, Public Law 38, and Public Law 727. In addition, it would add two new titles to the Bankhead-Jones Farm Tenant Act; namely, title V, "Rural Adjustment Credit," and Title VI, "Family Farm Developing Act." The Department recognizes that some changes are needed in its existing credit authorities and is in agreement with some of the objectives of the bill, particularly those which would extend and improve the credit services available to farmers under Titles I and II of the Bankhead-Jones Farm Tenant Act. The specific recommendations of the Department have been submitted to the Congress and are embodied in S. 3429 and S. 3559.

One of the reasons enactment of S. 3790 is not recommended is that this bill would change substantially the character of the credit services of the Department and make it directly competitive with private and cooperative lenders. This position would be in sharp contrast to the present status of the Department in the farm credit field; namely, as a supplementary source of credit to be used only when applicants cannot obtain loans from other creditors at reasonable rates and terms. More specifically, the bill would provide that applicants who could not obtain credit for real estate and operating purposes from other sources at rates of not more than 4 percent would be eligible for loans under the Bankhead-Jones Farm Tenant Act. Since the going rate of farm loans, particularly operating loans, is more than 4 percent, most farmers who need credit could establish their eligibility for assistance under the Bankhead-Jones Farm Tenant Act. Increasing the loan limits on title II loans to $40,000, eliminating the 7-year continuous indebtedness period, as well as authorizing chattel and real-estate loans up to $50,000 under title V of the proposed bill, would permit loans to farmers and stockmen whose operations are substantially larger than family size. At present, loans under the Bankhead-Jones Farm Tenant Act can be made only to farmers whose operations are not larger than family size.

The minimum 3-percent interest rate for insured loans specified in S. 3790 would make the insured loan authorities practically inoperative in the current money market. Our experience has been that at present a 3-percent interest rate is not sufficiently attractive to lenders to assure an adequate supply of funds for insured farm ownership and soil and water conservation loans. This provision, unless compensated for by increased direct appropriations, would curtail rather than expand the credit facilities available to farmers.

The bill proposes a number of lending authorities which are not directly related to extension of credit to bona fide farmers. Title V, for example, authorizes loans to "farm-related small businesses." This type of credit program should be administered by an agency other than the Department of Agriculture. Title VI includes loan authorities with respect to both farm and nonfarm aspects of a comprehensive rural development program. Since the Bankhead-Jones Farm Tenant Act is primarily a credit statute, this Department is of the opinion that the portions of title VI that pertain to phases of a comprehensive rural development program other than credit to farmers are not germane to the Bankhead-Jones Farm Tenant Act.

The bill, if enacted, would establish additional lending authorities under the various titles which would differ in only minor respects. These small differences with respect to eligibility, loan purposes, and terms of loans would be difficult to explain to farmers and would unnecessarily complicate the administration of the Department's credit services. Furthermore, there would be considerable duplication of lending authorities under the various titles for chattel and real-estate purposes.

The Bureau of the Budget advises that there is no objection to the submission of this report.

Sincerely yours,

TRUE D. MORSE, *Acting Secretary.*

CONCLUSION

Relating to the need for a comprehensive "yardstick" family farm credit agency, James G. Patton told the Senate Agriculture Committee on June 7, 1955:

"The credit needs of family farming are tremendous and growing. Credit should be available at the times needed and its terms and conditions should be adopted to characteristics of farming as a combined business and way of life.

"Much of the credit needs of family farming can be met by loans obtained from private individuals and such credit institutions as banks and insurance companies. Farmers themselves can meet other needs cooperatively through the institutions of the farm credit system. Together, it should be expected that these sources should supply the great bulk of the credit needs of agriculture. However, inasmuch as all of these must obtain their funds from commercial money markets and conduct their operations along traditionally conservative financial lines, they find themselves unable to perform the entire farm credit job. Such institutions find it difficult to pioneer in the meeting of newly recognized or newly emerging farm credit problems. They are not set up to use their credit resources in meeting the high risk needs of severe disasters and emergencies, economic or natural. They cannot afford to participate in credit operations when a relative high intensity of technical assistance and loan servicing are required to render loaning activities essentially sound from a strictly financial viewpoint. Moreover, all of these private individual corporate and cooperative institutions have a marked tendency in the absence of outside stimulation to become traditional, custom-bound, and increasingly restrictive in their credit policies.

"There is nothing morally wrong about this nor even economically unsound. It just means that the best interests of family farmers require a separate supplemental and yardstick credit operation. This can best and most efficiently be supplied to the Nation by the Federal Government. Such an agency should have the legal authority and sufficient funds to meet all of the family farm credit needs not filled on reasonable terms by private cooperative and other corporate lending agencies.

"This is a problem not strictly of young farmers, nor of low-income farm families, nor of disaster situations. It is a need that extends across the board. Such an agency would stand ready to meet any legitimate farm credit need not met by existing private agencies on reasonable terms. The agency would make both direct governmental loans and would insure loans of private lending agencies."

BIBLIOGRAPHY

1. S. 3790, Family Farm Credit Act, introduced by Senator Humphrey and other Senators.
2. House Report No. 2260, Farm Loan Programs.
3. Acts of Congress administered by Farmers' Home Administration, compilation.

Mr. BAKER. Farm people are concerned not only with their own income and credit prospects and opportunities. We know that farm people cannot prosper in a nation with a weak financial structure nor one primarily dominated by bankers alone. We are, also, interested in keeping opportunity open and encouraging to small-business men in rural and urban areas, in making adequate consumer credit available at reasonable rates to wage and salary employees of private and public institutions, and in providing the social and credit capital investments required to maintain a constantly and rapidly expanding national economy.

Andrew Jackson's successful fight to gain control of the banking system for the common people is a part of our organization's tradition and of the Nation's heritage.

It seems appropriate that the draft bill before your committee should bear the name of a Senator from the same State as Carter Glass, of Virginia, the author and protagonist who brought about the adoption of the great financial reforms embodied in the original Federal Reserve Act.

We urge that you conduct your deliberations and make your decisions in the great traditions of Andrew Jackson and Carter Glass. And I know that all or most of your members agree with us that the financial institutions of this Nation exist to serve the people of our Nation and not the other way around.

We are convinced that the national welfare depends upon control over the financial institutions of the Nation by democratic political processes as directly as is consistent with efficient and effective management and administration and not official encouragement of cooptation of that function by semipublic boards of bankers' representatives. This has been a continuous and significant fight throughout the history of America.

I have full confidence in this committee and the Senate to make sure that whatever amendments they make to existing Federal laws regulating our financial institutions will move in the direction of greater control by and service to the people as a whole rather than giving primary attention to the power drives of those who by control of great wealth could in the absence of Federal regulation demand and obtain their Shakespearean "pound of flesh."

Other than this general statement, we do not wish to direct any statement toward most of the specific provisions of the proposed bill, except those relating to the Federal Credit Union Act.

Farmers Union is very much interested and concerned about the welfare of credit unions. Many farmers are members of credit unions. Moreover, credit unions were organized and do operate to provide additional bargaining power in the money markets for little people of all walks of life who, like farmers, find themselves in a grievously disadvantaged bargaining position in respect to those who control large accumulations of wealth and credit. The individual farmer or consumer is almost completely without bargaining power if he must go, almost literally, with hat in hand and knock on the front door of Wall Street to obtain a needed loan. Credit unions allow such litttle people with but small amounts of accumulated wealth of their own to put their financial resources into a joint pool and combine their strength to the mutual protection of themselves.

Most credit unions have been successful in their efforts; and some have become financial institutions of considerable size and strength. We are told that the big-money interests have now withdrawn their objections to the small-loan business of credit unions but are beginning to view with alarm the growing ability of credit unions to make loans, for example, of sufficient size to a family farmer to finance his land purchase and equipment.

Remembering that many economically adequate family farms in many areas of the Nation involve a capital investment of as much as $150,000 to $270,000, I suggest the need to maintain as in existing law the definite legal authority of credit unions to make individual loans up to 10 percent of the unimpaired capital and surplus. We do not fear that loan committees of credit unions, being made up as they are of members of the institution and not subject to control of management but elected by members directly, will squander assets nor make unwise large loans. Nor do we believe that credit unions will be able or willing to make so many large loans that they will become a legitimate threat to the financial integrity, nor even a sizable competitive force against the other large financial institutions of the Nation.

As a matter of fact, existing law now provides the same limitation on the size of single individual loans for credit unions as for the institutions that come under the Federal Bank Act.

We believe that continuation of this provision of existing law is vital to continued service and significance of credit unions, which now have some 10 million members in the United States and about $3 billion of assets. Credit unions are still growing as little people make increasing provision to protect their interests in ther own credit resources. There are farmer credit unions, and labor credit unions, church membership credit unions and community credit unions. This type of local economic self-protection needs to be encouraged and permitted to grow. It should not be knocked in the head at its growing edge, the right to make larger loans within the safe limits of net worth where such loans are required to further the aims for which credit unions were originally organized.

We, therefore, strongly urge that your committe delete from the proposed bill the provisions that will eliminate from existing law the legal right of credit unions to make individual loans up to a maximum size of 10 percent of unimpaired capital and surplus.

Senator ROBERTSON. We have been glad to hear your views and we authorized you to put in the record your memorandum of August 30 called Legislative Analysis, Memorandum No. 56–17, Revision No. 1.

Mr. BAKER. Thank you, sir.

Senator ROBERTSON. The chairman has made just a hasty examination of the various things covered by that memorandum but he has reached the impression that all of them or practically all of them are outside the jurisdiction of this committee.

Mr. BAKER. That is correct, sir.

Senator ROBERTSON. You want to show the whole credit structure in which your organization is interested?

Mr. BAKER. That is correct; yes, sir.

Senator ROBERTSON. Any questions?

Senator BENNETT. No questions.

Senator ROBERTSON. If not, we thank you.

The committee now stands in recess until 10 o'clock tomorrow.

(Whereupon, at 11:20 a. m., the subcommittee recessed until 10 a. m. the following day, Thursday, January 31, 1957.)

STUDY OF BANKING LAWS

(Financial Institutions Act of 1957)

THURSDAY, JANUARY 31, 1957

UNITED STATES SENATE,
COMMITTEE ON BANKING AND CURRENCY,
SUBCOMMITTEE ON BANKING,
Washington, D. C.

The subcommittee met, pursuant to recess, in room 301, Senate Office Building, at 10:05 a. m., Senator A. Willis Robertson (chairman of the subcommittee) presiding.

Present: Senators Robertson, Frear, Clark, Bricker, and Bush.

Senator ROBERTSON. The committee will come to order.

The first witness today will be Mr. Sam M. Fleming of Nashville, Tenn., representing the Association of Reserve City Bankers.

The committee will be glad to hear Mr. Fleming.

STATEMENT OF SAM M. FLEMING, APPEARING ON BEHALF OF THE ASSOCIATION OF RESERVE CITY BANKERS

Mr. FLEMING. Thank you, Senator. Shall I proceed, Senator?

Senator ROBERTSON. You may proceed.

Mr. FLEMING. Mr. Chairman and members of the committee, my name is Sam M. Fleming. I am president of the Third National Bank in Nashville, Tenn. I am also a member of the committee on Federal relationship of the Association of Reserve City Bankers. I have been asked by the president of the association, James D. Robinson, Jr., chairman of the board of the First National Bank of Atlanta, to represent the association before this committee today.

The Association of Reserve City Bankers is an organization of senior executive officers of banks located in Reserve or central Reserve cities which do a correspondent banking business. The Association was founded in 1912 to promote the general interest of banking with particular reference to the banking business located in Reserve and central Reserve cities. It has a present membership of 400.

These hearings are being held to consider the tentative bill entitled the "Financial Institutions Act of 1957."

Essentially, this bill is the result of the recognition by the members of this committee of the need for a technical revision of the Federal laws affecting financial institutions. As Senators Fulbright and Robertson have pointed out in statements made from time to time in connection with the study which preceded this bill, there has been no major overhaul or revision of the Federal laws relating to our private financial institutions since the passage of the acts of the early thirties. Generally, in the area of banking, legislation enacted in the intervening period has taken the form of isolated amendments. The result has been a continuing patch job on existing laws. Over the years many of the provisions of existing law have become obsolete or unnecessary. Other provisions have been found to be technically or substantively inadequate to meet the requirements imposed on banking by the changing needs and patterns of the business, industrial, and agricultural community. Additional or amended authority is needed in certain areas to facilitate the service our financial institutions render to their communities.

In our opinion the design of this bill is to be commended. In effect, if enacted, it would rearrange and recodify the Federal laws relating to our primary private financial institutions. Each title of the bill largely embraces the provisions of law applicable to the type of financial institution affected. Thus, title I, the National Bank Act, largely contains the body of laws affecting national banks. By thus bringing these laws together in one title the task of the supervisory authority, the banker and lawyer should be greatly facilitated.

In the existing laws there are many instances of overlapping and duplicate provisions, the elimination of which will be a practical and worthwhile result.

A further benefit of the enactment of the bill is apparent in the organization and arrangement of the provisions of Title I. Many of the provisions of existing law affecting the powers and duties of national banks are scattered through title 12 of the United States Code. By comparison, these provisions are brought together and logically arranged under chapter 6 of title I of this bill. This would obviously facilitate quick access to a particular provision.

Another practical advantage of this bill derives from the elimination of obsolete or unnecessary provisions of existing law, which now serve only to clutter up the statute. Title I of this bill, for example, eliminates from existing law provisions applicable to national banks which have expired by their own terms; provisions relating to the circulation of notes by national banks, which provisions have long not been in use and are not likely to be used in the future; and provisions relating to governmental institutions which have been dissolved. Similarly, title II of this bill, the Federal Reserve Act, reflects the elimination of many obsolete provisions now found in the existing Federal Reserve Act relating, for example, to the organization of Federal Reserve banks.

Many other such examples could be cited to show how the existing law would be improved by the elimination of obsolete, unnecessary, overlapping, or duplicate provisions contained in it.

This bill, if enacted, would make many technical changes in existing law. Under title 12, United States Code, section 24, for example, it is not clear that a national bank may make contributions to educational and civic improvement organizations. Under this bill a national bank is expressly authorized to make such contributions. Further, under present law, contributions by a national bank may not be made to funds or instrumentalities to which a State bank located in the same State is expressly prohibited from contributing under the law of that State. Under this bill the authority of a national bank to make authorized contributions would not be dependent on the law of the State in which it is located. Thus, this provision makes a technical as well as a minor substantive change in existing law.

Similarly, under present law a national bank continuing to operate after merger or consolidation with another national bank or State bank must again secure the approval of the Comptroller of the Currency to operate branches it lawfully had in operation immediately prior to the merger or consolidation, establishment and operation of which branches had already been approved by the Comptroller of the Currency. This new bill dispenses with this burdensome and technical requirement. There are many other such technical changes in this bill.

Amended authority is provided in this bill with respect to certain lending authority of national banks. Thus, for example, this bill would amend exception 6 of section 5200 of the Revised Statutes to permit a national bank to lend one obligor not more than 25 percent of its capital and surplus against insurable, perishable, readily marketable staples under refrigeration for a period not exceeding 6 months. Under present law, readily marketable staples must be nonperishable in order to qualify as security under exception 6 of the above-cited provision. A national bank will also be permitted under this bill to acquire to a limit of 25 percent of capital and surplus obligations from dealers of dairy cattle arising out of the sale of dairy cattle which bear a full recourse endorsement or unconditional guarantee of the dealer. Section 84 of title 12 of existing law poses unnecessary and undesirable obstacles to the financing of business, industry or agriculture, and I shall speak specifically of several of these later on in this statement.

There are many provisions of title I of this bill which would tighten existing law affecting national banks. By way of illustration, the present law with respect to the declaration and payment of dividends by a national bank would be amended under this bill to require the specific approval of the Comptroller of the Currency where the total of all dividends declared in any calendar year by a national bank exceeds its total net profits for that year plus its retained net profits of the preceding 2 calendar years. The requirement of present law that the stock of a national bank must be 50 percent paid in before such a bank is authorized to commence business is amended to require 100 percent payment. Under present law negotiable recourse installment paper may be acquired by a national bank without limitation. Under this bill a limitation of 25 percent of capital and surplus is imposed on the amount of such paper a national bank may acquire from one customer unless the bank certifies in writing that it is relying on the maker rather than the endorser of such paper. Under present law shareholder approval is not required with respect to a bulk sale of the assets of a national bank preliminary to voting the bank into voluntary liquidation. Under this bill approval by a two-thirds vote of the shareholders would be required to authorize such a sale unless, in the case of an emergency, the Comptroller specifically waives this requirement.

There are, Mr. Chairman, certain provisions of this bill which I should like particularly to emphasize. Section 23 of title III of the bill, the Federal Deposit Insurance Act, provides that no insured bank shall enter into any merger, consolidation or assumption transaction with any other bank, without the prior written consent of the Comptroller of the Currency if the resulting bank is a national bank, of the Board of Governors of the Federal Reserve System if the resulting bank is a State member bank, or of the Federal Deposit Insurance Corporation if the resulting bank is a nonmember insured bank. This recommendation would require the Comptroller of the Currency, the Board of Governors, or the Federal Deposit Insurance Corporation, as the case may be, in granting or withholding consent, to consider the competitive or monopolistic aspects of any proposed merger, consolidation, or assumption transaction, which they are not now by existing statute required to do.

Senator ROBERTSON. Will you yield there for a suggestion?

Mr. FLEMING. Yes, sir.

Senator ROBERTSON. Before I comment on that statement, I want to say in effect that it is very helpful to all bankers and financial institutions, and to Member of Congress, to know that an organization like the one for which you speak has made a very careful examination of the provisions of this bill now coming before us.

You mentioned items in the bill which have your approval. You have approved this provision for a new law on bank mergers and have pointed out at the present time there is no State law and there is no Federal law which requires consideration to be given to the competitive situation and possible monopolistic situation.

Mr. FLEMING. That is correct, sir.

Senator ROBERTSON. This bill supplies that defect.

Mr. FLEMING. That is correct, sir.

Senator ROBERTSON. You know, of course, that the language in the bill is the exact language of the Fulbright bill that the Senate passed last year, but which did not get through the House.

Are you aware of the fact that every State has an antimonopoly law dealing with the merger of State banks?

Mr. FLEMING. No, sir. I was not aware of that.

Senator ROBERTSON. I understand that is correct. I have heard some little criticism voiced—I do not remember it last year, but I have heard it voiced this year—that we are not giving due consideration to State authorities when we let the Federal Deposit Insurance Corporation do this. The FDIC jurisdiction over a nonmember bank because of a Supreme Court decision that if a bank voluntarily takes out Federal insurance it submits itself to Federal control. That is something we in the South have always said, that is, that you cannot get Federal aid without Federal control, and in the case of schools or other institutions it is going to come sooner or later. As an illustration of that principle, when the State banks got their deposits insured first for $5,000 and then for $100,000, the Supreme Court said "The Federal Government has got you now."

Some State bank authorities think we have gone too far in letting a Federal agency like the Federal Deposit Insurance Corporation pass on the merger of State banks. I wish to call attention to the fact that before the application of two State banks to merge can ever get to the Federal agency, it must get past its own State authority, and there is such State authority in every State. They have to approve the application first. For that reason I feel that the fears voiced to me recently and which may be voiced again to me that we have not given due consideration to the States in this merger provision, are not justified.

In any event, I would not know how to pass a Federal law giving a Federal official the power to do something, and giving a State official the power to nullify what he is going to do. One or the other has to have the authority. There is no provision under our Constitution that they can act jointly or that the Federal Government can pass a law and then say that it shall be administered by some State official.

I just wanted to bring that out in connection with this. Of course, we are pleased to have the endorsement of the reserve city bankers of this and other provisions.

You may proceed.

Mr. FLEMING. I think that is a very appropriate statement, Senator Robertson.

The enactment of this proposal, previously incorporated in S. 3911, passed by the Senate but not by the House of Representatives in the 84th Congress, would enable the bank supervisory authorities to deal more effectively with merger, consolidation, and assumption transactions. It would place in the bank supervisory authorities final authority to pass on the competitive and other aspects of any such transactions. Banking is a supervised and regulated industry and in our opinion the respective bank supervisory authorities are best qualified by virtue of their intimate knowledge and long experience with banks under their supervisory jurisdiction to pass with finality on both the banking and competitive aspects of any such transactions. No logical reason is seen why authority over such transactions engaged in by banks should be vested in any Government agency other than the banking supervisory authorities. Further, the designation of another Government agency, foreign to the banking business, to exercise a major area of control over the banking business would result in a divisive, harmful, and burdensome regulation of the banking business which would not contribute to the public interest, the health of the banking business, or sound regulation.

I believe, Mr. Chairman, that that is in accord with the statement you have just made.

Senator ROBERTSON. Thank you.

Senator BUSH. You are discussing a situation which is not in this bill. No other agency than those mentioned is to be consulted in the matter of a merger; is it?

Mr. FLEMING. The point is——

Senator BUSH. You are discussing a bill which we had last year which would give the Department of Justice a position in this.

Mr. FLEMING. Only indirectly. I believe the point here is that the supervisory authorities must consider the competitive feature, Senator Bush, as well as the practical feature of any merger. At the present time the law does not require or even indicate that they should consider anything in respect to competition.

We feel that the supervisory authorities should have it spelled out that they should consider the competitive angle as well as the practical angle.

Senator BUSH. Does this bill specifically require them to do that?

Mr. FLEMING. Yes, sir.

Senator BUSH. It does?

Mr. FLEMING. It does.

Senator BUSH. That does away, really, with the argument in favor of the Department of Justice getting into this, which was up before this committee last year; is that not right?

Senator ROBERTSON. That is correct. We preferred the approach of the banking agencies to handle this, to the Celler proposal, which passed the House and came over to us, that this should be referred to the Department of Justice.

Senator BUSH. This bill would require 2 out of these 3 Federal agencies to approve of the merger, provided that the merger involved insured banks.

Mr. FLEMING. If it involved the merger of a State bank with a national bank, it might to a certain extent, Senator. If it involved the merger of a national bank with another national bank it would not.

Senator BUSH. If it involved two national banks, both insured, it would involve the Federal Reserve Board and the Federal Deposit Insurance Corporation.

Senator ROBERTSON. No. Only the Comptroller of the Currency.

Senator BUSH. Is that right?

Senator ROBERTSON. Yes. The Federal Reserve Board gets the member banks, the State member banks, and the Comptroller gets the national banks.

Senator BUSH. The Federal Reserve Board comes in where you cross a State line. Where you have a National and State bank merging; is that right?

Senator ROBERTSON. If just State banks are involved, as I said before, the State agency has to act first or the Federal agency will not even consider it.

Senator BUSH. If you have two State banks merging and they are both members of the Federal Reserve System, then the Federal Reserve comes in; do they not?

Senator ROBERTSON. That is right; if they are members.

Senator BUSH. And so does the Federal Deposit Insurance Corporation if those banks are insured.

Mr. FLEMING. Maybe I could answer that question a little bit better if I would read again the one statement I made in that connection earlier. May I?

Senator BUSH. What page are you on?

Mr. FLEMING. At the top of page 6.

* * * the Federal Deposit Insurance Act, provides that no insured bank shall enter into any merger, consolidation, or assumption transaction with any other bank, without the prior written consent of the Comptroller of the Currency if the resulting bank is a national bank, of the Board of Governors of the Federal Reserve System if the resulting bank is a State member bank, or of the Federal Deposit Insurance Corporation if the resulting bank is a nonmember insured bank.

Senator BUSH. My question still remains. Should it not read "and of the Federal Deposit Insurance Corporation if the resulting bank is insured"?

Mr. FLEMING. I think only when you cross lines that would apply. As long as a merger stays within the category of either the Federal Deposit Insurance Corporation or the Comptroller of the Currency or the Board of Governors of the Federal Reserve System it would not be necessary to have over one of the supervisors approve it.

Senator ROBERTSON. The Chair would like to point out that the emphasis is put on the word "resulting." That determines jurisdiction. If it is a national bank the jurisdiction is in the Comptroller of the Currency. If it is a member bank but not national there is jurisdiction in the Federal Reserve Board. If it is a State bank and a nonmember bank, jurisdiction is with the Federal Deposit Insurance Corporation, and they get that only because of the insurance.

Senator BUSH. I am still not clear on where the Federal Deposit Insurance Corporation is excluded.

Senator ROBERTSON. On nonmember State banks.

Senator BUSH. Nonmember?

Senator ROBERTSON. Nonmember State banks. If there are 2 or more State banks that are going to merge into 1 State bank. They all started out State banks and are going to wind up State banks, but they are all insured.

Senator BUSH. So they are not under the jurisdiction of the Comptroller.

Senator ROBERTSON. That is right.

Senator BUSH. And not under the jurisdiction of the Federal Reserve.

Senator ROBERTSON. That is right. But they are under the jurisdiction of the Federal Deposit Insurance Corporation, but that jurisdiction does not come to the Federal Government until the proposed merger has first been approved by State authorities.

Mr. FLEMING. That is correct.

Senator BUSH. But if they are insured?

Senator ROBERTSON. Then we have jurisdiction.

Senator BUSH. The Federal Deposit Insurance Corporation has jurisdiction?

Senator ROBERTSON. That is right.

Senator BUSH. Here is the point I am really getting at. Are there any of these mergers under this proposed legislation which are going to require the approval of two Federal agencies?

Mr. FLEMING. Could I answer that?

Senator ROBERTSON. You can answer that, yes. There may be a few instances where it could be possible.

Mr. FLEMING. If you had a State bank that was a member of the Federal Reserve System that was to merge with a nonmember bank that was a State bank, then you might have to have the approval of both the Federal Reserve Board and the Federal Deposit Insurance Corporation.

Senator BUSH. Is that so? Because it says, "If the resulting bank * * *." The jurisdiction is determined by what the resulting bank is. Is that not true?

Senator ROBERTSON. The jurisdiction is determined by what the resulting bank will be.

Senator BUSH. Under that understanding I still ask—and if the witness is not sure I will be glad to ask the chairman——

Senator ROBERTSON. I will let my counsel speak.

Senator BUSH. Is it likely a case will come up under this bill where two Federal agencies have to examine and approve the merger?

Senator ROBERTSON. I will let our counsel, Mr. Don Rogers, give us his opinion on that.

Mr. ROGERS. When you look at the end result I do not think it would be possible to have two Federal agencies.

Senator CLARK. I cannot hear you.

Mr. ROGERS. I do not think it is possible to have 2 Federal agencies passing on it, because you look at the end result and only one of the 3 has jurisdiction in the bill. There is a provision that all of these—

on the competitive factors all 3 agencies will consult with one another, so that they have a uniform pattern of approval; but it is certainly not contemplated that 2 agencies would have to pass upon it.

Senator BUSH. I do not wish to delay the gentleman any further, but I think it ought to be examined because it still is not clear to me that there cannot be two agencies having jurisdiction in this merger.

Senator ROBERTSON. We will look into it further.

Senator BUSH. I would like to have it made very clear as to whether or not there is a possibility under this bill for that. Then I would want to be convinced it is necessary to have two agencies of the Federal Government approving a merger.

Senator ROBERTSON. This bill, as we pointed out, contains the exact language of the bill that this committee approved last year, and the Senate passed. We think when final action is taken there will be only one Federal agency that has jurisdiction to act but, as our counsel has mentioned, it is possible that all agencies will be consulted.

Senator BUSH. That is desirable.

Senator ROBERTSON. That is right. Then if you look, as we believe, at the end result of what the bank will be after the merger has been accomplished, then that determines who has jurisdiction; and we think under the provisions of the law as we propose it, it is exclusive.

Senator BUSH. It still appears from the gentleman's testimony that in the end result when you have a bank and you say what is it going to be, it may well be a member bank and a member of the Federal Deposit Insurance Corporation. Therefore, under this language it would appear to me they both might have jurisdiction over the merger, and that is what I want to find out.

Mr. ROGERS. No. On a member bank it would always be the Federal Reserve Board.

Senator BUSH. Yes.

Senator ROBERTSON. If it is going to stay a member bank.

Senator BUSH. This language says:

> or of the Federal Deposit Insurance Corporation if the resulting bank is a nonmember insured bank.

If it is both a member bank and an insured bank, which has jurisdiction?

Mr. ROGERS. The Federal Reserve Board.

Senator BUSH. Is that clear in the law?

Mr. ROGERS. It is.

Senator BUSH. It is?

Mr. ROGERS. Yes.

Senator BUSH. And the Federal Deposit Insurance Corporation is excluded?

Mr. ROGERS. Yes.

Senator BUSH. If that is the case, it is all right.

Senator ROBERTSON. The biggest merger we had in recent years was Chase and Manhattan—Chase a national bank and Manhattan a State bank. Chase gave up its national charter and merged with the State bank and became a State bank after it was merged.

If that had happened under our law the Federal Deposit Insurance Corporation would have had to pass on it after the State of New York had approved the merger.

Senator BUSH. But the Federal Reserve would not have?

Senator ROBERTSON. Nobody except the Federal Deposit Insurance Corporation in that instance.

Senator BUSH. Why was the Federal Reserve excluded in that case?

Senator ROBERTSON. Because the Federal Reserve never had jurisdiction. If it was a national bank it would have been the Comptroller. He lost his jurisdiction when they gave up their charter.

Senator BUSH. But the resulting bank is a member of the Federal Reserve System.

Senator ROBERTSON. That may be true. Yes; it is true. It is a member of the System.

Senator BUSH. Then why does the Federal Reserve not have jurisdiction over that merger under this law?

Senator ROBERTSON. Because the way this law is framed—our counsel says, yes. If this is a member bank, that is the end result. The Federal Reserve System does have jurisdiction over it.

Senator BUSH. And how is the Federal Deposit Insurance Corporation excluded then?

Senator ROBERTSON. Because it only has jurisdiction of nonmember banks. If the end result is a nonmember bank and that is what it is going to be after it is merged, then the Federal Deposit Insurance Corporation and nobody else has jurisdiction there.

Senator BUSH. It has to be a nonmember State bank in order for the Federal Deposit Insurance Corporation to have jurisdiction?

Senator ROBERTSON. That is correct.

Senator BUSH. Is that right?

Senator ROBERTSON. That is correct.

Senator BUSH. And only under those circumstances?

Senator ROBERTSON. That is right.

Mr. FLEMING. I think, Senator Bush, if I might make one other statement, Mr. Chairman——

Senator ROBERTSON. All right.

Mr. FLEMING. I believe in line with what Mr. Rogers just said, it is quite clear that the supervisory authority over the resulting bank is the authority that must have and make the final decision—the resulting bank. That means there are three agencies that would have the authority of approving the merger, depending upon what the resulting bank is going to be.

Let us just give three illustrations on that. If the resulting bank is going to be a national bank, then the Comptroller of the Currency would have the final decision. If the resulting bank is going to be a State member bank, that means, a State bank which is a member of the Federal Reserve System, then the Board of Governors of the Federal Reserve System would have the authority. But if the resulting bank is going to be a nonmember insured bank, then the Federal Deposit Insurance Corporation would have the final authority.

However, as Senator Robertson and Mr. Rogers both pointed out——

Senator BUSH. A nonmember insured State bank?

Mr. FLEMING. That is right. A nonmember insured State bank only.

But, as Senator Robertson and Mr. Rogers both pointed out, there is bound to be a great deal of consultation between the various supervisory authorities before the merger comes to that final point.

Senator BUSH. All right. I do not want to delay it any further. Thank you.

Mr. FLEMING. May I proceed?

Senator CLARK. Could I ask one question?

Senator ROBERTSON. Senator Clark.

Senator CLARK. Mr. Fleming, I would like you to turn to page 7 of your statement, if you will. You are still commenting there, as I take it, on section 23 of title III, and I would like to ask you just exactly what you mean by that first full sentence, which reads:

> Further, the designation of another Government agency, foreign to the banking business, to exercise a major area of control over the banking business would result in a divisive, harmful, and burdensome regulation of the banking business which would not contribute to the public interest, the health of the banking business, or sound regulation.

Did you have the Attorney General of the United States in mind in that sentence?

Mr. FLEMING. We had the Justice Department in mind, sir, because that body had been discussed before when the bill was brought before the Senate. We feel that banking is a specialized and regulated business, and any matters of this importance can best be passed on by the particular supervisory authority that is intimately in touch with the day-to-day operations of banking.

Senator CLARK. What is your position, then, with respect to the provision in section 23 which calls for the rendering of an opinion by the Attorney General on the request of the appropriate agency with respect to whether a proposed merger would violate the Sherman Act or the Clayton Act, as well as the provisions of this section?

Mr. FLEMING. We feel when there was included in this bill the provision that the Comptroller of the Currency, or the Federal Reserve Board, or the Federal Deposit Insurance Corporation, must consider the competitive angle, that we have to a great extent precluded the necessity of such an opinion.

Senator CLARK. I understand your position. I am not at all sure I agree with you.

Mr. FLEMING. May I proceed, Mr. Chairman?

Senator ROBERTSON. You may proceed.

Mr. FLEMING. Sections 8 and 17 of title II of the tentative bill, the Federal Reserve Act, would limit the terms of service of members of the Federal Advisory Council of the Board of Governors of the Federal Reserve System and of the directors of the Federal Reserve banks. Section 8 provides that a member of the Federal Advisory Council who has served 6 full consecutive terms of 1 year each shall not be eligible to serve again in such capacity, until after an intervening period of not less than 3 years.

Section 17 of the tentative bill provides that a director of a Federal Reserve bank who has served 2 full consecutive terms of 3 years each shall not be eligible to serve again in such capacity until after an intervening period of not less than 3 years (except that a director designated as chairman may serve 3 full consecutive 3-year terms without such an intervening period). There are no such limitations in present law with respect to the terms of service of directors of the Federal Reserve banks or members of the Federal Advisory Council.

These provisions of the tentative bill follow the recommendations made to the Senate Banking and Currency Committee by the Board of

Governors. These recommendations of the Board of Governors were carefully considered by the advisory committee to the Senate Banking and Currency Committee. The advisory committee disapproved these recommendations of the Board of Governors on the ground—

that the advantages of preserving and promoting the autonomy of the Federal Reserve banks outweigh the possible benefits from rotation and the present system has been beneficial.

We are in agreement with the recommendation of the advisory committee and see no strong reason for thus limiting the terms of office of directors of the Federal Reserve banks or members of the Federal Advisory Council. Classes A and B directors are elected by the member banks in each Federal Reserve district, and the directors of each Federal Reserve bank annually select one member of the Federal Advisory Council from that Federal Reserve district. Thus, both in the case of the election of these directors and in the selection of Federal Advisory Council members, the power of appointment effectively resides in the member banks of each district. We believe it is important to retain this degree of autonomy of each Federal Reserve district without any such restraint as would be imposed by the provisions of the bill now in question. If the Congress nonetheless deems it advisable to impose any limitation on terms of service of Reserve bank directors and of Federal Advisory Council members, we suggest that any such limitation should apply only in respect to the terms of Reserve Bank directors or Federal Advisory Council members appointed or elected subsequent to the enactment of this act.

Another provision of this bill which we should like to underscore is the authority granted to national banks under sections 20 and 21 of title I to issue and have outstanding preferred stock, capital notes, and debentures. Under present law, a national bank may issue preferred stock under section 301 of the Emergency Banking Act of 1933 (12 U. S. C. 51a), but as this and related provisions are presently worded the use thereof at least suggests that the issuance is by way of an emergency. Further, under present law a national bank cannot issue debt obligations as a means of acquiring additional capital.

The restrictions of present law on the acquisition of additional capital by banks are not in our judgment reasonable. There are times, such as at present, when banks should have access to additional capital without total reliance on common stock. In some circumstances, preferred stock or debenture issues would offer a better and more feasible means of acquiring additional capital. Expansion of capital by this means is also advantageous for the reason that capital represented by such securities can be contracted by redemption or payment at any time that the additional capital represented by such securities is not needed in the business. The use of such securities, therefore, provides a flexible means of adjusting the capital requirements of banks to the needs of the times.

Senator Bush. May I go back for just a moment to the second paragraph?

Do I understand then, is it your feeling that there should not be any inhibitions on the part of the banks desiring more capital to use, let us say, preferred stock as a medium of financing?

Mr. Fleming. That is correct.

Senator BUSH. In other words, you do not approve of the present psychology, if it is that, that it is only to be used in the event of an emergency, perhaps to bolster up a tottering bank, but should be considered as a perfectly legitimate and respectable way to get new money?

Mr. FLEMING. That is correct, Senator Bush. As you will recall, there was a lot of preferred stock sold to the Reconstruction Finance Corporation back in the thirties under the Emergency Act. I think the public pretty generally feels that would be a sign of weakness today the way the law is now worded.

Senator BUSH. How are you going to change that point of view?

Mr. FLEMING. It's a matter of psychology, which is awfully hard to analyze and determine. But we feel if this new bill would say that banks are permitted to sell preferred stock or debentures as well as common stock, it would not be long before some of the larger banks of the country would be availing themselves of that privilege, and it would be a matter of education with the public. But if some of the larger banks take the lead on it, others could easily follow along.

Senator BUSH. Debentures in that event would be subordinated?

Mr. FLEMING. Yes, indeed. Otherwise they could not be considered as capital.

Senator BUSH. This is a new idea as far as I am concerned. I have not heard this seriously proposed by responsible bankers before.

Has it been a matter that has been under discussion among the Reserve city bankers?

Mr. FLEMING. Yes, it has, Senator Bush, because all the banks have grown so rapidly in deposit totals and in loan totals that naturally they want to keep their capital ratios in line, and the only means they have to do that now is to go out and sell common stock. Very often that dilutes the equity of the existing stockholders.

Senator BUSH. It always does.

Mr. FLEMING. Yes.

Senator BUSH. Is it true the banks have been having difficulty in recent years in selling common stock?

Mr. FLEMING. Yes, sir; in small communities. In some of the larger cities I would say no, but the small bank often has a very difficult time in selling stock and also has a difficult time in selling it at a fair price.

Senator BUSH. Do you think encouragement of the sale of other securities, such as debentures or preferred stock, would be of real assistance to the smaller banks who have had this difficulty?

Mr. FLEMING. I think it could conceivably be of major assistance, particularly to the smaller banks, in increasing their capital funds. It would be much easier for a small bank, as I see it, to sell a subordinated debenture carrying a fixed rate of interest than additional common stock in the small community in which it is operating.

Senator BUSH. Thank you.

Mr. FLEMING. Should I proceed, Mr. Chairman?

Senator ROBERTSON. You may.

Mr. FLEMING. I also call to your attention section 36 (e) of this bill, which would authorize national banks to make working capital loans to established industrial and commercial enterprises where the bank will primarily look to the earnings of the business for repayment, rather than to real estate which may be taken as a protection security.

Since with respect to such loans the lender looks primarily to the overall net worth and earnings of the borrower, such loans represent ordinary business financing and should be treated as commercial loans and not as real-estate loans subject to the restrictions and limitations of section 24 of the Federal Reserve Act. Under present law national banks also find themselves at a competitive disadvantage with respect to those State banks located in States, the laws of which are much less stringent in this respect. There appears to be no logical reason why national banks should be prevented from obtaining real estate as collateral security without having to comply with the technical restrictions of section 24.

Section 36 (a) of title I of the tentative bill would amend existing law (sec. 24, Federal Reserve Act), with respect to the aggregate limitation on real-estate loans by a national bank, by adding to the existing alternative limitations on such loans of 100 percent of capital and surplus or 60 percent of time and savings, whichever is greater, an additional alternative of 20 percent of demand deposits. We believe that the limitations under existing law are unnecessarily restrictive with respect to national banks which have a relatively low proportion of time and savings deposits. This problem is met particularly in communities where the competition for savings is such that national banks cannot acquire savings at reasonable interest rates in a sufficient amount to permit them to meet the normal demand of their customers for real-estate financing.

We accordingly endorse this amendment to existing law, but suggest for the purpose of this amendment that the term "demand deposits" not include public or interbank demand deposits.

Section 36 (c) of title I would amend existing law to enable national banks to make loans with maturities not exceeding 18 months to finance the construction of industrial or commercial buildings if there is a valid and binding agreement by a financially responsible lender to advance the full amount of the bank's loan on completion of the construction, without such loans being regarded as real estate loans. Authority for construction loans on industrial and commercial properties is essential, if the need for such loans is to be met and if national banks are to be able to compete with State banks in such financing. The limitation of 100 percent of capital and surplus on the aggregate of construction loans for residential, farm, industrial, and commercial construction seems to be reasonable and sufficient.

Section 26 of title I of the tentative bill amends existing law to make cumulative voting by shareholders in the election of directors of a national bank permissive, rather than mandatory. Similar legislation in the form of S. 256 was passed by the Senate during the 84th Congress and favorably reported by the House Banking and Currency Committee, but not finally enacted.

Mandatory cumulative voting may be sound in theory but has not in practice worked well in many instances, with the result that necessary cohesion and unity in direction and management is disrupted and confidence impaired. Also there always exists the danger of competitors or undesirable elements forcing representation on a bank's board of directors in order to obtain confidential information relating to operations or loan practices. In our opinion, the amendment as proposed is sound and most desirable.

There is a further provision of the bill which we consider to have a great importance for the future of the banking business, and that is the authority under section 31 (a) (9) of title I of the bill, which would authorize national banks to establish stock option plans for their employees. It should be noted that this provision expressly requires approval of the terms and conditions of any such plan by a two-thirds vote of the shareholders and by the Comptroller of the Currency. Under present law, national banks are not permitted to establish stock option programs for their employees.

The banking industry has for some time faced an acute problem of management development. The efforts of the banking industry to solve this problem have met serious obstacles, resulting in part from its inability to offer incentives such as the great bulk of American industry has been and is increasingly offering to present and potential management. Consequently, under existing circumstances, the banking industry is unable to compete with business and industry generally in management development.

Management development programs are no less essential to the banking industry than to other commerce and industry in the country, and if banking is to grow and prosper along with the rest of commerce and industry it must in this respect be placed in a reasonably competitive position with such other commerce and industry.

There are several provisions of this bill bearing on the same subject which I should like to raise before this committee. These provisions are section 8 of title I (identical with sec. 38 (i) of title II, sec. 40 (d) of title III, and sec. 19 (b) of title IV), and section 803 of title VIII. Section 8 (b) of title I, and the corresponding provisions of titles II, III, and IV, makes it a criminal offense for any employee or any former employee of the Office of the Comptroller of the Currency to accept employment in any national or district bank except pursuant to regulations prescribed by the Comptroller. The problem we see in this provision is its application to former employees of the Office of the Comptroller of the Currency. As the provision now stands, it would apply to all former employees of the Comptroller's Office without regard to the length of time which has elapsed from the time a particular employee terminated his service with the Comptroller's Office. Such a proposed application to former employees, in our opinion, requires careful consideration as to its administration and enforcement.

Mr. ROGERS. May I interrupt there?

Mr. FLEMING. Yes, sir.

Mr. ROGERS. Under that provision the bill provides that the supervisory agency by regulation shall prohibit. There was a thought in there that the supervising agency would set the time limitation.

Mr. FLEMING. But it is not mandatory. It is left entirely to his own decision.

Mr. ROGERS. That is correct. Would you recommend a definite time limitation be placed in there?

Mr. FLEMING. I believe the Comptroller has suggested a period of 2 years, which would certainly seem reasonable to us.

Mr. ROGERS. Thank you.

Senator ROBERTSON. You may proceed.

Mr. FLEMING. Section 803 of title VIII of the bill amends sections 217 and 218 of title 18 of United States Code. So far as this provision relates to the employment of officials or employees of the bank supervisory agencies by banks supervised by such agencies, we question the need for it. Our present thinking is that section 8 of title I, and the corresponding provisions of titles II, III, and IV applicable respectively to the Board of Governors, the Federal Deposit Insurance Corporation, and the Home Loan Bank Board, appropriately amended with respect to its application to former employees, would provide adequate authority to prevent or deal with any conflict of interest arising out of such employment of bank supervisory personnel. In addition, it appears to us that the meaning and application of these amendments made by section 803 to present sections 217 and 218 of title 18 United States Code are not clear and this seeming defect is serious in a penal statute. Finally, we are concerned as to the effect of these amendments to present sections 217 and 218 on the capacity of the supervisory authorities to acquire and maintain adequate and qualified examining staffs in the light of this provision. In our opinion, such a provision deserves and requires the careful consideration which we are sure it will receive from this committee.

At present there is a conflict in ruling between the Board of Governors for member banks, and the Federal Deposit Insurance Corporation for nonmember insured banks on whether absorption of exchange is the indirect payment of interest on demand deposits and hence prohibited by law. The ability of one class of banks to absorb exchange for customers, at considerable cost to themselves, has resulted in some instances in the building up of deposits through the unnatural and unhealthy circuitous routing of checks for collection. This system circumvents the most expedient method of collecting checks and places banks which are members of the Federal Reserve System at a competitive disadvantage with nonmember banks. It is not believed Congress ever intended such a situation to develop and should take appropriate action to correct this inequity. A practicable means of doing so was suggested by Mr. Kenton Cravens in his testimony on January 28 in behalf of the Advisory Committee.

This association included among the recommendations it made to this committee, in connection with the study that preceded this bill, a proposed amendment to existing law to authorize national banks and State member banks to engage in the underwriting of revenue bonds. Under present law such banks are prohibited from doing so. State and municipal authorities have in recent years been placing increasing reliance on such bonds to meet their financing needs. Banks have been substantial purchasers of these bonds for their own investment portfolios. It seems illogical to permit banks on the one hand to acquire such bonds for investment purposes and on the other hand to prohibit them from underwriting and dealing in the same bonds. Elimination of the present restriction would create a broader market and, therefore, increase competition with probable lower financing costs to the issuing bodies.

Mr. Chairman, we think the time has come to reexamine the requirements of present law with respect to assessments paid by banks to the Federal Deposit Insurance Corporation. The deposit insurance fund now exceeds $1,700 million, equal to 1.46 percent of insured deposits. Increase in the fund from assessment income after expenses and losses for 1955 was approximately $66 million. In addition, the deposit insurance fund has been increasing substantially each year from accrual income on investments, which amounted to over $40 million for the year 1956. Meanwhile, losses suffered by the Corporation have been minimal, amounting to only $19 million over the 22-year existence of the Corporation, or an average of less than $1 million per year.

In the light of these considerations, we are of the opinion that Congress should seriously consider the question whether it is necessary to continue assessing the banking system in order that the fund continue the present rate of growth. In our judgment the present deposit insurance fund, increased annually by income from investments, is adequate to meet losses arising from causes other than those incident to major national disaster, and we do not conceive that the Corporation was intended to, or indeed ever could, insure losses arising from such causes. It may be that our conception of the insurance liability of the Corporation is erroneous, but if it is, then we believe it is the Congress who should declare for the guidance of the Corporation and the insured banks, what the proper scope of the Corporation's liability should be.

As the law now stands, it is left, we think wrongly, to the Corporation itself to determine this most basic principle of the Corporation's creation and operation. We infer from the testimony of officials of the Federal Deposit Insurance Corporation (hearings, p. 298) that the existing policy of the Corporation appears to be based on the adequacy of the insurance reserve to total deposits rather than insured deposits. In this connection, Mr. Royal Coburn, counsel to the Federal Deposit Insurance Corporation, testified during the above-cited hearings:

> There has never been anyone in Congress or anybody else that I can see—and I come as a newcomer in this field—I do not see that there has been any attempt to get a proper relationship. Whether it should be 75 percent, or 1 percent, or 2 percent, or 5 percent—nobody seems to have given that any serious consideration. Frankly, my own point of view just personally is—it should be 1 percent and the present formula should be continued to operate until it does get to 1 percent, and then if it reaches that point, then I think Congress should take a look to see whether or not some adjustment should be made to maintain it at about that ratio.

Mr. Coburn's comments, as you will note, are based on a relationship of the Corporation's reserve to total deposits, and this, we contend, is an assumption in nowise supported by the statute or other congressional declaration. To the contrary, we believe that the concept of the statute as shown by the requirements of the law with respect to the types and maximum limits of deposits insured, is that the Corporation's reserve, or deposit insurance fund, should be related to insured deposits, and not to total deposit volume. It is significant that only 116 billion or less than 55 percent of the 212 billion bank deposit totals are insured by the Federal Deposit Insurance Corporation.

For the foregoing reasons, we recommend that Congress consider amending the present law to refund pro rata to insured banks the entire assessment income of the Corporation after making allowance for all expenses and known losses, so long as the accumulated reserve is not less than 1 percent of insured deposits. We do not think that the amount which would be refunded to insured banks pursuant to our recommendation would in anywise impair the capacity of the Corporation to discharge its responsibility under law, as we conceive it. On the other hand, such a refund would be of substantial benefit to the banking system by reducing the present strain on bank resources resulting from Federal Deposit Insurance Corporation assessments and in increasing the capacity of the banking system to meet its responsibilities to its depositors.

Finally, I should like to discuss briefly the question of an adequate and realistic bad debt reserve against loan losses by commercial banks. While this matter is not within the jurisdiction of this committee, the importance of the matter to the commercial banking industry is such as to bring it within the sphere of this committee's interest.

Under present regulations of the Treasury issued pursuant to section 166 (c) of the Internal Revenue Code of 1954, the bad debt reserve a bank is permitted to establish is based on that bank's past loan experience. This historical basis for computation of the allowable bad-debt reserve is inadequate on the basis of past experience, is widely variable and tends to penalize prudent management. This inadequacy is even more pronounced when considered in the light of the huge and constantly increasing demands that are being made on the banking system in an economy as dynamic as is ours. Moreover, the reliability of past experience as a guide to adequate present loan-loss reserves may be further questioned in the light of the well-known fact that the commercial banking system now extends in substantial amounts many types of credit not heretofore handled. These newer types of credit often carry risks againsts which historical experience can provide no guide.

Bad-debt reserves currently accumulated and permitted to be accumulated are, in our opinion, totally inadequate in terms of possible needs. Commercial banks should be permitted to set up loan-loss reserves based on a realistic percentage of loans outstanding, such percentage to be uniformly applicable to all commercial banks and to be determined with particular regard to the current risk exposure of the commercial banking industry. It is our considered judgment that the present law should be amended to permit commercial banks to establish bad-debt reserves against possible loan losses up to a maximum amount of 10 percent of outstanding loans, such reserves to be accumulated at an annual rate not exceeding 1 percent of such loans. By so doing, the banking system would be greatly strengthened, and there would be built into the system a stabilizing factor that would prove of incalculable value in a period of recession or depression. It would also tend to reduce the dependence of the banking system on the Federal Deposit Insurance Corporation.

In conclusion, gentlemen, the Financial Institutions Act of 1957, if enacted, would in our opinion constitute a marked improvement over existing law as a matter of technical substantive and organizational content. There are, of course, specific provisions in this bill with which we, and I am sure others, may differ in whole or in part on one or another ground. In general, however, it is an excellent bill and obviously the product of a prodigious amount of study, time, and work. We should hope that this committee, out of its long experience, would be able to resolve any differences that may be reflected before this committee during these hearings, so that the prospects of passage of the overall bill would not be imperiled. As I stated at the beginning of my appearance, this tentative bill reflects the recognition by the members of this committee of the need for just such a revision of the present laws affecting financial institutions as this bill embraces. In our opinion, this committee deserves and has the commendation of the financial community because the proposed revision now has been brought to the stage of public hearings.

I have greatly appreciated the privilege of appearing before you.

Senator ROBERTSON. Mr. Fleming, you have given us a fine statement and the committee, of course, appreciates the commendation given us in your last paragraph.

The chairman has noted that as you went through your prepared statement you endorsed many of the essential provisions of the tentative bill. You felt we should back off a little bit on the criminal provisions of sections 217 and 218, which the chairman is going to recommend we do. We cannot change anything until we write the formal bill.

You think we should reduce assessments, that is, the Federal Deposit Insurance Corporation assessments, but the Chair cannot take it on himself with no information on which to go, and there has not been a survey as to what it should be or what it is expected to cover. The chances are this committee will direct a survey as a basis for it. Then, of course, we note that you think commercial banks should be authorized to deal in revenue bonds.

Mr. FLEMING. Yes, sir.

Senator ROBERTSON. We thank you very much.

Are there any questions?

(No response.)

Senator ROBERTSON. If not, again we thank you.

The next witness—and we have to hurry because perhaps we have impinged upon the remaining program, although we hope we can finish them all—the next witness is a representative of the National Association of Supervisors of State Banks, Mr. Charles R. Howell, of New Jersey, who will be recognized and who will be assisted by a constituent from Virginia, Mr. Ritchie.

STATEMENT OF CHARLES R. HOWELL, CHAIRMAN OF THE LEGISLATIVE COMMITTEE; ACCOMPANIED BY LOGAN R. RITCHIE, PRESIDENT, NATIONAL ASSOCIATION OF SUPERVISORS OF STATE BANKS

Mr. HOWELL. Mr. Chairman and Senators, my name is Charles R. Howell. I am commissioner of banking and insurance for the State of New Jersey. I am speaking today in my capacity of chairman of the legislative committee of the National Association of Supervisors of State Banks.

I have a fairly brief oral statement and also an accompanying statement delineating the amendments to accomplish what we propose.

Senator ROBERTSON. Before you go further, I think it would be very well for this record to show that there are more State banks than there are national banks that constitute what we call the dual banking system.

Would you indicate approximately how many State banks and how many national banks there are?

Mr. HOWELL. I do not have those figures handy, but I think your statement is correct, Senator. I know in our own State there are a few more national banks, but the assets of the State banks are higher by a small proportion than the assets of the national banks.

Senator ROBERTSON. The statistics are changing all the time and it is difficult for the chairman to carry them in his memory.

Mr. HOWELL. Yes, sir.

Senator ROBERTSON. But as I recall it, there are something over 8,000 State banks and something over 5,000 national banks.

Mr. HOWELL. I think that is roughly about what it is, Senator.

Senator ROBERTSON. You may proceed.

Mr. HOWELL. As has been explained, I have with me the president of our association, Mr. Logan Ritchie, the commissioner of banking for the State of Virginia.

There are several provisions of the committee print introduced by Senator Robertson which our association feels should be altered in the interest of preservation of the dual banking system and the proper rights of the States in the banking and allied fields with which this proposed act deals. There may be a number of provisions in the bill on which individual members of our association would like to be heard, but I am going to testify only on those positions on which our association through its general meetings, its executive committee meetings, or its legislative committee has taken a stand.

In title I, chapter 7, paragraph 51, we feel that language should be added which would preserve the police power of the States in licensing in a very limited way institutions engaged in various forms of consumer finance. Proposed language to accomplish this as well as other changes recommended is contained in the supplemental sheet which I have supplied to the committee.

I might say many States in their consumer finance acts do require all banks, including national banks, to be licensed. I know there is some controversy over whether it is proper for the States to license in any way a national bank, but it has worked very well in the past and it is considered necessary in the general police powers of the States to police their statutes concerning consumer finance. Particularly they have the power to investigate and examine, in a very limited way, even national banks to see that their State statutes on those things are being observed.

So we think some additional language making that exception should be added to that provision.

Mr. ROGERS. May I interrupt, Mr. Howell?

Mr. HOWELL. Yes.

Mr. ROGERS. I believe that was the purpose of the Comptroller's recommendation. It was that very situation.

Mr. HOWELL. I think it undoubtedly was, but we feel there is still a need for our having that power under certain circumstances.

Mr. ROGERS. Thank you.

Mr. HOWELL. Under title II, chapter 9, paragraph 54, we suggest changes in the bank holding company provisions to give the Comptroller of the Currency or the appropriate State authority, as the case may be, a veto on bank holding company applications and also to provide that their approval shall only be overridden by the Board after a public hearing.

Senator ROBERTSON. You suggested that before, last year, and it was in the House bill.

Mr. HOWELL. Yes, sir.

Senator ROBERTSON. That was the most controversial thing that we had to go up against. The sum and substance of it was that each State would make the final decision on the bank holding company. The Congress was supposed to pass the act and the Federal Reserve Board was supposed to administer it.

Mr. HOWELL. Yes.

Senator ROBERTSON. And yet you insist on the dual banking system, but the partnership under that arrangement would have been all State and no Federal power.

Mr. HOWELL. The creation and operation of bank holding companies has such a tremendous impact on the pattern of banking within a State that I would say in the final analysis a State should be able either to prohibit or to regulate bank holding companies within its State.

Senator ROBERTSON. As we pointed out in the discussion on the Senate floor, there will not be many new bank holding companies formed for several reasons. First, it takes a great deal of capital, and that is not available. Second, it takes a number of small banks that are willing to sell, and that is not likely to appear.

Mr. HOWELL. I think you are right, Senator.

Senator ROBERTSON. Third, we have a much stronger law than we ever had before for them to get approval to get started again.

Mr. HOWELL. I think that is true.

Senator ROBERTSON. I am glad to say we do not have any in Virginia and I do not anticipate—and I would be glad to have Mr. Ritchie bear me out—that we are likely to have any under the new law.

Mr. HOWELL. I do not believe we have any in New Jersey, but at present we do not have a law prohibiting them, although we have introduced a bill.

Senator ROBERTSON. I understand they have a law in New York to stop the formation of one bank holding company up there. I do not know whether it stopped it, but it was intended to stop it.

You may proceed.

Mr. HOWELL. In other words, we suggest changes in the bank holding company provisions to give the Comptroller of the Currency or the appropriate State authority, as the case may be, a veto on bank holding company applications and also to provide that their approval shall only be overridden by the Board after a public hearing.

We suggest amending paragraph 58 to make more explicit the powers reserved to the States to deal with bank holding companies.

The language as it is may be all right, but this will make it more certain.

The creation and operations of bank holding companies can so drastically affect and disturb the pattern of banking in the various States that it should be a matter for State control regardless of whether holding companies are composed of State or national banks, or both.

Senator BUSH. May I interrupt to ask one question?

Mr. HOWELL. Yes.

Senator BUSH. In that last paragraph you read you said it should be a matter for State control.

Mr. HOWELL. Yes, sir.

Senator BUSH. As it is now, does not the State banking department have supervision, and can it not prevent and cannot State law prevent a holding company within its own State now?

Mr. HOWELL. We believe the States, where they have acts controlling them or prohibiting them, that that would be valid, but we want to make absolutely certain.

Senator BRICKER. It has never been decided, has it?

Mr. HOWELL. Not completely, in my opinion.

Senator BUSH. I wonder what you think should be done, because my impression is the States now have the authority you want them to have.

Mr. HOWELL. I am pretty sure they have, Senator, but there are some questions that are being tested here and there, and I think if we can tighten it up to the point where there would be no doubt about it, that would be desirable.

Senator ROBERTSON. We deliberately put in a reservation so the States, if they did not want a bank holding company, can pass a State law, and that ends it. Any State can pass that law under our bill.

Mr. HOWELL. I think that is what the law actually provides, but if there is any doubt about it I would like to tighten it up a little bit.

Senator ROBERTSON. You may proceed.

Mr. HOWELL. Title III—Federal Deposit Insurance Act: It has been the observation of the legislative committee that the operation of the Federal Deposit Insurance Corporation under a Board of Directors has been marked by ever-increasing efficiency and usefulness. The committee deprecates, therefore, the proposal to abolish the Board and set up in its place a single administrator.

Senator BRICKER. Do you think the Comptroller ought to be a third member of that Board?

Mr. HOWELL. No. I was coming to that.

The Board, in the opinion of the committee, should be retained in its present form and with its present powers, except that the Comptroller of the Currency should no longer be a Director. The fact that he supervises the national banking system, which is often in competition with the State banking system, makes it inappropriate for him to sit on a board which has supervisory powers over State-insured banks. He should be replaced on the Board of the Federal Deposit Insurance Corporation by a banker who will not be involved in this conflict of interests.

We therefore support continuance of the Board in contrast to a single administrator if the change is made eliminating the Comptroller as one of the members.

Senator FREAR. Is this proposed to correct anything that you think happened on the part of the Comptroller of the Currency in the past?

Mr. HOWELL. I do not think it is based on any single or specific occasion, or that it is directed against our very fine present Comptroller. It just does seem inconsistent for them to have that necessary representation on there when the States do not have it.

Mr. ROGERS. Mr. Howell, what is the general practice in the States, as to the State bank supervisors? Is it generally a single administrator, or a board?

Mr. HOWELL. I was afraid you were going to ask me that. It is almost always a single administrator, but with many States having advisory boards with different degrees of power, and some having virtually no power, and some having considerable power.

I think one distinction there would be you might say that the State supervisor was dealing just with his own children, and therefore the danger of being prejudiced in favor of one or the other actually does not exist. In most cases it works out pretty well. But actually in experience we think that the three-member Board of the Federal Deposit Insurance Corporation has been good, especially if the Comptroller is not a member of it.

Mr. ROGERS. Thank you.

Mr. HOWELL. Under paragraph 23, which deals with mergers and consolidations, we suggest some changes.

I might say our association has gone all over the lot on this and tried to come up with a proper answer. It is not easy. Last year when I testified before the O'Mahoney subcommittee of the Judiciary Committee our position was that the Fulbright bill of last year was not at all satisfactory, because it seemed to exclude completely even any duty to consult State supervisors in determining this; but in general this is our present feeling, which we have considered at some length and believe it might be a proper solution.

The national association considers the present situation where the State supervisor alone has power to approve or disapprove a merger or consolidation resulting in a State bank to be satisfactory. It recognizes, however, the strength of the demand within the Congress and without, for some Federal regulation of mergers and consolidations. In view of this demand, it recommends that the Federal body in which such authority should be vested on a parity with that of the States themselves be the Federal Reserve Board for all State-chartered insured banks, whether member or nonmember. The equal authority of the State supervisors should be recognized explicitly in the language of this section.

Since, if action on mergers or consolidations of State banks is to be taken by the Board as well as by the appropriate State supervisor, it is only fair that the Board also act on mergers or consolidations resulting in national banks. It would place State banks at a disadvantage if their mergers had to be approved by both the State authority and the Board while mergers of national banks could be effected with the sole approval of the Comptroller. Unless the consent of the Board is required for national-bank mergers as well as State-bank mergers, there will be a strong inducement for State banks to convert to national charters to the detriment of the dual banking system.

Senator BUSH. Cannot the State require by law just what you want done here?

Mr. HOWELL. No. I think it is pretty clear we would have the power to deny a merger where the resulting bank would go under the State charter, but if we approve it then under your proposal it would go to either one of them; that is, either the Comptroller or the Federal Reserve or the Federal Deposit Insurance Corporation, and they could negate our action, which may, in the final analysis, be right.

Senator ROBERTSON. You are recommending a matter which we gave serious consideration to last year. I think it was generally agreed that most people would like to have the Federal Reserve Board pass on all of these mergers, but by doing that we turn that possibly into an appellate court. They said they did not have the time to take on all of these and suggested we divide it up. They said, "Give us part of it and give the Comptroller a part and give the Federal Deposit Insurance Corporation a part. We do not have the personnel and the time just to become an appellate court, so to speak, on the question of bank mergers."

Otherwise, I think you have made a mighty good suggestion. Personally, I would like to see it amended, but they just told us they could not do it.

Mr. HOWELL. I do not know what the figures would be, but they would be apt to get most of the important ones anyway, because they would get all of the national banks, and all of the member State banks, which would include most of the important banks—not all, but most of them. The Federal Reserve Board is a fairly large board and composed of quite a representative body of citizens. They probably have more in the way of economists and staff in research personnel than the Federal Deposit Insurance Corporation does. It seems to me that they probably would be the logical ones to have the final say on it.

Mr. ROGERS. Under your proposal you would leave out the Federal Deposit Insurance Corporation entirely?

Mr. HOWELL. That is right.

Mr. ROGERS. So we would have no uniform Federal program as to all insured banks. We would have it as to national banks and member banks, but not as to insured banks?

Mr. HOWELL. No. The insured nonmember banks would be the responsibility of the State authority first and then the Federal Reserve Board.

Mr. ROGERS. Also I see you include here language raising a constitutional problem.

Mr. HOWELL. What part is that?

Mr. ROGERS. As to whether the Federal Government can direct any State authority to consider anything in passing on mergers.

Mr. HOWELL. Well, that might be a point. I agree. I am not a constitutional lawyer.

Senator ROBERTSON. You may proceed.

Mr. HOWELL. Title V—Federal Savings and Loan Act.

While the association greatly prefers the provisions of the original version of S. 972 of the 84th Congress, it would accept paragraph 6 (c) as written in preference to no legislation at all.

Senator BUSH. Just what does that mean? I am sorry, but I do not have that in front of me.

Mr. HOWELL. Simply it means when S. 972 was passed by the Senate it added that, let us say, the Federal savings and loan associations should have the same branch powers as not only any State-chartered savings and loan and mutual savings banks, but also the most liberal of any, including commercial banks and trust companies.

Senator BUSH. All thrift-gathering institutions would be on the same basis within a State?

Mr. HOWELL. Yes. That was the argument.

Senator BUSH. You favored that?

Mr. HOWELL. Yes. As a matter of fact, in New Jersey it would not create any problem, but there are other States where commercial banks have quite more liberal branch provisions than savings and loan and mutual savings banks.

Senator Bush. I just wanted to identify the problem. I understand it. Thank you.

Mr. Howell. We propose the deletion of all reference to State banks and trust companies, which would restrict branches of Federal savings and loan associations to the same pattern as State-chartered savings and loans and mutual savings banks. It does, however, consider the adoption in this session of Congress of specific regulations governing the branch powers of Federal savings and loan associations to be of utmost importance.

TITLE VIII—MISCELLANEOUS AMENDMENTS

Amendments to Criminal Code, section 217 (p. 247) and section 218 (p. 249):

The national association considers too severe the proposed restrictions on examiner and supervisory personnel, both Federal and State, in relation to employments by banks. It fears that the examiner and other supervisory positions would be made so unattractive that its members would find it only more difficult than at present to recruit new well qualified employees.

It suggests, therefore, that the penalties imposed on banking institutions for the employment or offering employment to examiners and other supervisory personnel be omitted from the bill. It also suggests that the State bank supervisors, as well as Federal supervisory authorities, be recognized as having authority to pass regulations dealing with the acceptance of employment in banking institutions by their examiners and other supervisory personnel.

I have one other brief statement, or proposal, or suggestion, that I would like to give strictly in my personal capacity rather than speaking for the national association.

There is one further matter which I would like to bring to the committee's attention. This suggestion is made personally and as commissioner of banking and insurance for the State of New Jersey. This suggestion has not been discussed with my colleagues in the National Association of Supervisors of State Banks.

I urge that the committee explore the desirability and feasibility of authorizing the Federal Reserve Board and the Federal Deposit Insurance Corporation to enter into reciprocal agreements with the State-bank supervisors with the view toward eliminating the need for duplication of examinations of State member banks and nonmember insured banks.

Presently these banks are examined yearly in our State both by the State examiners and the appropriate Federal examiners. In the interest of economy and avoidance of duplication, it might be possible to work out an alternating schedule under which the State supervisor would agree to accept the Federal Reserve or Federal Deposit Insurance Corporation examiner's report one year and have the State examiner's report accepted by the Federal agency the next year. It should not be mandatory, but only permissive, but would enable real savings to be made in cases where the efficiency and standards of State departmental examinations were considered adequate by the Federal Reserve, or Federal Deposit Insurance Corporation authorities. I believe it would be a forward step in preserving and strengthening the dual banking system and in promoting proper governmental economy.

Senator Bush. Mr. Howell, what you are proposing then is to reduce this examination process from 2 examinations a year to 1?

Mr. Howell. That is right. It would mean actually in practice in New Jersey we go in at the same time as the Federal Deposit Insurance

Corporation, or the Federal Reserve, and we do exactly the same things. It is a complete duplication of effort. We think we have a good examining staff and I am sure the Federal authorities believe they have, and we agree. However, I think as a practical solution if they examine one year and we the next and exchange reports, that the banks would be quite well controlled and supervised and a certain amount of economy would result.

Senator FREAR. It is practiced in some States now; is it not?

Mr. HOWELL. It is practiced only to the extent that they exchange reports, but they do not skip their examination and trust the State.

Senator FREAR. They send a few men in when the State is doing the examination.

Mr. HOWELL. I guess that sometimes happens. Yes.

Senator CLARK. Mr. Howell, in New Jersey do you have the problem of the need for bank mergers in order to give sufficient capital surplus to enable the merged bank to deal with their industrial clients who require loans larger than the small and unmerged banks are able to make?

Mr. HOWELL. Senator, I would say we at least purportedly have that problem, and I believe there is some validity to it. A number of our larger banks have complained to me about the inability to compete, particularly with the New York banks, and to some extent the Philadelphia banks, in handling large industrial loans.

Senator CLARK. Is that not really an inducement to mergers?

Mr. HOWELL. It has the effect and it promoted in this instance their desire to form a holding company, which I resisted and hope I can continue to resist. But I know it is a problem.

Senator CLARK. Is not one of the results of that perfectly natural move to diminish the number of banks in a given community, so that there is always the possibility of a tendency toward a monopoly in banks. Is that not so?

Mr. HOWELL. I think it is a real danger and a pattern which has to be watched closely and resisted where it gets to the point where it is.

Senator CLARK. Would you be in accord with the statement made by Mr. Fleming a little earlier that that problem should be handled entirely by experts in the banking field? As I understand him, he does not want the Attorney General to get into this picture in connection with his normal enforcement of the antitrust statutes.

Mr. HOWELL. As I suggested earlier, we have had an awfully hard time trying to discover what is the full and proper solution to this. Last year we thought that it would be more desirable, perhaps, to have the Justice Department, as proposed in the original Celler bill last year, to have the final power; although logically I think the banking supervisory agencies know more about the banking factors and actually, to a large extent, the competitive factors which are involved, than the Department of Justice, perhaps. I think even if we do it the way it is proposed here, that the general powers of the Sherman Act might still prevail if there is a merger that the Justice Department felt had to be dealt with.

Senator CLARK. The thing that would concern me is the possibility—and I make it only a possibility—that the overall philosophy of some of the regulatory agencies in the banking field would not be as zealous in connection with the enforcement of the antitrust statutes as the Attorney General's Department might be.

Mr. HOWELL. Many people fell that way. However, I earnestly believe that especially since the problem has become so acute and widespread and is developing so much, that the supervising authorities would pay pretty close attention to the reduction of competition and the monopolistic aspects of it.

Senator CLARK. Mr. Chairman, we are getting fewer and fewer banks in Philadelphia all the time. That may be a good idea. I am not sure. But I think it is something the committee ought to consider.

Senator ROBERTSON. I am sure we will look into it.

Thank you very much, gentlemen. Without objection, the amendments which you recommend will be made a part of the record at this point.

(The amendments referred to follow:)

AMENDMENTS RECOMMENDED BY CHARLES R. HOWELL, NATIONAL ASSOCIATION OF SUPERVISORS OF STATE BANKS, TO PROPOSED FINANCIAL INSTITUTIONS ACT OF 1957, JANUARY 31, 1957

(Underlined material is new. Matter in brackets would be omitted if suggested amendments are adopted)

TITLE I, NATIONAL BANK ACT

CHAPTER 7. NATIONAL BANK EXAMINATIONS AND REPORTS

§ 51. (Page 41) STATE EXAMINATION OR LICENSE PROHIBITED.

"No national banking association shall be subjected to examination by, or be required to pay any license or assessment fee, or penalty to, any State, political subdivision of any State, or any officer, agency or instrumentality of any State or political subdivision thereof under the requirements of any State or local law, in connection with or as an incident to such association's authority to carry on any share of the business which by law it has the right and power to conduct. No person, copartnership, association, or corporation shall be prohibited from borrowing from or discounting or negotiating promissory notes, drafts, bills of exchange, conditional sales contracts, installment consumer paper, or any other evidences of debt or otherwise dealing with a national banking association because of the fact that such association has not been licensed pursuant to any State or local law [.], *excepting, however, any business for the conduct of which a State or National bank may be required by State law to obtain a license and to be subject to the investigation and examination of its records, documents, and papers pertaining to such business by a State officer, agency, or instrumentality in the necessary and proper exercise of the police power of the State requiring such license, investigation, and examination.*"

TITLE II, FEDERAL RESERVE ACT

CHAPTER 9. REGULATION OF BANK HOLDING COMPANIES

§ 54. ACQUISITION OF BANK SHARES OR ASSETS

* * * * * * *

"(b) (Page 139) Upon receiving from a company any application for approval under this section, the Board shall give notice to the Comptroller of the Currency, if the applicant company or any bank the voting shares or assets of which are sought to be acquired is a national banking association or a district bank, or to the appropriate supervisory authority of the interested State, if the applicant company or any bank the voting shares or assets of which are sought to be acquired is a State bank, and shall allow thirty days within which the views and recommendations of the Comptroller of the Currency or the State supervisory authority, as the case may be, may be submitted. If the Comptroller of the Currency or the State supervisory authority so notified by the Board disapproves the application in writing within said thirty days, the Board shall *deny the application and shall* forthwith give written notice of that fact to the

applicant. *If the Comptroller of the Currency or the State supervisory authority approves the application in writing within said thirty days, the Board shall forthwith give written notice of that fact to the applicant unless it disapproves in which event* [within three days after giving such notice to the applicant] the Board shall notify in writing the applicant and the [dis]approving authority of the date for commencement of a hearing by it on such application. Any such hearing shall be commenced not less than 10 nor more than 30 days after the Board has given written notice to the applicant of the action of the [dis]approving authority. The length of any such hearing shall be determined by the Board, but it shall afford all interested parties a reasonable opportunity to testify at such hearing. At the conclusion thereof, the Board shall by order grant or deny the application on the basis of the record made at such hearing.

"(c) In determining whether or not to approve any acquisition or merger or consolidation under this section, *the Comptroller of the Currency or the appropriate State authority, as the case may be, and* the Board shall take into consideration the following factors: (1) the financial history and condition of the company or companies and the banks concerned; (2) their prospects; (3) the character of their management; (4) the convenience, needs, and welfare of the communities and the area concerned; and (5) whether or not the effect of such acquisition or merger or consolidation would be to expand the size or extent of the bank holding company system involved beyond limits consistent with adequate and sound banking, the public interest, and the preservation of competition in the field of banking."

§ 58. (Page 145) RESERVATION OF RIGHTS TO STATES.

"The enactment by the Congress of this chapter shall not be construed as preventing any State from exercising such powers and jurisdiction, *including the power to prohibit the formation or operation of bank holding companies,* which it now has or may hereafter have with respect to banks, bank holding companies, and subsidiaries thereof."

TITLE III, FEDERAL DEPOSIT INSURANCE ACT

CHAPTER 6. SUPERVISION OF INSURED BANKS

§ 23. (Page 162) MERGERS AND CONSOLIDATIONS.

"Without prior written consent by the Corporation, no insured bank shall (1) merge or consolidate with any noninsured bank or institution or (2) assume liability to pay any deposits made in, or similar liabilities of, any noninsured bank or institution or (3) transfer assets to any noninsured bank or institution in consideration of the assumption of liabilities for any portion of the deposits made in such insured bank. No insured bank shall convert into an insured State bank if its capital stock or its surplus will be less than the capital stock or surplus, respectively, of the converting bank at the time of the shareholders' meeting approving such conversion, without prior written consent by the Comptroller of the Currency *and by the Board of Governors of the Federal Reserve System* if the resulting bank is to be a district bank, or by the Board of Governors of the Federal Reserve System *and the appropriate State supervisory authority* if the resulting bank is to be a State member bank (except a district bank) *or a nonmember insured bank* [, or by the Corporation if the resulting bank is to be a State nonmember insured bank (except a district bank)]. No insured bank shall merge or consolidate with any other insured bank or, either directly or indirectly, acquire the assets of, or assume liability to pay any deposits made in and other insured bank without the prior written consent (i) of the Comptroller of the Currency *and of the Board of Governors of the Federal Reserve System* if the acquiring, assuming, or resulting bank is to be a national bank or a district bank, or (ii) *of the appropriate State Supervisor and* of the Board of Governors of the Federal Reserve System if the acquiring, assuming, or resulting bank is to be a State member bank (except a district bank), *or a State nonmember insured bank,* [or (iii) of the Corporation if the acquiring, assuming, or resulting bank is to be a nonmember insured bank (execpt a district bank).] In granting or withholding consent under this subsection, the Comptroller, the Board, or the [Corporation] *appropriate State supervisory authority,* as the case may be, shall consider the *following* factors: [enumerated in section 15 of this Act.] *(1) the financial history and condition of the company or companies and the banks concerned; (2) their prospects; (3) the character of their management; (4) the convenience, needs, and welfare of the communities and the area concerned; and (5) whether or not the effect of such merger, consolidation, acqui-*

sition of assets, or assumption of liabilities would be to expand the size or extent of the bank involved beyond limits consistent with adequate and sound banking, the public interest, and the preservation of competition in the field of banking. In the case of a merger, consolidation, acquisition of assets, or assumption of liabilities, the appropriate agency shall also take into consideration whether the effect thereof may be to lessen competition unduly or tend unduly to create a monopoly, and, in the interests of uniform standards, it shall not take action as to any such transaction without first seeking the views of each of the other two banking agencies referred to herein with respect to such question; and in such a case the appropriate agency may also request the opinion of the Attorney General with respect to such question. No insured State nonmember bank (except a district bank) shall, without the prior consent of the Corporation reduce the amount or retire any part of its common or preferred capital stock, or retire any part of its capital notes or debentures."

Chapter 3. Powers and Duties of Administrator (Pages 151–155)

Chapter 9. Miscellaneous

§ 42. (Page 181) Abolition of Board of Directors.

It has been the observation of this National Association that the operation of the Federal Deposit Insurance Corporation under a Board of Directors has been marked by ever increasing efficiency and usefulness. It deprecates, therefore, the proposal to abolish the Board and to set up in its place a single administrator. The Board, in the opinion of this Association, should be retained in its present form and with its present powers except that the Comptroller of the Currency should no longer be a director. The fact that he supervises the National banking system which is often in competition with the State banking system makes it inappropriate for him to sit on a board which has supervisory powers over State insured banks. He should be replaced on the Board of the Federal Deposit Insurance Corporation by a banker who will not be involved in this conflict of interests.

TITLE V, FEDERAL SAVINGS AND LOAN ASSOCIATION ACT

§ 6. (Page 211) Federal Savings and Loan Branches.

* * * * * * *

"(c) An association may, with the approval of the Board, establish and operate new branches within the State in which the home office of such association is situated, if such establishment and operation are [(i)] at the time expressly authorized to State savings and loan associations or mutual savings banks, [or (ii), after June 30, 1959, expressly authorized to State banks or trust companies by law of the State in question,] or, in the absence of any such law, if such establishment and operation are at the time in conformity with the practice within the State with respect to branches of State savings and loan associations or mutual savings banks [or, after June 30, 1959, in conformity with the practice within the State with respect to branches of State banks or trust companies] except that no approval of the State authority having supervision over State savings and loan associations or mutual savings banks [or banks and trust companies] shall be required, and such new branches shall be subject to the least onerous restrictions with respect to number and location as may be imposed by the law of the State or the practice therein with respect to branches of State savings and loan associations[,] *and* mutual savings banks. [, or State banks and trust companies.] No branch of any Federal savings and loan association shall be established outside the State in which its home office is located. The Board shall, before approving or disapproving an application of a Federal savings and loan association to establish and operate a branch, give consideration to the same requirements as are set forth in this subsection with respect to the granting of charters of Federal Savings and loan associations."

TITLE VIII, MISCELLANEOUS AMENDMENTS

Amendments to Criminal Code

Sec. 217. (Page 247.)
Sec. 218. (Page 249.)

The National Association considers too severe the proposed restrictions on examiner and supervisory personnel, both Federal and State, in relation to employment by banks. It fears that the examiner and other supervisory positions would be made so unattractive that its members would find it even more difficult than at present to recruit new, well qualified employees.

It suggests, therefore, that the penalties imposed on banking institutions for employing or offering employment to examiners and other supervisory personnel be omitted from the bill. It also suggests that the State Bank Supervisors, as well as Federal Supervisory Authorities, be recognized as having authority to pass regulations dealing with the acceptance of employment in banking institutions by their examiners and other supervisory personnel.

Senator ROBERTSON. The next agency we have is the United States Savings and Loan League, and Mr. Henry A. Bubb is the witness for them.

The Chair will observe that Mr. Bubb has a statement and some exhibits that go with it. Without objection, the exhibits will be accepted for the record and will be inserted at the end of Mr. Bubb's statement.

You may proceed, Mr. Bubb.

STATEMENT OF HENRY A. BUBB, CHAIRMAN, LEGISLATIVE COMMITTEE; ACCOMPANIED BY STEPHEN SLIPHER, VICE PRESIDENT; AND T. BERT KING, WASHINGTON COUNSEL, UNITED STATES SAVINGS AND LOAN LEAGUE

Mr. BUBB. Thank you, Senator Robertson and gentlemen. It almost seems like old-home-week for me to come back here because I have been here so often lately.

I have Mr. Slipher and Mr. King of our Washington office with us. It is a little embarrassing for me to read the first paragraph, but, in order to acquaint some of the other Senators who might not know of my activity in this recodification, I will say that my name is Henry A. Bubb and I appear here today as chairman of the legislative committee of the United States Savings and Loan League.

By way of further introduction, I am past president of the league, chairman of the Federal Home Loan Bank of Topeka, president of the Capitol Federal Savings & Loan Association of Topeka, director of the Merchants National Bank, and it was my privilege to serve as a member of the Cravens advisory comittee on recodification. However, I appear here today solely in my capacity as spokesman for the United States League.

In general, we believe that this bill goes a long way toward accomplishing the basic objective of codifying and clarifying the statutes dealing with savings and loan associations and we commend all of those who have participated in the work. To make my statement as brief as possible, I will omit references to the mere technical changes in the bill and I will also omit reference to those items in which the league concurs and supports. In this statement I will comment on our several specific suggestions which, in most cases, are implemented by language included in addendum A which I submit to you here this morning as a supplement to my statement. Several other entirely technical and minor suggestions as to phraseology have been noted by our attorneys and I have placed these in addendum B.

TITLE IV, FEDERAL HOME LOAN BANK ACT

The only change proposed in the Board's present limited authority to supervise, examine, and regulate uninsured bank member institutions is the proposal in section 4 (d), page 183, to prohibit the use of Federal Home Loan Bank emblems and insignia except in the office of the association or as authorized by the Board. We approve this provision, but would like to record our hope and expectation that in adopting regulations the Board will take the commonsense approach of permitting these institutions to continue to use the emblem on their letterhead, financial statement and other customary purely local advertising. So long as there is no danger of the representation being construed as meaning insurance of accounts, no one objects to reasonable use of the bank emblem.

Section 5, page 184, of the Federal Home Loan Bank Act and section 4, page 203, of the Federal Savings and Loan Association Act deal with interest and charges. The intent of the proposed revision was to clarify the right of Federal associations to make property improvement loans on a discount basis as other lenders do and as is permitted under the FHA title I program without conflicting with State usury laws. Our attorneys believe that the proposed language is not entirely workable and have drafted language (addendum A, items 1 and 3) which we think will accomplish the objective in a more satisfactory manner.

In section 13, page 196, there was apparently an oversight in that as drafted it would have the effect of repealing the Public Debt Act of 1941 affecting Federal home loan bank obligations and therefore we suggest the insertion of the words "income taxes" before the word "surtaxes" to correct this error. With this addition these obligations would continue to be subject to income tax.

We recommend that section 19 (b), page 200, be amended to provide some reasonable time limit, such as 2 years. As now written, persons who worked for the Board 20 years ago would still be required to get permission of the Board before accepting employment and we attach a suggested draft (addendum A, item 2).

TITLE V, FEDERAL SAVINGS AND LOAN ASSOCIATION ACT

As previously indicated, we have suggested language with respect to section 4 (addendum A, item 3).

With respect to section 5 (d) (2), our people suggest the addition of one sentence as follows:

> No supervisory representative in charge, conservator or receiver shall be appointed for a solvent and nonimpaired institution if the alleged wrongdoing can be corrected as provided in this section, or otherwise by law, without the seizure of private property.

The purpose of this amendment is so that there will be no seizure of private property until other methods have been used. This has the unanimous concurrence of the Cravens committee, as evidenced by the testimony before this committee Monday.

We are submitted a redraft for section 5 (d) (3), which we believe accomplishes the objective intended more effectively and with greater clarity (addendum A, item 4).

With respect to section 5 (i) and (j), page 209, we recommend the insertion of the word "mutual" before the words "savings and loan type" in the second line of the subsection and deletion of provision (4) on page 210, and the renumbering of provision 5 as No. 4, and the deletion of subsection (j). The purpose of this amendment is to make it clear that a Federal association can convert to a State mutual only and to make it clear that they cannot convert to any other type institution.

Section 6, page 211, with respect to Federal savings and loan branches, of course, constitutes a major substantive addition rather than a revision or recodification. We would prefer that the matter be handled in separate legislation as it has been in the past. We again point out, as we have in previous testimony, that Federal savings and loan associations have fewer branches per home office than any other major financial institutions in the country. There would be some major hardships and inequities under this provision, as for instance in the States of Minnesota and Florida where associations would be prohibited from having branches, although chain and group banking accomplishes the same as branch banking for the commercial banks.

If this committee feels that there should be legislation, we would recommend a section directing the Federal Home Loan Bank Board to establish by regulation the conditions under which branches may be established and operated. We have long agreed with our banking friends that it is appropriate that there be some published standards which will enable all concerned to know the ground rules for the establishment of branches. We do believe that it is necessary to leave the Board considerable leeway because of the complexities of determining what is the State pattern in a number of instances. If this did not work out to the satisfaction of the Congress, legislation could be passed at a later date.

Senator BUSH. Do I gather from that you are opposed to the bill we have had up here in the last two Congresses, which gives branching privileges to these organizations in connection with the State law for all thrift gathering institutions?

Mr. BUBB. Let me answer it this way, Senator Bush: We are for liberalizing it where it would also include chain banking and chain ownership.

Senator BUSH. You mean you think the Federal Government should pass a law which would override the State law?

Mr. BUBB. No. Not at all. You are not overriding the State law. As I pointed out, in the States of Florida and Minnesota particularly the banks have branches through chain and group banking, which we cannot have. I might say this: Of course, we would rather have a bill directing the Federal Home Loan Bank Board to set up regulations, but if that is not the wish of this committee the bill that was introduced with that one addition would be very satisfactory to us, and I think it would be perfectly fair to both sides concerned.

Mr. ROGERS. That would write into law the present practice.

Mr. BUBB. That's right.

Senator ROBERTSON. You may proceed.

TITLE VI, FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION ACT

Mr. BUBB. With respect to section 403 (e), page 217, we recommend the insertion of the words "income taxes" before the word "surtaxes" in the third line. This is to eliminate the repeal of the Public Debt Act of 1941 affecting these obligations.

With respect to section 404 (c), page 221, we recommend the insertion "by regulation" after the word "impose" in the fifth line from the bottom and the deletion of the last sentence. This is to make it clear that conditions are to be prescribed by regulation and will be applicable to all alike. The last sentence is to be stricken because we do not know what contracts have been made and what conditions have been made. We do not believe in blanket approval of an "unknown quantity."

With respect to section 404 (e) and (f), page 221, the league recommends some spelling out in the statute of the rules for mergers, purchases, et cetera, rather than leaving complete discretion in the hands of the Insurance Corporation. In addendum A, item 5, we have suggested language which would retain in the Insurance Corporation the complete authority over major mergers and mergers which involve extension of lending area, but would exempt minor transactions in the local area.

With respect to section 406 (b), page 223, our people are satisfied with the committee print language as it is. If any changes are made, we trust that you will continue the policy of this committee and the Congress of preserving parity of treatment as between the insured accounts of savers of savings and loan associations and banks.

TITLE VIII, CRIMINAL CODE AMENDMENTS

We agree with the testimony of Mr. Cravens to this committee on Monday concerning the various matters considered under title VIII of the bill.

I would just like to add one thing, if I may, Senator Robertson.

We also agree with previous comments before this committee that some action should be taken to prevent the joint operation and advertising of savings and loan associations and banks such as Senator Bennett has discussed, which just happened in Utah.

Senator ROBERTSON. We appreciate very much your statement and the suggestions concerning changes in the tentative bill, most of which are regarded more or less minor. The Chair frankly says, and would say, that last summer, when he started this study, he was very much afraid that the commercial banks would want too many restrictions on their competitors, the savings and loan companies, and that the savings and loan operation would not want enough. He was pleasantly surprised. We worked out a compromise that apparently for the most part is acceptable to all parties concerned, and to the Chair that was a very encouraging thing.

Are there any further questions?

We thank you then, Mr. Bubb.

Mr. BUBB. I would like to say again—I have said it as a member of the Cravens committee, and I want to say it now for the United States League—that we appreciate very much, Senator Robertson, your bringing about this recodification program and giving us an opportunity to work with the bankers. We appreciate all of the work that Mr. Rogers and the rest of the staff have done, and we think that a lot has been accomplished and are very appreciative of it.

Senator ROBERTSON. Thank you.

Without objection, at this point in the record your exhibits will be entered.

(The documents referred to follow:)

United States Savings and Loan League

ADDENDUM A. RECOMMENDED REVISIONS SPECIFICALLY REFERRED TO IN STATEMENT OF HENRY A. BUBB

I. For consideration in lieu of section 5 of Federal Home Loan Bank Act

SEC. 5. (a) No institution shall be admitted to or retained in membership or granted the privileges of nonmember borrowers if the interest and any other charges for the use of the money charged on loans made by it shall exceed the rate per annum authorized or permitted on loans of a similar character by the laws of the State where its home office is located, or if such law prescribes no limit on such interest rates, then not to exceed 8 per centum per annum: *Provided*, That upon installation loans repayable in not to exceed five years, such rate may be charged on a discount or gross charge basis for the period of the loan.

(b) In addition to interest and any amounts charged for the use of the money, such associations may require the borrower to pay to others or to the association for the account of them or for its own account, if it renders such services, reasonable compensation to cover the cost of taking and processing loan applications and making loans for its full protection, and such charges shall not be deemed to be interest.

(c) In the event a Federal savings and loan association charges more interest than is authorized by this section, the borrower shall be entitled to a cancellation of his obligation and cancellation and return of any security therefor upon a tender of his unpaid balance and shall be relieved of any interest after the date of such tender. In the event a Federal savings and loan association makes service charges in excess of the amount authorized by this section, or requires the same to be paid to others, it shall be subject for a period of two years to suit for the recovery of the excess so charged. In the event any other member institution or nonmember borrower makes interest or service charges in excess of the amount specified in this section, such institution if a member shall be removed from such membership, or if a nonmember, shall be ineligible for membership and ineligible as a nonmember borrower.

II. Page 200

"19 (b) It shall not be lawful for any member of a Federal home loan bank to employ an employee of the Board or a former employee of the Board who has left its service within two years except pursuant to regulations made by the Board or with the express written approval of the Board, and it shall be unlawful for any such employee or former employee to accept employment in violation of this subsection. Any violation of this subsection shall be punished by a fine of not more $10,000 or imprisonment of not more than five years, or both."

III. Federal Savings and Loan Association Act (page 203)

SEC. 4. (a) The interest and any other charges for the use of the money charged by a Federal savings and loan association on loans made by it shall not exceed the rate per annum authorized or permitted on loans of a similar character by the laws of the State where its home office is located or, if such law prescribes no limit on such interest rates, then not to exceed 8 per centum per annum: *Provided*, That upon installment loans repayable in not to exceed five years such rate may be charged on a discount or gross charge basis for the period of the loan.

(b) In addition to interest and any amounts charged for the use of the money, a Federal savings and loan association is authorized to require the borrower to pay service charges to others or to the association for the account of them or for its own account, if it renders such services, reasonable compensation to cover the cost of taking and processing loan applications and making loans for its full protection and such service charges shall not be deemed to be interest.

(c) In the event a Federal savings and loan association charges more interest than is authorized by this section, the borrower shall be entitled to a cancellation of his obligation and cancellation and return of any security therefor upon a tender of his unpaid balance and shall be relieved of any interest after the date of such tender. In the event a Federal savings and loan association makes service charges in excess of the amount authorized by this section, or requires the same to be paid to others, it shall be subject for a period of two years to suit for the recovery of the excess so charged.

IV. Page 207

With respect to section 5, subsection (d) (3), rewrite to read as follows:

"(3) Whenever any director or officer of a Federal savings and loan association has violated or is violating any law relating to such association or has engaged or is engaged in unsafe and unsound practices in conducting the business of such association, after having been warned in writing by the Board to discontinue such violations of law or such practices, the Board may cause notice to be served upon such director or officer in writing to appear at a hearing before such Board or any member thereof or any person designated by the Board and show cause why he should not be removed from office. A copy of such notice shall be sent to each director of the association affected by registered mail and shall specify the violation of law and the unsafe and unsound practices alleged. The hearing shall be held in accordance with the provisions of the Administrative Procedure Act and shall be subject to review as therein provided and the review by the court shall be upon the weight of the evidence. If the Board finds that the accused director or officer after being warned in writing by the Board to discontinue such violations of the law or such practices, has violated or is violating any law relating to such association or has engaged in or is engaging in unsafe or unsound practices in conducting the business of such association, the Board may order that such director or officer be removed from office. A copy of such order shall be served upon such director or officer. A copy of such order shall also be served upon the association of which he is a director or officer, whereupon in the event he does not appeal, such director or officer shall cease to be a director or officer of such an association. Such order and the findings of fact upon which it is based shall not be made public or disclosed to anyone except the director or officer involved and the directors of the association involved, otherwise than in connection with proceedings for a violation of this section. Any such director or officer removed from office by final order as herein provided who thereafter participates in any manner in the management of such association shall be fined not more than $5,000, or imprisoned for not more than five years, or both."

Comment.—This leaves out "in the opinion of the Board" and "in the discretion of the Board" to make the appeal effective so that the trial will be on the facts. It provides for the notice to be in writing. It provides for removal only for violations after the warning in writing. It makes the removal effective only after the final order, that is when he fails to appeal or appeals and loses. All of this is to clarify. It is believed that the original draft is intended as above.

V. Page 221

With respect to section 404 (e), rewrite to read as follows:

"(e) No insured institution shall merge or consolidate with another institution or purchase or sell assets in bulk except the purchase or sale of mortgages in the market at market prices except with the approval of the Corporation if such transaction would increase the assets of an insured institution by virtue of such merger, consolidation, or purchase of assets by more than 25 per centum, or would have the effect of extending the lending area of an insured institution."

ADDENDUM B. TECHNICAL REVISIONS SUGGESTED BY UNITED STATES SAVINGS AND LOAN LEAGUE

1. Section 2 (6) (page 182), change to read as follows:

"The term 'home mortgage' means a mortgage upon real estate, in fee simple, or on a leasehold under lease for a period to run or which is renewable for a period of at least ten years beyond the maturity of the mortgage upon which there is located a dwelling for not more than four families, and shall include in addition to first mortgages such classes of first liens as are commonly given to secure advances on real estate by institutions authorized by this Act to become members, under the law of the State in which the real estate is located, together with the credit instruments, if any, secured thereby."

2. Strike out section 10A (p. 192), *Advances to nonmembers.* This section has not been used.

3. With respect to section 16 (p. 197), *Reserves and dividends*, strike out the third sentence so that an increase in membership or an increase in mortgage holdings which increases the capital stock would not necessitate discontinuance of dividends.

Amend the last sentence to read:

"The reserves of each Federal Home Loan Bank shall be invested in such securities as may be prescribed by the Board."

This modification will supply needed flexibility and latitude in the investment of reserves, to the end that they may be used for the benefit of members and not at all times be locked up in Government obligations.

4. With respect to section 401 (b) (p. 214), *Federal Savings and Loan Insurance Corporation Act*, rewrite the last sentence to read as follows:

"In any State, district, Territory, or possession having a community property law whether the money in the account or accounts is community property or not a withdrawable account or accounts in the name of a married person and an account or accounts in the name of his or her spouse and an account or accounts in the name of the two of them in community shall each be insured in an amount not to exceed $10,000 for the aggregate funds in the name of the married person, $10,000 for the aggregate funds in the name of the spouse, and $10,000 for the aggregate funds in the name of the two of them in community."

Comment.—The sole purpose of this is to make it clear that in community property States the husband can have $10,000 of insurance coverage, the wife $10,000 of insurance coverage and the two of them $10,000 of insurance coverage as such person may have in common law States.

5. With respect to section 403 (j) (p. 219), strike out "a member or of" in the second line and the words "the member or" in the second line on page 220.

Comment.—The sole purpose of this is to make it clear that we are dealing with insured associations only. This is evidently to correct an error.

6. With respect to section 17 (p. 197), some objection has been made by our people to the fact that you can not tell from the fact of this Act that the Federal Home Loan Bank Board is a bipartisan board and how many members of the Board there are. It has been suggested that this be redrafted to state the character of the Board in the Act rather than by reference.

Senator ROBERTSON. We have here another representative of a savings and loan organization, Mr. Lawrence F. Speckman, of Louisville, Ky. I understand he does not wish to testify, but just wishes to offer a statement for the record.

STATEMENT OF LAWRENCE F. SPECKMAN, PRESIDENT, LINCOLN BUILDING & LOAN ASSOCIATION, LOUISVILLE, KY.

Mr. SPECKMAN. Mr. Chairman, my name is Lawrence F. Speckman and I am from Louisville, Ky., president of the Lincoln Building & Loan Association. That institution has over 20,000 stockholders and $22 million paid in. We are an uninsured institution.

I came here to Washington to attend a conference of the United States league with the hope that they would adopt this amendment which I want to make and offer to subsection (d) of section 4 in regard to the Federal Home Loan Bank Act. I do not wish to argue the point, but only want to offer this and submit the statement later on, if it is your pleasure.

Senator ROBERTSON. You may proceed.

Mr. SPECKMAN. That subsection (d) of section 4 of title IV of the Federal Home Loan Bank Act be eliminated and in its place the following be substituted:

No member of a Federal home-loan bank whose accounts are not insured by the Federal Savings and Loan Corporation shall advertise or represent in any manner to so state, imply or convey the impression that those accounts are insured by said corporation. Any such member institution found violating this section by the Federal Home Loan Bank Board shall be removed from membership in the Federal Home Loan Bank.

I wish to offer that and I will type it and send it in to the committee along with my statement, if that is satisfactory, Mr. Chairman.

Senator ROBERTSON. How much time do you want to submit your statement?

Mr. SPECKMAN. How much time would you give me?

Senator ROBERTSON. Would a week be enough?

Mr. SPECKMAN. A week would be plenty.

Senator ROBERTSON. Then you may have a week.

Mr. SPECKMAN. Thank you, sir?

Whom will I address it to? To you, Mr. Chairman?

Senator ROBERTSON. No. You will address it to the clerk, Senate Banking and Currency Committee, Washington, D. C.

(The statement referred to follows:)

STATEMENT OF LAWRENCE F. SPECKMAN, PRESIDENT AND GENERAL COUNSEL OF LINCOLN BUILDING & LOAN ASSOCIATION OF LOUISVILLE, KY.

My name is Lawrence F. Speckman. I am president and general counsel of the Lincoln Building & Loan Association of Louisville, Ky., chartered by and under the supervision of the Commonwealth of Kentucky, an uninsured member of the Federal Home Loan Bank of Cincinnati, Ohio, and also a member of the United States Savings and Loan League. I am also a past president of the Kentucky League of Local Building Associations, and currently a member of the legislative committee of said association.

The Lincoln Building & Loan Association has been a member of the United States Savings and Loan League since shortly after it obtained its charter to operate as a State building and loan association under the supervision of the State of Kentucky on March 11, 1914, and also a member of the Federal Home Loan Bank, Cincinnati, Ohio, since September 22, 1932.

The Lincoln Building & Loan Association was organized with an authorized capital of $100,000 and went through the depression of the 1930's with a record of not missing a dividend or suffering a loss to any stockholder since its organization. It now has more than 20,230 members with total assets of $22,344,640.40 as of December 26, 1956. It has reserves in excess of 7.7 percent of its paid-in capital liability. It holds at the present time 3,281 shares of stock valued at $328,100 in the Federal Home Loan Bank of Cincinnati, Ohio. Its current dues for membership in the United States Savings and Loan League is $909.53 per year.

I did not expect to appear before your committee unless the legislative committee of the United States Savings and Loan League failed to support our contention that subsection (d) of section 4 of title IV of the proposed Financial Institutions Act of 1957, named the Federal Home Loan Bank Act, should be modified or substituted. As the legislative committee through its chairman, Mr. Henry A. Bubb, who appeared before the committee on January 31, 1957, as the spokesman for the United States Savings and Loan League did not support our contention, it became necessary for me to appear before the committee, representing the Lincoln Building & Loan Association, to oppose the enactment of the proposed law by the Congress on several grounds; that it would be unfair to us and others similarly situated, discriminatory, and a delegation of discretionary authority.

I am filing herewith as exhibits, or an addendum to my statement, samples of advertising material which we are now and have been using for some time, which we would be prohibited from using if subsection (d) of section 4 as written on page 183 of the committee print would become the law of the Congress. The exhibits consist of a letterhead, a condensed statement of the financial condition of the Lincoln Building & Loan Association as of the close of business on December 26, 1956, and other materials, with an imprint of the insignia of membership in the Federal home loan bank and also membership in the United States Savings and Loan League. It has been our custom to advertise the fact on all of our letterheads, financial statements, and in local newspapers that we are members of the Federal Home Loan Bank System and the United States Savings and Loan League. These two membership emblems are printed on all of our advertising matter jointly.

If the act becomes law as written in the committee print it would be unlawful for us "to advertise or represent in any way, off the premises on which we are situated, our main office or any branch office or agency thereof, that we are a member of a Federal home loan bank or we are otherwise associated with the

Federal Home Loan Bank System or to use for advertising display or publicity purposes any insignia, emblem or indicia designed to identify us as a member of the Federal Home Loan Bank System, except as the Board may expressly authorize by regulation referring to this subsection."

It will be noted that if we should so offend the Federal Home Loan Bank Board, we would be subject to a penalty of $1,000 which the Board may recover for its use.

The chairman of the legislative committee of the United States Savings and Loan League in his statement on page 3 thereof, approving the proposed act, expressed a "hope and expectation that in adopting regulations the Board would take the commonsense approach of permitting these institutions to continue to use the emblem on their letterhead, financial statement, and other purely local advertising. So long as there is no danger of the representation being construed as meaning insurance of accounts, no one objects to reasonable use of the bank emblem."

It is understandable that the chairman of the legislative committee of the United States Savings and Loan League, who is chairman of the Federal Home Loan Bank of Topeka and president of the Capitol Federal Savings & Loan Association of Topeka, would oppose a change in the wording of the section which we have found very objectionable to us, for the simple reason that he is president of a Federal association and presumably on that account, being insured, would take a position which would prohibit the use of the Federal home loan bank emblem and insignia except to those who are not only members of the Federal home loan bank, but are insured by the Federal Savings and Loan Association Insurance Corporation. We do not blame him for his position but we do protest before this committee that such a prohibition against the use of the advertising emblem is unfair to those who are also members of the Federal home loan bank, although uninsured.

At the close of the hearing of the committee on January 31, 1957, I was granted by the chairman, Senator Robertson, the privilege of making a statement and offered the following: That subsection (d) of section 4 of title IV of the Federal Home Loan Bank Act as it appears in the committee print on page 183 be eliminated and in its place the following be substituted:

"No member of a Federal home loan bank whose accounts are not insured by the Federal Savings and Loan Corporation shall advertise or represent in any manner to so state, imply or convey the impression that its accounts are insured by said corporation.

"Any such member institution found violating this section by the Federal Home Loan Bank Board shall be removed by the Board from membership in the Federal home loan bank."

We want the committee to understand that we do not defend any uninsured institution, member of the Federal home loan bank, who attempts by any form of advertising to represent that it is insured. Such form of advertising or representation should be dealt with severely, and we share with the legislative committee of the United States Savings and Loan League a condemnation of such practices. The only difference between us that I can see is that we think that the offense should be clearly identified and the offenders dealt with accordingly, in a manner befitting the offense. The league approves the prohibition of the use of the emblem and insignia as an advertising medium, except in the office of the association or as authorized by the Board, but leaving it up to the Board to adopt regulations that would take a commonsense approach, and exempting certain institutions who continue to use the emblem on their letterheads, financial statements, and other customary purely local advertising from the prohibition provided in the act. Such a provision would place the institutions wholly at the mercy of the Board without any directives as to its powers except to recover the $1,000 for its use, without the power to exclude such a member from membership in the Federal Home Loan Bank System. In other words, it would have the effect of enforcing the prohibition by regulation of the Board instead of by the law of the United States. We quote with approval the advice of Mr. Ben Dubois in his statement made before this committee on January 30, 1957, as secretary of the Independent Bankers Association, page 5:

"Legislation delegating discretionary authority should be as limited as possible."

Under the proposed act, a member could violate the provisions of the act and pay the $1,000 penalty and still continue as a member and violate again, whereas under the substitute we propose, while it permits the use of the emblem or insignia in advertising as it is now conducted by practically all of the 800 uninsured members of the Federal Home Loan Bank System, it would deter any advertisement or representation in any manner which would imply or convey the impression that its accounts are insured by the Federal Savings and Loan Corporation. Expulsion from membership in the Federal Home Loan Bank System would have more of a deterring effect than the payment of a $1,000 fine.

I think it is safe to assume that any member who so falsely betrays his membership in the Federal Home Loan Bank System deserves a penalty of expulsion from membership, not a $1,000 fine and continuing membership.

On examination of the Federal Home Loan Act I find that members of the Federal home loan bank are punished only by expulsion, as we now advocate in the substitute. Only nonmembers are punished through the Federal Criminal Code.

Personally we know of no instance of false representation having been made by any institution, but have been told by those who are proposing this prohibition that several associations who are uninsured members of the Federal Home Loan Bank System have advertised in such a manner as to convey the impression that they are insured by reason of being a member of the Federal Home Loan Bank System. It seems to us, who are innocent of such conduct, that the Board itself does have inherent power to prevent those acts by seeking an injunction in a court of equity, without having the Congress to adopt a law which would prevent honest-to-goodness members of the Federal Home Loan Bank System publishing and declaring to the world that they are members of that System. If there is need of a law to bar impersonation or false representation by its members, it should be by due process and not by regulation.

THE PROPOSED ACT IS DISCRIMINATORY

Let us for the purpose of argument assume that there are 800 uninsured members of the Federal Home Loan Bank System in the United States, and that 10 of them are guilty of the act complained of. If the proposed act becomes a law or regulation it would result in 790 innocent members of the bank being prohibited from advertising the fact that they are members of the Federal Home Loan Bank System, except in their local communities, although the insured members are permitted to display the emblem and advertise it without any limit whatsoever. Both insured and uninsured members of the Federal Home Loan Bank System have in all other respects the same rights and are under the same liabilities, except that the uninsured members are not chartered by the Federal Government or insured by the Federal Savings and Loan Corporation. As far as their rights are concerned they have the same right of borrowing power and ownership of stock. As their size increases they automatically are required under the rules of the Federal Home Loan Bank System to increase their capital stock holdings.

The Federal Home Loan Bank System was created by act of Congress in 1932 and was largely patterned after the provisions of the Federal Reserve System, the purpose of which was to provide a means by which its members could by the purchase of stock in the bank provide a reserve of liquidity available to the member institutions in the event of a stringency in finance, which stringency would prevent commercial banks from advancing their funds to the building and loan institutions. It provides an independent agency or reserve system which would be available to its member institutions in the case of an emergency. It will be seen, therefore, that membership in the Federal Home Loan Bank System is a valuable source of supply to the institutions when the institutions need financial help. Fortunately, up to this moment, it has not been necessary for any institution within our knowledge to use its reserves so built up in the treasury of the Federal Home Loan Bank System. On the contrary, they have used the bank as a means of deposit for surplus funds and have proven their loyalty to the Bank System by so doing.

It seems that a Federal Home Loan Bank Board should not be put in a position where it must discriminate between its members, not because of acts they have committed offensive to the System, but that may be offensive to some of the members of the System. It must be remembered that we are all bound together by the same tie, and what affects one member affects us all. No association can live to itself, because its acts reflect upon the whole membership of the bank and on the whole industry, irrespective of whether they belong to the bank or not.

It is most surprising to those of us who are members of the United States Savings and Loan League to have it take the position that it has before this committee, by its approval of an act of discrimination; and if the act is a proposal of the Federal Home Loan Bank Board it proves that it is in sympathy with the act of discrimination which is evidenced by the wording of the act, and therefore they should not be vested with a power of discrimination.

THE TREND TO FORESAKE THE TRUE PURPOSES OF THE ORGANIZATION AND FUNCTIONS OF A SAVINGS AND LOAN OR BUILDING AND LOAN ASSOCIATION

Last year at its convention in Philadelphia, Pa., the United States League celebrated the 125th anniversary of the founding of the savings and loan or building and loan associations in the United States. The principles undergirding the movement until recently have been:

1. The realization of a local community need of decent housing by the citizens of the community.
2. The pooling of their savings into a mutual fund to be used to supply the need.
3. The sharing of the profits equally among those contributing to the fund.

It has been therefore a purely mutual cooperative private enterprise. Through a strict observance of those principles above enumerated, the movement has grown in proportion to the growth in population and wealth of the people of the United States, until it has been recognized that "The American Home is the safeguard of American liberties."

Secretary H. L. Cellarius of the United States League in his 1930 annual report listed the following:

States	49
Number of associations	12,342
Membership	12,111,209
Assets	$8,695,154,220

The savings and Loan Fact Book published by the United States Savings and Loan League in 1956, pages 40 and 41, reports as follows:

States	48
Territories	4
Number of associations	6,048
State	4,365
Federal	1,683
Assets	$37,800,000,000

Of the above, 4,307 are members of the Federal home loan bank as of December 31, 1955, divided as follows:

Federal charter	1,683
State charter, insured	1,861
State charter, uninsured	763
Total	4,307

During the decade ending with 1955, savings and loan associations made the largest gain in savings (336 percent of any type of thrift institution with the exception of credit unions (500 percent). In third place were mutual funds (291 percent); and in fourth place mutual savings banks (84 percent).

A large part of this increase is due to favorable economic conditions such as a booming national income, although aggressive advertising of the Federal insurance feature has contributed in a large measure to the increase. In the battle for the community's savings the insured, as well as the uninsured institution, must of necessity use every honorable and ethical means to secure the savings of the people.

The insured institution rests its security upon its contribution to a fund in the Federal Savings and Loan Corporation or a State guaranty fund, the uninsured upon a sound and safe management and the building of its own reserves for that rainy day which may or may not come, practicing in its own policy those attributes it encourages its stockholders to practice.

We, who are not insured, deplore the trend not only of the banks but also of the savings and loan associations to grow to be the largest in the community, therefore placing the emphasis on bigness rather than safety. A steady normal growth is much more to be desired than a phenomenal growth.

We limit our mortgage lending to encourage home building and home ownership, and limit it to the local community of the State in which we live, not crossing State lines.

In the conduct of our institution we keep in mind always the above principles, and although we are an uninsured State association we feel absolutely secure, and merit the confidence which we have earned of those who place their savings in our care.

We do not ask and have never used any Federal help in the way of FHA or GI loans.

We make only conventional mortgage loans on the direct reduction plan bearing 6 percent interest, although we do have an FHA Home Improvement Loan Department for the convenience of our stockholders.

Based on long experience, we firmly believe that the State uninsured savings and loan or building and loan association dependent wholly on the honesty and integrity of its management is the best demonstration of what a group of free citizens in a free republic may accomplish to teach thrift, inspire faith in our fellow countrymen, and thus encourage home ownership instead of public housing tenancy. It is a shining example of free private enterprise.

We submit that if the act as proposed becomes a law of the Congress we shall be compelled to withdraw our membership in the Federal home loan bank as well as in the United States League.

For the above reasons we submit that our substitute, or any other wording you may deem necessary to implement the objectives we have attempted to enumerate herein, should be enacted into law by the Congress, rather than the proposed act.

We thank you for your indulgence.

(The attachments to Mr. Speckman's statement will be found in the files of the committee.)

Mr. SPECKMAN. Thank you very much.

Senator ROBERTSON. Thank you very much.

The committee will stand in recess.

(Whereupon, at 11:45 a. m. the subcommittee recessed until 10 a. m. the following day, Friday, February 1, 1957.)

STUDY OF BANKING LAWS

(Financial Institutions Act of 1957)

FRIDAY, FEBRUARY 1, 1957

UNITED STATES SENATE,
COMMITTEE ON BANKING AND CURRENCY,
SUBCOMMITTEE ON BANKING,
Washington, D. C.

The subcommittee met, pursuant to recess in room 301, Senate Office Building, at 10: 05 a. m., Senator A. Willis Robertson (chairman of the subcommittee) presiding.

Present: Senators Robertson and Clark.

Senator ROBERTSON. The committee will please be in order. The first witness today will be Mr. James W. Grant, representing the Credit Union National Association. You may proceed.

STATEMENT OF JAMES W. GRANT; ACCOMPANIED BY DAVID R. WEINBERG, REPRESENTING THE CREDIT UNION NATIONAL ASSOCIATION

Mr. GRANT. Mr. Chairman, our association has prepared a statement which I believe has been passed out to the members of the committee. It pretty much states our position and the changes which have been suggested by the advisory group in the Federal Credit Union Act.

Mr. Weinberg of our national association is here with me and we would be very happy to be interrogated and answer any questions which the Chair or members of the committee might see fit to put to us.

Senator ROBERTSON. Without objection your statement may be incorporated in the record.

Mr. GRANT. Thank you.

(The prepared statement of the Credit Union National Association follows:)

STATEMENT OF THE CREDIT UNION NATIONAL ASSOCIATION, INC.

TITLE VII—FEDERAL CREDIT UNION ACT

SEC. 1. *Short title.*—Same as section 1 of Federal Credit Union Act (F. C. U. Act).

SEC. 2. *Definitions.*—The revision of section 2 of the F. C. U. Act is supported.

SEC. 3. *Creation of bureau.*—Insertion of the new provision herein is supported.

SEC. 4. *Federal credit union organization.*—Same as section 3 of F. C. U. Act.

SEC. 5. *Approval of organization certificate.*—Same as section 4 of F. C. U. Act.

SEC. 6. *Fees.*—Same as section 5 of F. C. U. Act.

SEC. 7. *Reports, examinations, and audits.*—It appears that the two references to "section 5" in the last sentence of subsection (a) should properly be to "sec-

84444—57—pt. 2——12

tion 6." We are opposed to the provisions in subsection (b) for the following reasons:

1. In our opinion, the Bureau of Federal Credit Unions is presently maintaining close, effective supervision and is performing thorough, comprehensive examinations of the credit unions under its jurisdiction.

2. The Credit Union National Association supports the bureau's policies in this connection.

3. The Bureau of Federal Credit Unions and the credit-union movement are cooperating in a study of methods and techniques for improving internal control and supervisory committee audits, and definite action is being initiated to achieve this goal. As an integral part of this program, the bureau recently prepared and issued a comprehensive supervisory committee manual which enlarges upon and explains with clarity and in considerable detail the purpose, theory, and process of audit and is primarily designed to enhance the quality of audit performance. An internal control checklist contained in this publication should prove of considerable value as a further guide to the committee. A supplement to the accounting manual, also recently issued by the bureau, contains additional information designed to assist in the institution and maintenance of effective internal control.

4. In conjunction with this endeavor, the Credit Union National Association and the various State leagues and chapters are conducting training classes and publishing materials which are now reaching supervisory committee members and other credit-union leaders and officials on a National, State and local level.

5. Among the proposed additions to section 14 in this committee print bill is authorization for the directors to provide for compensation of necessary clerical and auditing assistance requested by the supervisory committee. Utilization of such assistance will result in assigned portions of the audit being performed by skilled professionals under the direction and control of the committee.

6. As a result of the present joint studies and endeavors, appropriate revision of the section of the act specifically dealing with the duties and responsibilities of the supervisory committee may be proposed.

7. Since the credit-union movement and the bureau are in the process of making a complete and careful study of the entire subject and are in the midst of instituting concrete action based upon their findings, it is suggested that the proposed addition to the act set forth in subsection (b) is premature. We therefore respectfully request that the entire subsection be deleted.

SEC. 8. *Powers.*—Same as section 7 of FCU Act.

SEC. 9. *Bylaws.*—The amendment to section 8 of the FCU Act is supported.

SEC. 10. *Membership.*—Same as section 9 of FCU Act.

SEC. 11. *Members' meetings.*—Same as section 10 of FCU Act.

SEC. 12. *Management.*—Same as section 11 (a) of FCU Act. Advisory committee recommendation 168 indicates that it is the feeling of the committee that the treasurer be prohibited from serving on the supervisory committee. We urge that consideration be given to incorporating such exclusion in this section.

SEC. 13. *Officers.*—The amendment to section 11 (b) of FCU Act is supported.

SEC. 14. *Directors.*—The amendment to section 11 (c) of the FCU Act and incorporation of advisory committee recommendation 170 are supported.

SEC. 15. *Credit committee.*—The amendments to section 11 (d) of the FCU Act are supported. However, in order properly to define the scope of activity of the loan officer, for whom compensation is authorized in proposed section 14, it is suggested that the following be added after the last word in the second sentence:

", or by any loan officers appointed by the committee. No loan officer may approve a loan in excess of the unsecured limit unless such excess is fully secured by unpledged shares."

SEC. 16. *Supervisory committee.*—Same as section 11 (e) of FCU Act.

SEC. 17. *Reserves.*—Same as section 12 of FCU Act.

SEC. 18. *Dividends.*—The amendments to section 13 as proposed by advisory committee recommendation 180 do not appear to be accurately reflected in the wording of the proposed section. It is respectfully suggested that a section worded somewhat as follows be substituted therefor:

"Annually or semiannually, as the bylaws may provide and after compliance with reserve requirements, the board of directors may declare a dividend to be paid from the remaining net earnings. Such dividends shall be paid on all paid-up shares outstanding at the end of the dividend period. Shares which become fully paid up during the dividend period shall be entitled to a proportional part of said dividend provided that said shares shall be outstanding at the close of the period for which the dividend is declared. Dividend credit for the month may be accrued on shares paid in and which become fully paid during the first 5 days of the month."

SEC. 19. *Expulsion and withdrawal.*—Same as section 14 of FCU Act.

SEC. 20. *Minors.*—Same as section 15 of FCU Act.

SEC. 21. *Certain powers of director.*—We have no position regarding new subsection (i) relating to conflicts of interest. However, we are of the opinion that if the proposal is adopted, the restriction imposed therein upon former employees should be limited to a 2-year period from the date of termination of employment.

SEC. 22. *Fiscal agents and depositories.*—Same as section 17 of FCU Act.

SEC. 23. *Taxation.*—Same as section 18 of FCU Act.

SEC. 24. *Partial invalidity; right to amend.*—Same as section 20 of FCU Act.

SEC. 25. *Space in Federal buildings.*—The amendment to section 21 of FCU Act is supported.

SEC. 26. *Territorial applicability of act.*—The amendment to section 22 of FCU Act is supported. However, it is suggested that the Panama Canal Zone, which is in the current act and is neither a possession nor territory, be specifically included in the proposed section.

TITLE VIII—MISCELLANEOUS AMENDMENTS

Amendments to Criminal Code

SEC. 803. (a) *Section 217 of title 18 of the United States Code.*—We do not support the portions of the proposed amendment dealing with offers of employment. It is suggested that adoption of these portions of the amendment may result in unduly restricting the opportunity of credit unions to attempt to obtain skilled, qualified help in a reasonably specialized field. We are of the opinion that the incorporation of proposed section 21 (i) in the FCU Act would establish sufficient control and prevent possible abuses since employment could not actually be accepted in any Federal credit union by the affected employees except pursuant to regulations prescribed by the director of the bureau.

It is further suggested that the language of the proposed amendment may be too broad in that the restrictions contained therein apparently also apply to clerical and other employees who are not directly or indirectly involved in the supervision and/or examination of Federal credit unions.

The loan restrictions contained in subsection (iii) also appear to be unduly restrictive.

(b) *Section 218 of title 18 of the United States Code.*—We do not support adoption of the portions of the proposed amendment dealing with acceptance or agreement to accept offers of employment since we are of the opinion that incorporation of proposed section 21 (i) in the Federal Credit Union Act would establish an effective means of controlling such activity.

It is further suggested that the language of the proposed amendment may be too broad in that the restrictions contained therein apparently also apply to clerical and other employees not directly involved in the supervision and/or examination of Federal credit unions.

The loan restrictions contained in subsection (iii) also appear to be unduly restrictive.

(h) *Subsection (g) of section 2113 of title 18 of the United States Code.*—The amendment is supported.

Senator ROBERTSON. Do you wish to highlight any part of your statement on which you care to place emphasis?

Mr. GRANT. Not in any particular fashion, sir. As I said, I think it states very clearly and concisely our position on the act. The one particular point which is contained on the first page of this statement, under section 7—I will not go into the reading of it or anything of that type—but I just want to emphasize our position verbally in opposition to the suggestion that the Federal credit unions be subjected to an additional examination by outside agencies of certified public accountants.

We in the national association have long felt the need of better supervisory reports and we have taken, as this statement will indicate, steps during the years to provide for better supervisory work. Many of our credit unions at the present time are engaging the services of accountants in their own sphere of membership or outside to perform the type of supervisory work which will give them the type of report which is indicated here by the recommendation.

Senator ROBERTSON. I understand then that you support the major provisions of the bill with respect to Federal credit unions but you offer some changes?

Mr. GRANT. Yes, sir. That is true.

Senator ROBERTSON. I notice you offer a change on page 4 of your prepared statement wherein you say that you do not think the language of the bill on dividends is quite accurate, and you suggest a different wording there.

Mr. GRANT. That is true. Yes, sir.

Senator ROBERTSON. When the committee writes up the technical bill we will be glad to bear in mind the suggestions you made, and we appreciate your appearance.

Mr. GRANT. Thank you very much.

(The following was subsequently received for the record:)

REVISED STATEMENT OF CREDIT UNION NATIONAL ASSOCIATION, INC., ON PROPOSED SECTION 15 OF SENATE COMMITTEE PRINT BILL ENTITLED "FINANCIAL INSTITUTIONS ACT OF 1957"

The Credit Union National Association, Inc., hereby reverses its position with respect to the change in proposed section 15 of the Federal Credit Union Act as indicated in its statement on the Senate committee print bill entitled "Financial Institutions Act of 1957" which authorizes the Director of the Bureau of Federal Credit Unions to establish by regulation lower loan limits than those currently in effect.

When the Congress originally adopted the Federal Credit Union Act in 1934, it very wisely prescribed a reasonable limit on both loans made without security (signature loans) and on those larger loans which required collateral. Since that time, credit unions have functioned within these limits although a normal growth in the size of the average loan granted has occurred. This has been due in large measure to our improved standard of living and increased cost of goods and services which has resulted in a diminution in actual purchasing power of the dollar. Further, as credit unions developed, the close association of the members in a common bond provided a firm basis upon which to extend increased credit.

In the more than 22-year period since the law has been in effect, millions of individual loans have been granted with an insignificant and enviable loss record. This fact is borne out by the testimony of the Director of the Bureau before this committee to the effect that the loss experience of Federal credit unions is only 0.15 percent of the money loaned. No evidence has been presented to indicate that a change in the current loan limit is warranted on the basis of excessive losses.

Credit unions are designed to serve broad and diverse segments of our population with varying economic needs and capabilities. For example, organizations of professional people are helping members buy equipment essential to setting up or expanding practices. Although a relatively higher loan might be required, the member's current and potential income makes such loan sound and desirable. The need of the farmer for substantial, short-term credit in order to finance crops is also being met. Other groups are being served by comparatively smaller loans for longer periods of time. Such variations make essential the retention of flexibility and self-determination in the law.

Although instances of extension of excessive credit may have occurred, they have been few and isolated. No evidence has been presented to indicate that such loans have resulted in losses which have impaired the value of members' shareholdings or have forced the liquidation of credit unions. It would, therefore, appear to be evident that boards of directors and credit committees have generally met their responsibility in this connection in an effective manner.

Generally, as credit unions have grown, these bodies have by self-regulation established lower loan limits than allowed by law.

It is respectfully suggested that the advisability of authorizing the Director of the Bureau to establish by regulation lower loan limits for all credit unions or for one or more classes of credit unions than those currently prescribed by law be subjected to a searching reevaluation. The net effect of such provision would be to centralize in one person a discretionary power which is of vital importance to each individual credit union and does not lend itself to general or blanket administration. Further, it would seriously infringe upon the responsibility of the board of directors and the credit committee to determine practical loan limits within their own credit union based upon their knowledge of the needs and capacities of the membership. This could result in depriving the members of maximum utilization of the credit facilities made available as a result of funds accumulated through cooperative thrift. It is urged that this flexibility is essential and would inevitably be lost under administrative directives and regulations. Based upon the above factors, we are of the firm conviction that empowering the Director of the Bureau of Federal Credit Unions to establish lesser loan limits than those currently provided for in the law is unnecessary and unwarranted. It is therefore respectfully requested that such provision be deleted from proposed section 15.

Senator ROBERTSON. The next witness is the National Association of Credit Men. I understand Mr. Robert L. Roper will speak for them.

STATEMENT OF ROBERT L. ROPER, LEGISLATIVE DIRECTOR, NATIONAL ASSOCIATION OF CREDIT MEN

Mr. ROPER. Mr. Chairman, distinguished gentlemen, I am Robert Lee Roper, legislative director of the National Association of Credit Men, New York City. I am here to present the statement of Mr. Henry H. Heimann, executive vice president of our organization, with regard to that part of section 26, title III, of the Financial Institutions Act of 1957 which proposes to extend certain of the interest provisions of the Federal Reserve Act to the Federal Deposit Insurance Act.

First, may I say that Mr. Heimann has asked that I convey his most sincere regrets to the distinguished members of this committee that he cannot personally appear to present the views of our organization's membership. He would certainly want to do this and would do so if it were not for a family illness problem of the most pressing urgency which takes him to the Midwest. He does wish to thank this committee for letting us submit the views of our organization and its membership at this time.

Our organization and our members have always held this particular committee in the highest esteem and have cooperated with it on many occasions. We want to do everything in our power to give you gentlemen our fullest cooperation always.

The following statement which I shall read if the committee so desires is our observation only on that part of title III, section 26, appearing at page 163 of the committee print which reads as follows:

No insured bank shall, directly or indirectly, by any device whatsoever, pay any interest on any deposit which is payable on demand and for such purpose the Administrator may define the term "demand deposits"; but such exceptions from this prohibition shall be made as are now or may hereafter be prescribed with respect to deposits payable on demand in member banks by the Federal Reserve Act, as amended, or by regulation of the Board of Governors of the Federal Reserve System.

This provision as we understand it would in effect prohibit the absorption of exchange by nonmember banks who are insured under the Federal Deposit Insurance Corporation. We are, of course, fully aware that this would in no way prohibit the charging of exchange, nor would it prohibit the nonpar payments of bank checks.

We also understand that the enactment of this provision would in no way affect the 500 or so nonmember banks who are not presently insured under the Federal Deposit Insurance Corporation. We do emphatically applaud the fact that the enactment of this provision would at long last bring to an end through an act of Congress the confusion which has arisen over the years from diverse rulings of different agencies as to what constitutes an unlawful payment of interest.

We further applaud the fact that the enactment of this provision would in effect give congressional sanction to one uniform definition of interest, a sanction which we respectfully submit has long been needed.

Despite the fact that much of the following statement may seem an argument for par clearance of bank checks and therefore seemingly irrelevant to the basic question now under consideration as to whether or not exchange absorption should be deemed an unlawful payment of interest, we hold that there is indeed now, as there has always been, a direct relationship between these two questions, and that in making our position on the one clear we must perforce bring forth our arguments for the other. The relationship of these two questions we believe you will find is developed in the course of our presentation.

Mr. Chairman, is it the desire of the committee that I read the statement of Mr. Heimann.

Senator ROBERTSON. The committee would be just as willing for you to insert that full statement in the record and then you summarize it for us.

Mr. ROPER. Yes.

Senator ROBERTSON. Because as you know we have already had considerable testimony on this very issue.

Mr. ROPER. Yes.

Senator ROBERTSON. Naturally we will be glad to have your viewpoint, but it will not involve anything that is new to us in arguments pro and con.

Mr. ROPER. Yes.

Senator ROBERTSON. Without objection the full statement of Mr. Heimann can be inserted in the record and then you can summarize it for us.

(The prepared statement of Henry H. Heimann follows:)

STATEMENT OF HENRY H. HEIMANN, EXECUTIVE VICE PRESIDENT, NATIONAL ASSOCIATION OF CREDIT MEN

I am executive vice president of the National Association of Credit Men. Our home officeis in New York with direct branch offices in Chicago and St. Louis. Our local offices of affiliated units are 144 in number and are located throughout the country.

I herewith respectfully submit the views of our organization and the majority of its members with respect to that part of title III, section 26, payment of interest of the Financial Institutions Act of 1957, which would, in effect. extend the exchange-absorption provisions of the Federal Reserve Act to the Federal Deposit Insurance Corporation Act as respecting nonmember insured banks.

Our organization, composed of more than 35,000 credit executives in industrial, commercial, and financial concerns of all sizes—large, medium, and small—and operating in all lines of business, has always been keenly aware of the need for sound banking law as essential to the economic health of the Nation. For the more than 60 years of its existence its members have taken keen interest in the promotion of sound banking legislation. Our members were very active in the promotion of the Federal Reserve Act, a work which the late Hon. Carter H. Glass so generously acknowledged.

It has been the particular interest of our members that bank checks be cleared and payable at par and that check recipients, wherever they may reside, shall be able at all times to receive full payment for the goods they sell and the services they render. Our organization and our members urged the inclusion of the par payment provisions in the Federal Reserve Act at the time it was originally enacted. Also, through the years we have sought, by educational means, to persuade the nonpar banks that it is to their long-range advantage to adopt a policy of honoring their depositors' checks to out-of-town payees for the full face amount at which their depositors indicate they wish their checks to be paid.

That we have been, to some measure, successful in this program is borne out by the fact that there are now 10 fewer nonpar States than there were in 1943. Seven of the ten have become par clearing entirely by voluntary action. In a few areas, however, our members have felt obliged to seek remedy through appeal to their State legislatures. Largely at the behest of our members in those States, therefore, par clearance legislation was enacted in Iowa in 1943, in Nebraska in 1945 and in Wisconsin in 1949. In Nebraska the constitutionality of its par clearance legislation was upheld in 1947 by the State Supreme Court in *Placek* v. *Edstrom* (*Saunders Co.*) (32141 17 S. C. J. 79, 148 Neb. 79).

The particular interest of the credit community in par clearance is based on the fact that credit plays a major role in the commerce of our Nation. It may indeed be called the very lifeblood of commerce and industry. It is our national currency. It has been our constant aim, therefore, that everything possible be done to keep credit channels open. It is our firm conviction that wherever barriers exist against the free flow of credit, business is impeded at least to that extent in its service to the public. Exchange charges on bank checks are such barriers.

Years ago bank checks were not generally acceptable. Modern transportation and communications did not exist. Marked variations existed between States and between regions in the supply and demand for money. To cover the costs of transference, deduction of a part of the face amount of any check became common banking practice. Many bankers discovered that such deductions also added substantial revenue. For example, prior to the establishment of the Federal Reserve System, many banks found it to their advantage to route checks from one out-of-the-way point to another. Thus in many instances one check would be routed through a half dozen banks or more, with each bank gaining its advantage before the check was finally cleared. Circuitous routing of checks in those days permitted many banks to show favorable balance sheets by reason of the number of checks outstanding which were not reflected in the total deposits shown on their statements.

In earlier days the argument was put forth that the currency needs of banks were increased by their out-of-city payments and that this involved a measure of expense. It is significant that at no time was an exchange charge levied by a central city bank on its checks to cover such expense. It should not have been done, but if this expense of clearing out-of-city checks had been a factor, then it would have been consistent for the central city banks to levy a charge on their own checks. Obviously, they did not feel this to be warranted.

Today, however, with the clearing facilities of the Federal Reserve System open to all par banks. State and National, member and nonmember, an efficient method for check clearances has been established. Not only are check clearances to any part of the country greatly speeded but the expenses to the banks involved are substantially reduced. The increased facility of check collection through the Federal Reserve has contributed in no small measure to the increased use of bank checks as a standard medium of currency.

It is no exaggeration to say that today by far the greatest proportion of business is handled by check. Even at the consumer level, each year finds more and more people paying their monthly heat, rent and light bills, and even their grocer's bill, by bank check. As such, bank checks may now, more than ever, be considered the basic currency of the land. Nevertheless, there are some 2,000 banks, banking offices and branches which still follow the old practice of discounting these checks. In effect, they are discounting the national currency.

Their reason for continuing this custom, as we understand it, is basically that to do away with this income to which they have been accustomed would affect their earnings. We appreciate this view. Certainly no group recognizes better than the credit men that sound banking requires adequate levels of bank earnings. The bankers are entitled to and should have reasonable returns on their capital investment. We fully subscribe to that fundamental premise because we are interested in having the soundest possible banking system. However, a point frequently overlooked in their argument is their assumption that no alternative income sources could readily be substituted for the exchange charge. This is a fallacious assumption. Experience with par clearance confirms our view.

When par clearance legislation was being sought in Nebraska, for example, some 2 years after the Iowa act, a comparative statement of earnings and expenses of the Iowa banks for the years before and after the enactment of the par clearance statute in that State was submitted by the superintendent of banks in Iowa. In an accompanying letter he said not only that "no Iowa bank was forced out of business on account of the passage of the Iowa par check bill," but added: "Iowa banks have quite generally adopted service charges, which income has more than offset the loss of exchange from the antiquated method of charging on checks received in the mail. Thus, each account in the bank pays its own way and the responsibility for the activity is borne by the owner of the account. I have heard of no complaint by an Iowa bank of the loss of income from charging exchange on incoming items." Such favorable experience has also been reported from the other States whose banks have become all par clearing.

The Iowa bank superintendent's statement was submitted in 1944 during World War II, when interest rates were artificially low. They now have reached much more favorable levels from the banking standpoint. Interest rates today make loans an excellent source to expand bank revenues. At the same time such loans would permit concentration of needed funds in the development of local communities rather than in the balances of exchange-absorbing correspondent banks located in other areas.

Alternative sources of revenue today would include, first of all, compensating service charges to depositors. These are truly competitive, as they are in effect the price of a bank's services to its customers. This cannot be said of exchange charges. A payee whose checks from customers are discounted certainly has no control as to what bank his customer uses. A second alternative source is interest on loans; a third, the bank's returns on its own investments.

The fact that the vast majority of the Nation's banks—including large banks and small banks, city banks and country banks—find service charges to depositors, interest on loans and returns on investments to be ample source of revenue, should be argument enough that elimination of exchange charges would not impede future operations, despite the claims of some exchange-charging banks.

Furthermore, there are banks which both collect exchange on checks and levy a service charge against their depositors. By this charge they collect twice for the same check—once from the depositor and once again from the payee.

The equity of service charges as against exchange charges should have consideration at this point. Any person or businessman who receives a check should get 100 cents on the dollar. A check payee accepts a check through a desire to accommodate his customer. A depositor, in writing a check for a certain amount, expresses his intent that the payee receive the amount designated on the face of the check in full settlement of that depositor's obligation to the payee. The costs of handling the depositor's check are, or should be, considered a part of the bank's normal overhead expense; if they are not, then the bank should be compensated for them by the one it serves—its own customer who is the depositor. The check payee is not served by the depositor's bank, but is merely accommodating his customer by accepting the latter's bank check in full settlement of the customer's obligation. If the bank does not pay in full a depositor's check, the depositor's obligation is not fully settled, though he did in fact write a check for the full amount.

It is a rather startling and revealing fact that in the vast majority of instances depositors using nonpar banking facilities are totally unaware that their banks are failing to honor the full amounts of their checks and that those who receive their checks are receiving less than face value. If the fact were more widely known, we are confident that most would seriously object.

Some of our members have expressed a desire for an amendment to the National Banking Act, or other legislation, making it compulsory for banks to state publicly if they are par or not. If, as nonpar spokesmen profess, these banks have nothing to hide or apologize for in discounting their customers' checks, the exchange-charging banks should not be reluctant to let the customers know. We feel that such a "Pure Food and Drugs" Act of banking, by putting the right label on the right container, as it were, would in a very short time halt check-discounting practices, and the pressure would be from these banks' own depositors. Exchange charges may be described as hidden charges in every sense of that phrase—concealed as they are from the eyes of the banks' own depositors.

The proposed provision, now under discussion by this committee, to amend the Federal Deposit Insurance Act with regard to payment of interest would not directly make illegal the nonpar payments of bank checks, nor would it directly prohibit the charging of exchange, but it would, by forcing into the open, those hidden exchange charges which are now absorbed by correspondent banks, cause the customers of these banks to understand these discounting practices and enable them to object to them. With absorption prohibited, however, most check discounting banks would no doubt immediately see the wisdom of ceasing exchange charging operations altogether.

Another fact not commonly known is that, despite maximum exchange charge limits of one-tenth or one-eighth of 1 percent, set by statute in some States and determined by general agreement in others, these charges are not so nominal as appears on the surface. Rates charged by nonpar paying banks frequently vary and the intermediate correspondent banks in many cases add further charges, so that the amount of exchange and collection charges paid by our members reach totals which are a real burden on commerce. We have been advised of charges amounting to as much as $2.04 on a check of $340.10, $24 on a check of $15,000, $68 on a check of $17,000, and $70 on a check of $35,000. These run well above the original exchange charge rate of $1 or $1.25 per $1,000. Total costs to business and the public at large from such charges are estimated to be millions of dollars each year, despite the fact there are now only about 2,000 exchange-charging bank outlets out of a total of well over 20,000 banking offices.

Furthermore, the costs to the public are not to be measured only in terms of the direct monetary costs of exchange charges alone. These charges must often be met by out-of-town hospitals, schools, churches, and charitable organizations just the same as any business. They receive less than their well-intentioned contributor indicates on his check. The depositor pays in full, but the organization gets less while the depositor's bank benefits by the difference.

Exchange charges also affect the public in terms of their day-to-day necessities and cost of living. While many of the larger businesses and corporations are able to keep substantial compensating balances with the exchange-absorbing banks, this is not generally true of smaller businesses in the nonpar areas. The grocer, plumber, dry-goods dealer, and other small merchants and tradesmen in these communities, in accepting a check drawn on an out-of-town bank, must often be content with payment for less than the true value of their goods and services.

The small-business man faced with such exchange charges is often helpless to do anything about them. He usually does not have the resources or the competitive position to enable him to risk losing an account by refusing his customer's checks. Yet he must meet these extra costs. They are therefore necessarily reflected in the bill to the customer, along with overhead and other business expenses. Once again the exchange-charging bank gains, while the public pays.

It has been suggested that the elimination of exchange absorption by insured banks, as contemplated by the provision under discussion, might be detrimental to small banks. In the aggregate, exchange charges are absorbed only where compensating balances are maintained. In the case of interbank balances, the larger banks which hold these balances recoup the cost of such absorption by investing the funds left with them by their small bank correspondents.

In the case of business depositors, only the larger firms and usually those with a nationwide distribution can afford to maintain the large balances necessary to compensate for exchange charges on their customers' checks. It is revealing, also, that well-managed small banks, even in areas where the nonpar banks are concentrated, serve their communities well, make a fair return on their investment, and cash checks drawn on themselves at par, whether presented over the counter or through the mails.

The thought also has been advanced that such a provision as proposed carries a threat to our Nation's traditional dual-banking system. Most of the State banks, as well as all National banks, now pay their checks at par, and make efficient use of the par-collection facilities of the Federal Reserve banks, without discrimination of any sort between the State and National banking systems. For this reason, we feel, the dual-banking system is not jeopardized and the argument has no validity.

There has been the assertion, too, that elimination of exchange absorption would threaten the individual unit bank operation, as opposed to branch, chain,

and group banking operations. It is wholly fallacious to assume that those banks which are now nonpar could not exist if their exchange-charging operations were to be abruptly terminated, and that branch, group, or chain banks are poised ready to step into their community and take over when this former source of revenue is eliminated.

Alternate sources of revenue, as we have pointed out, are now abundantly available. That such small unit banks can prosper without the exchange absorption privilege has been proved time and again by the many who do expand on a par-paying basis of operations.

Our organization and the members it represents heartily concur with those who deplore the existing lack of uniformity in our present banking regulations as to what does and what does not constitute an unlawful payment of interest. The proposed amendment would bring to an end once and for all the conflict in ruling. By putting all insured banks, whether or not members of the Federal Reserve System, on a uniformly competitive basis, the provision would in itself be a vastly significant milestone in sound banking legislation, with farflung benefits not only to the entire banking community but to all business and to the public.

We in business, and particularly in the credit profession, have traditionally regarded as interest any compensation for the use of someone else's funds, whether those funds are in the form of outright cash or of credit. The fact that exchange-absorbing banks insist that large compensating balances be kept with them on deposit by their nonpar paying correspondents, in return for the privilege they accord them of having these charges absorbed, makes exchange absorption a payment of interest on demand deposits, from whatever angle you view it.

In summation may we say that when any bank pays on its depositors' checks less than the amount written, commerce is impeded, the Nation's currency is debased, and the sound business concept of "fair payment for service rendered" is impaired. Business and the public pay the cost, while the advantage accrues to only the few. We, therefore, suggest that favorable consideration, with recommendation for adoption, be given title III, section 26, payment of interest, of the Financial Institutions Act of 1957.

Mr. ROPER. Thank you. I would like to highlight the parts of the statement in which Mr. Heimann says——

Senator ROBERTSON. You might first tell us in your own language why creditmen are interested in this provision.

Mr. ROPER. Yes. For many years now creditmen have been affected by deductions on the checks which they receive from customers. In many instances, of course, these deductions are absorbed by correspondent banks, and in those cases they are not directly affected by these deductions. However, the fact that absorption is allowed on the part of nonmember banks promotes the condition whereby exchange charges are made on checks.

Senator CLARK. Mr. Roper, could you tell us what States still engage in that system of deductions?

Mr. ROPER. There are 19 States in which there are now nonpar banks.

Senator CLARK. Are they geographically grouped together or are they scattered?

Mr. ROPER. Mostly in the South and Central Northwest.

Senator CLARK. Thank you.

Senator ROBERTSON. Your organization is a national organization; is it not?

Mr. ROPER. That is right. We have 144 offices throughout the United States with 35,000 members. Before I go further and before I answer further questions I want to say I am not a lawyer and neither am I a banker, nor have I ever had any banking or legal experience. Our purpose in submitting the presentation is to convey to the distinguished gentlemen of this committee the nonbank and nonlegal point of view of our members who are preponderantly lay executives in private commerce and industry, and who are charged with the responsibility in their own concerns of managing and administering their concerns' credit and collection policies.

We did in 1938 pass a resolution which was in effect a statement of policy of our organization and we have since abided by it fully. If I may, I will read that now:

The association fully recognizes the right of banks to charge their customers for services rendered to them. It recognizes and is sympathetic with the problems faced by many smaller banks throughout the country as a result of decreased revenue from the normal sources of banking income. It realizes that the practice of making exchange charges for clearing checks from a distant point has been adopted by a great many of the smaller banks as a means of obtaining additional needed revenue. While it believes that exchange charges are also being made by many banks which do not need the extra revenue thus obtained, the association does recognize that the complete and immediate cessation of making exchange charges by many smaller banks throughout the country would be detrimental to them. The association, however, does not regard the practice of clearing checks at less than par by making an exchange deduction from the face value of the checks as a legitimate method of obtaining revenue by banks. It believes that this practice is an unsound banking practice because its result is to impose the charge not upon the customer of the bank which clears the check and for whom the service was rendered, but upon the payee who sold merchandise to that customer and who was, therefore, entitled to full payment of the agreed price for that merchandise.

The association is aware of the argument that while a bank is obligated to clear checks in their full amount at the location of the bank, clearance for remittance to a distanct point may result in an additional expense to the bank. It realizes that banks should be compensated for service expenses but contends that the compensation should be paid by the banks' customer, the buyer of the merchandise. It recognizes also that the collection system of the Federal Reserve System was developed to obviate the losses and delays which formerly characterized many check clearances, and favors the use of that system with the consequent par clearance of checks as an aid to business and financial stability.

Senator ROBERTSON. Then nearly 19 years ago your organization, a national organization representing the credit men in all the States, said it was not fair to them to get a check which would not pay off what it said on the face of it.

Mr. ROPER. That is correct.

Senator ROBERTSON. And that they should not be called upon to make that type of contribution to the success of certain small banks.

Mr. ROPER. That is right.

Senator ROBERTSON. Has that been your consistent position ever since?

Mr. ROPER. That is right.

Senator ROBERTSON. While you would really prefer a mandatory par clearance law, considering the difficulties of getting one enacted you do endorse the pending proposal that we have a uniform definition of what is interest, which would automatically preclude the absorption of exchange?

Mr. ROPER. We feel that the enactment of this provision will bring many of the exchange charges which are now hidden from the depositor, in effect, by the absorption device, out into the open, and that many of the depositors who are unaware of having their checks discounted by their own banks will become aware of it and will be able to object to their own banks.

Senator ROBERTSON. You believe also that the competition will take care of the situation?

Mr. ROPER. That is right. The enactment of this provision will bring those hidden charges out into the open. Therefore, we favor it.

Senator ROBERTSON. I am not sure it is correct but I have been told we have only one nonpar bank in Virginia.

Mr. ROPER. That is correct.

Senator ROBERTSON. That is correct then?

Mr. ROPER. Yes, sir. Also there are only 2 in Kansas, and only 2, I believe, in Illinois.

Senator CLARK. Are those all small banks?

Mr. ROPER. There are some large banks and there are some large banking chains even, in certain States, which are nonpar. Many of our members who do extensive business in the Southern States or in the upper Midwest have reported considerable amounts that they have had to spend in exchange charges alone. One member with whom I was talking only a little more than a week ago said that his firm paid $8,000 in exchange charges over just the past year. Another firm it has been reported to us has had exchange charges of $75,000 over the past year.

Senator CLARK. Are those banks of which you speak, member banks?

Mr. ROPER. The exchange charges would be only from nonmember banks.

Senator CLARK. But from insured banks?

Mr. ROPER. There is no delineation there as to insured and noninsured. We do not have records on that, but I assume many of them are insured.

Senator CLARK. Probably most of them are; are they not?

Mr. ROPER. Most of them. Yes.

Senator ROBERTSON. I think your testimony has been interesting and helpful. Various State agencies have expressed to their Senators their interest in this provision. We think it could be a considerable item in doing business if 1 man had to pay $75,000 in 1 year. That is not any small charge.

We thank you very much.

Mr. ROPER. Thank you very much, Mr. Chairman.

Senator ROBERTSON. Mr. Donald E. Durick, Fort Wayne, Ind., was scheduled to appear representing the American Industrial Bankers Association. We have received a letter from him with a statement which he submits and without objection it will be made a part of the record.

(The statement of Mr. Durick follows:)

STATEMENT OF DONALD E. DURICK, FORT WAYNE, IND., EXECUTIVE SECRETARY, AMERICAN INDUSTRIAL BANKERS ASSOCIATION

Mr. Chairman, my name is Donald E. Durlick, executive secretary of American Industrial Bankers Association. We maintain our national headquarters at Fort Wayne, Ind. I have been with that organization for the past 3½ years and maintained the position of executive secretary in June 1956.

Due to conditions beyond my control, I find it impossible to appear, personally, before your committee in regards to the Financial Institutions Act of 1957.

Our understanding is that this bill does not include in its scope industrial banks, Morris Plan banks and industrial banking companies, all of which we are primarily concerned.

In various States, such as Colorado, New York, North Carolina, Massachusetts, and Michigan, the statutes provide for the organization and supervision of "banks," "savings banks," and "trust companies" as defined; but, in addition, provide, also, for the organization and supervision of "industrial banks" or "banking companies."

As far as the hearings are concerned, we are primarily interested with title III of the act which amends and revises the statutes governing the Federal Deposit Insurance Corporation.

Most of the industrial banks and industrial banking companies affiliated with our association accept public money which is not insured. The total of these savings, which are termed "deposits," "savings," "thrift accounts," "certificates of investment," "thrift notes," and "installment investment certificates," are in excess of $225 million. Although this amount is small compared with other banking institutions which accept public money, we definitely feel that these companies should have the opportunity of offering to their depositors Federal insurance on their savings.

We respectfully suggest that an amendment be inserted in title III, chapter I, section 301, section 2 (a) of this bill which would read as follows:

"2 (a) The term 'bank' means any bank, banking association, trust company, savings bank, industrial bank, industrial banking company, Morris Plan company or other banking institution, which is engaged in the business of receiving deposits, other than trust funds as herein defined, and which is incorporated under the laws of any State, any Territory of the United States, Puerto Rico, Guam, or the Virgin Islands, or which is operating under the Code of Law for the District of Columbia (except a national bank), and includes any unincorporated bank the deposits of which are insured on the effective date of this amendment, and the word 'State' means any State of the United States, the District of Columbia, any Territory of the United States, Puerto Rico, Guam, or the Virgin Islands."

If this is not deemed advisable, we believe that consideration should be given to the inclusion of a section in the Financial Institutions Act of 1957, which would include these institutions.

Senator ROBERTSON. The next witness scheduled was Mr. A. D. Shackelford of Wilson, N. C., but he sends a letter saying that his interest is in this question of absorption of exchange and he is satisfied to submit his written statement for the record.

Without objection we will file in the record at this time Mr. Shackelford's statement.

(The statement of Mr. Shackelford follows:)

STATEMENT OF A. D. SHACKELFORD, PRESIDENT, NATIONAL BANK OF WILSON, WILSON, N. C.

Mr. Chairman and members of the committee, I appreciate the opportunity to appear before you as a country banker deeply interested in legislation to eliminate the competitive advantage enjoyed by insured nonmember banks over member banks through absorption of exchange.

According to the June 30, 1956, edition of Polk's Bank Directory, North Carolina has 47 national banks with 59 branches. The State banks and trust companies number 167 with 270 branches. Only 6 State banks are members of the Federal Reserve System—one of which operates 12 out of city branches. In the immediate area of Wilson are 3 banks with 56 branches, over 45 of these branches being on a nonpar basis. In a few cities and towns these banks are forced to pay their checks at par because of par banks being located in these cities and towns. Obviously, we are in a position to experience the full effects of the competitive advantage afforded insured nonmember banks through the absorption of exchange.

During the year 1956 the exchange charged by nonpar banks on checks deposited by our customers amounted to $13,012.06. This represents the amount of bait our competitors were in a position to offer our customers through absorption of exchange if they would transfer their accounts to the nonmember banks. This is tempting "bait" for a concern handling a sizable amount of checks drawn on nonpar points.

Since 1943 the member banks of North Carolina and a few other States have been faced with this unfair competition, because the Board of Governors of the Federal Reserve System has taken the position that absorption of exchange charges by member banks involves a payment of interest, whereas the Federal Deposit Insurance Corporation has taken the position that the absorption of such charges by insured nonmember banks does not constitute a payment of interest. Surely it was not the intent of Congress to place member banks at a disadvantage competitively with insured nonmember banks. Yet this has occurred because of the conflicting rules by the two agencies respecting the absorption of exchange.

Officials of both agenies are in agreement that this condition should be corrected. In the November hearings before your committee (p. 169) Mr. J. L. Robertson, member, Board of Governors, Federal Reserve Board, stated: "The Board believes that this lack of uniformity should be corrected, either by an express statement in the law that absorption of exchange is, or is not, to be considered a payment of interest for both member and nonmember insured banks." At the same hearings in November (pp. 292–293) Mr. Royal R. Coburn, General Counsel, Federal Deposit Insurance Corporation, in reply to questioning by Mr. Kenton R. Cravens, chairman of the advisory committee, stated: "The matter was presented to Congress some 10 years ago and it was our position then that if it was to be deemed to be the payment of interest, that is, the absorption of exchange, Congress should expressly so provide. We feel that Congress should so expressly provide. There is no doubt that there is unfairness when one bank can absorb it and another bank cannot, depending on whether or not it is a member of the Federal Reserve System. But we think that that is a matter which should be decided by Congress, and should not be done indirectly under present law."

Probably it was presumptious on my part but when I requested permission to appear before this committee it was my intention to make the following recommendations:

(1) That title II, Federal Reserve Act, section 41B of the committee print bill, on page 118, be amended in the portion preceding the first colon to read "No member bank shall, directly or indirectly, by any device whatsoever, including absorption of exchange, pay any interest on any deposit which is payable on demand."

(2) That the first sentence of title III, Federal Deposit Insurance Act, section 26 of the committee print bill, on page 163, be amended to read "No insured bank shall, directly or indirectly, by any device whatsoever, including absorption of exchange, pay any interest on any deposit which is payable on demand and for such purpose the Administrator may define the term 'demand deposits' but such exceptions from this prohibition shall be made as are now or may hereafter be prescribed with respect to deposits payable on demand in member banks by the Federal Reserve Act, as amended, or by regulation of the Board of Governors of the Federal Reserve System."

I am not a lawyer and possibly this recommendation will not stand up in the suggested form under lawmaking procedure, but if it could be adopted, it would put member and insured nonmember banks on a uniform basis so far as absorption of exchange is concerned.

Last Monday, Mr. Kenton R. Cravens, chairman of the advisory committee, made recommendation No. 115F for the committee respecting absorption of exchange as an indirect payment of interest. This recommendation removes the possibility of varying interpretations and places both member and insured nonmember banks, as Congress no doubt originally intended, on a uniform basis. I strongly urge you to adopt his recommendation.

Senator ROBERTSON. We will continue these hearings next week and during that period we will hear from the National Savings and Loan League, the United States Chamber of Commerce, the Robert Morris Associates, and we will have a number of individuals.

The following week we will start on the Federal agencies. The Federal agencies, when they testified before us in November, had to qualify their testimony by saying, "It has not been cleared by the Budget Bureau." I instructed them that when they came before us this year we wanted specific language on the changes that they recommend and we want them to say, "It has been cleared by the Budget Bureau."

I have also sent all of the agencies a letter saying that interesting testimony has been given to us not only on what the agencies recommended but some new items, and that I hoped when they testified they would be reasonably familiar with all of the testimony that had preceded that testimony and would give us the benefit of their advice. We wanted their advice not only on those proposals which they had made and which had been considered by our splendid Advisory Committee and incorporated into the tentative bill, but also on these other helpful suggestions that have come to us.

Apparently we cannot conclude these hearings until Monday of the week after that. That would be the 18th of February. I have been informed by the chairman of this committee that there are a number of other pressing matters awaiting committee attention.

The chairman has very kindly and graciously given us priority, right-of-way, but we cannot hold that indefinitely. So, the chairman of the subcommittee is forced to announce that he sees no chance to continue these hearings beyond the scheduled date. All those who have previously asked to be heard will be heard. They have had plenty of time to submit their requests. We cannot continue beyond the 18th of February. However, if anything has been developed here on which any group or any individual feels that we need further enlightenment if it is appropriate, of course, we will consider a memorandum that they may file to be incorporated in the record.

If there are no further witnesses today the committee will stand in recess until 10 a. m. next Monday.

(Whereupon, at 10: 30 a. m., the subcommittee recessed until 10 a. m., Monday, February 4, 1957.)

STUDY OF BANKING LAWS

(Financial Institutions Act of 1957)

MONDAY, FEBRUARY 4, 1957

UNITED STATES SENATE,
COMMITTEE ON BANKING AND CURRENCY,
SUBCOMMITTEE ON BANKING,
Washington, D. C.

The subcommittee met, pursuant to recess, in room 301, Senate Office Building, at 10:05 a. m., Senator A. Willis Robertson (chairman of the subcommittee) presiding.

Present: Senators Robertson, Frear, Bennett, and Bush.

Senator ROBERTSON. The subcommittee will please come to order.

The Chair wishes to announce that the Senate meets at 12 o'clock and we do not have permission to be in session while the Senate is in session, so we will have to adjourn at that time. We have eight witnesses scheduled to be heard, and all of them have equal rights. Some of them have come a long distance.

I just want to say to all of these witnesses that we will be very happy to put in the record everything that you have prepared, but if you could condense your statements so that each witness would not take over 10 or 12 minutes, that would enable all of the witnesses to be heard and not force some of them, perhaps, to come back and impinge upon the schedule, which is a tight one, that we have for tomorrow.

The first witness is Mr. Walter E. Cosgriff, president of the Continental Bank & Trust Co. of Salt Lake City, Utah. We will be glad to hear you, Mr. Cosgriff.

STATEMENT OF WALTER E. COSGRIFF, PRESIDENT, CONTINENTAL BANK & TRUST CO., SALT LAKE CITY, UTAH

Mr. COSGRIFF. My name is Walter E. Cosgriff. I am president of the Continental Bank & Trust Co. of Salt Lake City, Utah. I am also president of the Bank of Las Vegas, Las Vegas, Nev., and chairman of the board of directors of the Colorado Commercial & Savings Bank, Colorado Springs, Colo. I have been a full-time salaried officer of the Continental Bank & Trust Co. for almost 22 years.

In addition, I am an officer, director or majority stockholder in several other banks in the Intermountain country, and during my banking career I have engaged in substantial banking operations all the way from Goodland, Kans., to Long Beach, Calif. My banking connections have included both National and State banks, members and nonmembers of the Federal Reserve System, banks that were members of the Federal Deposit Insurance Corporation and some that were not.

Some of you may recall that I served on the Board of Directors of the late but not lamented Reconstruction Finance Corporation during portions of 1950 and 1951.

Some of you may also have heard that my principal bank, the Continental Bank & Trust Co., is now engaged in an unprecedented contest with the Board of Governors of the Federal Reserve System, seeking to determine whether the Federal Reserve Board has the power to require a State member bank to increase its capital structure to an amount which the Board may consider to be adequate. Later on in my testimony I expect to discuss this question in more detail.

First of all, let me say that I am completely in accord with the basic objectives of this committee in seeking to revise and codify the banking laws of the United States, to bring them up to date, to eliminate obsolete and overlapping provisions and to improve them where improvement is warranted. Certainly I feel no reasonable banker can quarrel with these objectives. There are, nevertheless, certain provisions in the bill, as now proposed, which seem to me are in need of correction and clarification. It is some of these that I wish to discuss this morning.

One of the most time-honored principles of American banking has been that it is in effect a dual system. For about a century, both the National and State Governments have chartered and supervised bank operations. So far as I know, there is no serious quarrel with this dual arrangement. I do not know of any responsible authority who has suggested that State banks be abolished and that control of all banking be taken over by the Federal Government. Nevertheless, State banks which are members of the Federal Reserve System and the Federal Deposit Insurance Corporation are more and more coming under almost exclusive Federal control, leaving little or no authority to the States which created them.

I do not believe it is the intention of Congress that Federal agencies should preempt control of State banks. Some time ago, when certain directors of the Federal Deposit Insurance Corporation came before the Senate Banking and Currency Committee for confirmation of their appointments this question was raised. The directors were requested to write letters which in substance and effect indicated that the State banking authorities had primary responsibility for the supervision of State banks. Assuming then that this action represented the will of the Congress that State banking authorities have basic control over the banks they charter, I believe it can be shown that many provisions of this proposed bill are at cross-purposes with this policy.

Of course, paramount in my mind at this time is my own bank's battle with the Federal Reserve Board over capital adequacy. This battle was started by the Federal Reserve unilaterally without consultation with or participation by the Utah State Banking Commissioner. It is this sort of arbitrary action, without any statutory authority, that is destroying our dual system, and this bill as drafted leaves the situation wide open.

Sections 22 and 23 of title II of the proposed bill are apparently derived from the present section 9 of the Federal Reserve Act, slightly rearranged. With that as a premise, it should be pointed out that there are some loosely worded provisions in the present law which the Board of Governors has seized upon to expand its powers beyond those which Congress intended.

For example, the first paragraph of section 9 of the present Federal Reserve Act (sec. 22 (a) of the proposed bill), relating to admission of State-chartered banks into the Federal Reserve System, provides:

> The Board of Governors of the Federal Reserve System subject to the provisions of this Act and to such conditions as it may prescribe pursuant thereto, may permit the applying bank to become a stockholder of such Federal Reserve Bank.

These limitations on the conditions which the Board may impose were added by the Congress in 1927. These changes in the law were made necessary when a full examination into the activities of the Board indicated that the Board was arrogating to itself, by the imposition of conditions, powers far beyond those intended by Congress.

Senator ROBERTSON. May I interrupt?

Mr. COSGRIFF. Yes, sir.

Senator ROBERTSON. I call your attention to the fact that we did not make any changes in the existing law as quoted. We did not change it. It is the existing law.

Mr. COSGRIFF. That is true, Senator.

Senator ROBERTSON. That is right. We did not go into this overall policy question of the powers of the Federal Reserve Board. That is one of the things to be studied by the Monetary Commission, if, as, and when it is established. We are trying to do mostly a technical job, that is, to eliminate obsolete sections and codify all of the provisions, and in some instances streamline them where there can be a reasonable area of agreement.

We cannot expect everybody to agree with everything in a 250-page bill, but we did not go into that point you mentioned right there, and certainly we have not done anything in this bill that in any way impinges upon the future of a dual banking system, with the Federal banks on one side and the State banks on the other. Neither have we challenged or tried to nullify the decisions of the Supreme Court, which have held that State member banks of the Federal Reserve System are subject to Federal law, and all insured banks are subject to Federal law, because the Federal Government has to guarantee up to $10,000. That is approximately one-half of the assets of over $200 billion, and that is quite a little undertaking on the part of the Federal Government.

It has been brought out in the testimony here that if we had just a little touch of deflation—not a real depression—nobody could anticipate what the demands on the Federal Deposit Insurance Corporation's reserve fund would be. We are going to ask them to make a study. They want us to cut down on the assessment and charge the banks less, but we do not know the facts. It has been pointed out if we had a depression no one could tell what the liability is or could be, because there is no clear conception as to what the Government has set out to do here. Would it try to take care of everybody in the event of atomic war, for example? We do not know. We are leaving those larger problems.

That is what you are discussing here when you say the Federal Reserve Board has too much power and as a State member bank it has moved in on you and you do not like it and want something done about it.

With all due deference, it is a little beyond the province of this study.

Mr. COSGRIFF. Senator, I might suggest if you pass the thing in this way it has been explained to me you will automatically resolve this question in this way.

Senator ROBERTSON. Again I repeat, we have not confirmed or denied anything when we merely put into the code a repetition of existing law. We are just carrying it forward.

Mr. COSGRIFF. Senator, I am told if you put in a repetition of existing law and there is an administrative interpretation of that law, then by repassing the legislation in the new bill you automatically pass the administrative interpretation.

Senator ROBERTSON. That is an assumption that the Chair does not agree with. Those in favor of it could argue it. Those opposed to it could argue the contrary. The Chair does not take any position. He does not agree with you.

Mr. COSGRIFF. So that would not be your intention?

Senator ROBERTSON. It would not be the intention of the Chair. The Chair does not know anything about the interpretation that you are talking about, so how could he confirm it?

You may proceed.

Mr. COSGRIFF. Senator George Wharton Pepper, of Pennsylvania, said of the situation in 1925:

> There was no intent of Congress when the Federal Reserve Act was passed to create in the Federal Reserve Board a body to prescribe any kind of conditions it pleased as conditions precedent to admissibility to the Federal Reserve System, but rather to confer upon the Federal Reserve Board authority to make regulations, pursuant to the act, fixing the terms upon which banks might become members of the Federal Reserve System.

The next year Senator Carter Glass, the father of the Federal Reserve Act, stated in a hearing before this committee that the Federal Reserve Board "has usurped the legislative functions of Congress."

As I have stated, the views of these Senators prevailed and legislation was adopted in 1927 restricting the conditions to be imposed by the Board to those expressly authorized by the Federal Reserve Act.

But the aggressiveness of the Board has not changed in the 30 years since Congress last spoke, and that limitation has not deterred the Board from trying to keep its omnipotence in pace with its omniscience. Without any statutory authority at all, the Board required a small California bank to agree that it would withdraw from membership in the Federal Reserve System if any interest in the bank, no matter how small nor how obtained, was acquired by certain other banking interests. The bank took the matter to court and won a sufficient victory so that the Board never attempted to enforce the provision on which it had previously insisted. Congress has resolved the fundamental issue in that case by enacting the Bank Holding Company Act of 1956.

In another field, the Board has imposed conditions of membership relating to capital adequacy without the benefit of a grant of such power by the Congress. The Board claims as its authority the very section of the statute under discussion, which was amended to limit conditions of membership. Although the Board has been imposing this condition since the 1930's, no bank has called its hand until this year when the Board demanded of my bank that it increase its capital by $1½ million. Later, after we resisted, it raised the ante to 2.9 million, almost 100 percent of our present capital account. We are now faced with an administrative hearing brought by the Board as judge and prosecutor to determine how much it is going to insist we increase our capital or, on failure to do so, be expelled from the Federal Reserve System.

It is a sad commentary on the courage or lack of it of some members of the banking profession in that we are the first bank to actively resist such demands by the Board, although students on the subject have questioned its authority to make or enforce such demands.

My point is this: The present act does not authorize the Board to impose, as a condition of continued membership, that a State member bank increase its capital at the demand of the Board. Nevertheless, the Board asserts that it does have such power. If requiring a State member bank to increase its capital to avoid what the Board calls "capital inadequacy" is a legitimate function of the Board, Congress should say so, with appropriate standards to guide both banks and the Board, and not leave it to the unbridled and arbitrary discretion of the Board.

It is questionable, however, whether this should be a legitimate function of the Board. There are three classes of banks subject to Federal control in some degree—national banks under the supervision of the Comptroller of the Currency, nonmember insured banks under the Federal Deposit Insurance Corporation, and State member banks under the Federal Reserve. Neither the Comptroller nor the Federal Deposit Insurance Corporation has or asserts the power to make a bank under its supervision increase its capital. They both have, as does the Board of Governors of the Federal Reserve System, a substantial arsenal of powers to insure the soundness of banks under their control. If capital inadequacy is the result of unsafe and unsound practices or management policies, it is far better to cure the cause than try to pour in more capital which, in turn, will become "inadequate" if the causes continue.

Perhaps the issue can better be understood by examining the function of bank capital and what is meant by the supervisory authorities when they speak of inadequate capital.

Capital in a bank performs a function not much different from that in most businesses. As do most businesses today, a bank operates on borrowed money. In the case of industry, the borrowings are from banks and other sources of accumulated money, such as insurance companies, or borrowings are in the form of the sale of the company's bonds or other securities. In the case of a bank, its borrowings are in the form of its deposits. Just as in industry, the bank invests its borrowings in income-producing assets. In the case of a bank, it is in the form of loans to industry, farmers, small businesses, and to ordinary consumers.

With respect to its deposits or borrowings, a bank's capital serves as a cushion to insure the ability of the bank to meet its deposit liabilities if the reserves that a bank is required to have by State and Federal regulations are exhausted. As no two banks are alike, it is difficult to prescribe any general rule as to how large this capital cushion should be. It must depend primarily on the nature of the bank's assets and the skill and experience of its management. But my friends at the Federal Reserve have found a searching appraisal of both physical and human assets too difficult. They resort to such formulas as arithmetical ratios of loans and other assets to capital and then compare individual bank ratios with national averages. Since the Federal Reserve Act gives the Board no power to inquire into such matters, let alone setting standards to guide it, the Board sets its own criteria. In so doing it has not only failed to see that national averages and arbitrary ratios are meaningless when applied to individual banks, but has overlooked the possibility that capital plays any part in the operation of a bank other than as an ultimate protection to the depositors.

It cannot be denied that depositors are entitled to protection—to protection against all losses that might reasonably be anticipated in the light of the bank's assets and its management skill and experience. The responsibility of providing such protection and insuring its adequacy rests even more on the bank's officers and directors than it does on bank examiners and other regulatory authorities. But the officers and directors of a bank have other responsibilities as well. They have to look to the welfare of the stockholders whose investment forms the capital; they must be sure that the bank is able to provide adequate service and facilities for its borrowers; and they must see that the employees are honest and efficient and are fairly compensated.

If overemphasis is put on the amount of capital, if the determination of the amount of capital required for a sound banking operation is looked at with the blinders of only one viewpoint, a proper balance will not be achieved.

In this connection it might be mentioned that the troubles with some Illinois banks and bank failures in the country in recent years were due primarily to embezzlements, not to bad loans. A prime cause of embezzlement is failure to compensate employees adequately. It also should be recognized that bad loans themselves are ordinarily due to lack of qualified personnel. Unless a banking career can be made attractive financially, such qualified personnel cannot be obtained.

Another aspect of the imbalance is the return on investment. If there is an overemphasis on the amount of capital, the bank would not be able to earn a reasonable return on the shareholders' investment, leaving them the alternatives of liquidating the bank or selling out to a larger organization. This problem is well pointed out by Prof. Roland Robinson, formerly of Northwestern University, and now with the Federal Reserve System. In his book on the management of bank funds, he gives the example of a bank with a 5-percent ratio of capital to assets. If its capital were increased to a national average of, say, 6.6 percent, this would be equal to a 32-percent increase in the capital account, only a 1.6-percent increase in the total assets, and would dilute earnings almost one-fourth.

With respect to the problem of dealing with capital adequacy, I should like in summary to make these points:

1. The primary responsibility for capital adequacy should be placed on the officers and directors of the bank. They are the ones most familiar with the assets and the requirements of the bank. They are the ones who most realistically can achieve the balance needed between protection to depositors and the rights of the owner-stockholders.

2. If it is desired to give some power over capital adequacy to Federal regulatory authorities, these requirements should be met:

(*a*) Such a grant of power should be express, with adequate criteria or standards to guide not only the regulatory authorities but also the bankers in the operation of their own institutions. These standards should include (1) an appraisal of all the bank's assets at their true market value, whether carried on the books or not; (2) the bank's past loan loss experience and its reserves for future losses; (3) the experience and competence of its management; (4) its past and prospective earnings record; (5) the needs of the area served; and (6) the nature and amount of its deposits and other liabilities. Without such standards, each bank is subject to the unbridled whims and theories of the regulatory authorities.

(*b*) Any additional capital requirements should be limited so as to preserve a proper balance among the interests of depositors, stockholder-owners, borrowers, and employees.

(*c*) Since we are talking about State banks which are members of the Federal Reserve System, the primary responsibility for action with respect to capital adequacy should be placed upon the State authorities, who are better acquainted with the needs of the area served and are in a better position to appraise the individual bank's assets and requirements. It is my belief the Federal Reserve Board should not be able to proceed without the consent or participation of the State authority concerned.

(*d*) Provision should be made for a fair hearing, either public or private, at the bank's request, and for a court review to insure against arbitrary administrative proceedings.

Another matter to which I should like to direct the attention of the committee is the matter of payment of alleged "unearned" dividends.

The matter of dividend payments by banks has long been a subject of controversy. The position of most of the supervisory authorities seems to be that the stockholders of banks are not entitled to any dividends and should be willing to forego them merely for the "honor" of owning bank stock. In the report of your Advisory Committee submitted in December 1956, the following sentence appears on page 4:

> Stockholders in banks have had to be content with a smaller dividend return on their invested capital than have the stockholders of other major segments of American business and industry.

In spite of the committee's recognition of this fact, the proposed bill does nothing to alleviate the situation. In fact, the bill would make the situation worse by maintaining and fostering the overcapitalization of banks. By an overcapitalized bank I mean one in which the net investment of the stockholders has risen to such a point in relation to the bank's earning assets that it is no longer possible to earn a fair return on that investment. When this situation exists, sooner or later the stockholders are strongly tempted to liquidate the bank and invest their money in some other business where the returns are greater. Stockholders who want to abandon banking can, as recent events indicate, do so in many other forms. They can merge with other banks, or sell to a branch banking organization which then liquidates the independent bank and puts a branch of the larger organization in its place, or they can sell to a bank holding company. Overcapitalized banks are the natural prey of branch banking organizations and bank holding companies.

Any effort to limit dividends along the lines of the provisions of this bill will greatly accentuate the trend already too prevalent of independent bankers to sell their institutions to branch banks or holding companies. If any limitation on the payments of dividends is desirable, other than those that exist at the present time, I respectfully suggest the possibility of using some formula which ties dividends to the same standards as I have suggested for determining capital adequacy. Then those banks which saved their money in prior years or who, for some other reason, accumulated capital funds far above their present needs would not be penalized.

I am now referring to unearned dividends under section 23 (a) of title II on page 91, and sections 17 and 22 of title I on pages 7 and 11 of the bill.

I would like to point out certain ambiguities remain. That section incorporates without change the provision of the present law that State member banks shall be required to comply with the provisions of law imposed on national banks which relate to the withdrawal or impairment of their capital stock and which relate to the payment of unearned dividends. The provision of law imposed on national banks on such subjects are sections 17 and 22 of title I of the proposed bill.

Section 17 provides that an association whose stock shall become impaired shall within 3 months after receiving notice thereof from the Comptroller of the Currency make up the deficiency by assessment on its stockholders. This reference with respect to State banks is, of course, nonsense. It certainly is not intended that the Comptroller have any responsibility or authority over State banks. No reasonable person would question the obligation or duty of a supervisory authority to correct impairment, but I suggest that the bill be drawn to place the responsibility over State member banks where it belongs, that is, with the State supervisory authorities in conjunction with the Board of Governors.

Similar inconsistency is contained in the reference to State member banks with respect to unearned dividends. Section 23 (a) of title II and section 22 of title I give control over such dividends to the Comptroller. It is suggested that any reference to payment of unearned dividends by State member banks be expressly dealt with under the authority of the State supervisory authority and the Federal Reserve Board and not by reference to the Comptroller.

Senator ROBERTSON. I believe we merely continue existing law.

Mr. COSGRIFF. Not in this case, Senator.

Senator ROBERTSON. Oh, yes; we did. A good many of the bankers are finding out for the first time what the laws are that they have been operating under. We have had one letter, as I pointed out before, from a savings and loan association, complaining that small States had no chance to elect directors of the board, and he thought the law was very wrong that I put in there. I merely call attention to the fact that we are only continuing the law we had all along. This provision you say is ambiguous is the present law, and we just carried it forward into this bill.

However, the Chair will be glad to instruct the staff to make a special study of your suggestion that it is ambiguous and that is should be changed along the lines you are now suggesting. You may proceed.

Mr. COSGRIFF. When I started reading this, Senator, I was dumfounded at it too, because the thing seems to me to be very clear that it refers right back to the Comptroller. At my own expense I had two of what I considered to be very good lawyers working on the question independently, and they came right back to this same answer.

Senator ROBERTSON. Well, some very good lawyers are going to learn something they did not know before.

Mr. COSGRIFF. I think that is possibly so, but certainly it would be very helpful to clear that situation up if that is not what is intended.

Senator ROBERTSON. I think you are not arguing the language, but you are arguing the interpretation of the language.

Mr. COSGRIFF. I was surprised, and I would think anybody else would be too, to look at this and see how strong and clear it seems to be. Yet, of course, we know that so far the Comptroller has not done that.

Senator ROBERTSON. You do not agree with the interpretation.

Senator BENNETT. When was this law Mr. Cosgriff is discussing put on the statute book?

Mr. ROGERS. I would have to check it. It is part of the old revised statutes, so it goes back before that.

Senator ROBERTSON. Before 1933?

You may proceed.

Mr. COSGRIFF. Another matter to which I should like to call the committee's attention is sections 23 (b) of title I, 23 (i) of title II, and 27 of title III.

These sections provide, among other things, that the president or cashier shall notify the Comptroller, the Federal Reserve Board, or the Federal Deposit Insurance Corporation, as the case may be, immediately of any single transaction involving the purchase or sale of 10 percent or more of the outstanding shares of such bank.

Senator ROBERTSON. That is a new provision put in there because there was some finagling done in stock handlings at several Chicago banks and we wanted to safeguard against that situation in the future.

Mr. COSGRIFF. As far as it goes at the present time, this obligation would not seem to be objectionable since, obviously, none of the three authorities has any power to prevent such sale or transfer. I suggest, however, that these provisions are merely an entering wedge or "foot in the door" operation to eventually bring all pledges and sales of bank stock under jurisdiction of the Federal agencies involved. Followed to its logical conclusion, it would mean that no one in the United States could buy or sell any considerable proportion of stock in a bank without the approval of the Federal authorities. Needless to say, such a law would give the Federal authorities almost unlimited power over who could participate in the banking business, would leave the State governments without any control in the matter, and would be an unlimited weapon for enforcing the will of the Federal supervisory authorities on the management or stockholders of any bank.

Senator ROBERTSON. I may interrupt to say that the chairman would be so opposed to any such action that he would take that as following that to its illogical conclusion. You may call it a logical conclusion, but from the chairman's standpoint he would call it following this proposal to an illogical conclusion.

Mr. COSGRIEF. I might say I am very happy to bring that out, because I am just afraid if it goes through in this form 5 years from now

I am going to be back here fighting against the provision we are talking about.

Senator ROBERTSON. If this chairman is here 5 years from now you will not have to be fighting him.

Mr. COSGRIFF. I certainly do not think this is the intention of the Congress, and I feel then that these sections are, at best, useless and, at worst, a wedge to bring about such a situation. I do not feel that the supervisory authorities or anyone else can make out a case for these sections on any other basis. I once again submit that in this matter, as in many others, the States will be completely bypassed.

In each section of the bill dealing with the three Federal supervisory agencies are provisions with respect to branches of banks under their jurisdiction. On their home grounds each of these various classes of banks is in competition with the other. It would seem that, to preserve the dual system of banking to which I have referred, the provisions of the act with respect to the right to establish or acquire branches should be uniform. The present bill would seem to my mind to grant discriminatory privileges to national banks over State banks which are either members of the Federal Reserve System or whose deposits are insured by the Federal Deposit Insurance Corporation. I suggest that these provisions as to branches be looked at as a whole in order to prevent discrimination.

In conclusion, let me state that I have assumed that in rewriting existing banking legislation and adding new provisions, it is not the intent of Congress to destroy the rights of States to supervise the banks which they charter. Neither have I assumed that it is the purpose of Congress to create conditions which will drive the independent banker out of business, force him to sell or liquidate his institution, or turn over control to holding companies or to large chain banking organizations. I am sure that every one of you is familiar with the tremendous wave of bank sales, liquidations, mergers, and consolidations which has occurred during recent years and which led Congress to enact the Bank Holding Company Act of 1956. That act may, of course, slow down the trend but certainly will not of itself halt it altogether. If any vestige of the independent banking system is to be preserved, it can only be done by creating a climate which makes independent banking more attractive. In other words, by forcing the independent banker to put up more capital, restricting his dividends, imposing more Federal regulation, etc., you are encouraging him to go out of business and invest his time and money in something else. No case on the basis of the failure or trouble with banks generally can be made which justifies, in my opinion, increasing Federal regulation at this time. Efforts to prevent bank mergers, liquidations, and consolidations by passing laws against them, in my opinion, treats the symptom rather than the disease. Only by making independent banking more attractive can independent banks be preserved.

I wish to thank the committee for listening to me this morning.

Senator ROBERTSON. Are there any further questions?

Senator BENNETT. I think the chairman has brought out the questions involved. Thank you.

Senator ROBERTSON. Thank you, Senator, and we thank you, Mr. Cosgriff.

The next witness is the National Savings & Loan League, Mr. James E. Bent of Hartford, Conn., and W. Franklin Morrison, Washington, D. C.

STATEMENTS OF JAMES E. BENT, CHAIRMAN, FEDERAL HOME LOAN BANK SYSTEM COMMITTEE; ACCOMPANIED BY W. FRANKLIN MORRISON, CHAIRMAN, FEDERAL LEGISLATION COMMITTEE; AND HAROLD P. BRAMAN, EXECUTIVE MANAGER, NATIONAL SAVINGS & LOAN LEAGUE

Mr. BENT. It is a pleasure to be here, Senator.

Senator ROBERTSON. Gentlemen, do you have a consolidated statement?

Mr. BENT. Yes, I do, Senator, and rather than speak myself, in the interests of brevity and in the interests of time I have put this in writing in order to make it as brief as possible.

Senator ROBERTSON. It will be acceptable to the committee and you may put in the record what you see fit. You may proceed with your statement.

Mr. BENT. My name is James E. Bent. I am president and managing officer of the Hartford Federal Savings & Loan Association, Hartford, Conn. I might also add that I am a member of the Federal Savings and Loan Advisory Council created pursuant to section 8 (a) of the Federal Home Loan Bank Act, an elected director of the Federal Home Loan Bank of Boston, and chairman of the National Savings & Loan League's Federal Home Loan Bank System committee, in which capacity I am appearing today. I have no other banking connections.

I have with me Mr. Frank Morrison, executive manager of the First Federal Savings & Loan Association here in Washington and chairman of the Federal legislation committee of the National Savings & Loan League. I also have with me Mr. Harold P. Braman, the league's executive manager.

Needless to say, Mr. Chairman and members of the committee, I am most appreciative of the opportunity to appear once again before the Senate Banking and Currency Committee. Over the years we have felt that this committee always considers and carefully weighs the arguments we present against its objective of legislating in the public interest. We could not ask for more.

By and large, we feel that this bill is a good one. Its basic objective, as we understand, is to clarify and bring together for the first time all the laws relating to financial institutions. With this objective we heartily agree. This type of codification is of great benefit to lawyers and laymen alike.

Federal Savings and Loan Branches (Title V, Sec. 6, p. 211)

Section 6 of the proposed Federal Savings and Loan Association Act restricts the establishment of branches by Federal savings and loan associations. Unlike other amendments contained in this codification, this section embodies substantive changes in basic law of very great significance to our business.

This question is not new to this committee. Hearings were held in the 82d, 83d, and 84th Congresses. On each of these occasions the banking supervisors and spokesmen for certain commercial banking interests and mutual savings banks have, in our judgment, skirted and camouflaged the true motives behind the position which they take. What they are really after is elimination of competition offered by savings and loan associations. Spokesmen for the American Bankers Association have repeatedly stated that their No. 1 competitive problem is the savings and loan associations. That may be the case, but it is a problem the American people cannot do without.

Non-savings-and-loan members of the financial fraternity say they want equality of competition between State and federally chartered savings and loan associations. If we may translate this, what they actually have in mind is the procurement of a competitive advantage for themselves.

The same people also plead the cause of States' right—a subject which offers an emotional appeal for the enactment of this type of legislation.

This section should not be considered by the Congress as affecting States rights. The "rights" of the Federal and State Governments are derived solely from the Constitution of the United States. The courts have long ago determined, in the national banking cases, and later in cases affecting Federal savings and loan associations, that the Federal Government has the right to charter and regulate financial institutions in the national interest and to grant the branches and other facilities they need to serve the public. The States have similar complete powers within their own jurisdiction. It is settled national policy that both the Federal Government and the States may create and maintain systems of financial institutions, and they shall operate side by side in competition in the public interest. There is no legal or constitutional issue with respect to States rights involved in this section of the bill.

This States rights issue was concisely analyzed and discussed by a former member of this committee on June 23, 1955. If the Chair permits, I would like to insert in the record at this point that portion of his comments relating to the States rights issue. It will run only about two pages.

Senator ROBERTSON. Without objection, you may insert that, although it is not the general practice of the committee to insert in the current record testimony that has been previously given before some other congressional committee, because that is a duplication of printing.

Mr. BENT. It is merely in the light of explaining the statement, Senator.

Senator ROBERTSON. It is a brief statement, so we will let it go, but we do not pick up from 1925 or 1933 some voluminous testimony and reprint it here.

(The document referred to follows:)

STATES RIGHTS ARGUMENT REFUTED BY SENATOR MORSE IN CONGRESSIONAL RECORD, 84TH CONGRESS, 1ST SESSION, THURSDAY, JUNE 23, 1955

Mr. MORSE * * *.

*   *   *   *   *   *   *

I respectfully submit that in the position taken by the majority of the committee there is an unwarranted basic assumption that must be dealt with before we can discuss the merits of S. 972 in the form in which it came from the committee. My reference is to the assumption that the doctrine of States rights makes it imperative that we pass the bill as recommended by the majority of the committee.

I cannot imagine a more loose and inaccurate application of the States rights doctrine. I digress for a moment to say that the inaccurate application of broad legal concepts is never justified, and can be very dangerous. It is dangerous for many reasons, but mainly because it establishes a precedent and the possibility of compounded error.

I believe my observation to be particularly true in the case of the doctrine of States rights. The doctrine has been used increasingly of late to thwart legitimate policy goals in instances wherein it had no application. When I say that I speak advisedly and with the thought in mind that I have often defended States rights on the floor of the Senate, and I will do so again when the occasion for me to do so arises on sound legal questions.

I wish to stress that there is no room ever for an argument about States rights in connection with legislation unless a constitutional issue is involved. Yet in debate on the floor of the Senate we hear, I do not know how many times a month, that someone is opposed to proposed legislation because he believes it violates the principle of States rights.

It has become an emotional sanction in political debate in America. No one can possibly argue accurately on the doctrine of States rights unless one argues on constitutional grounds. The political argument advanced by some persons that they do not want the Federal Government to do something as a matter of Federal legislative policy is one thing, and let us face it on the question of whether it should be established as public policy by way of Federal legislation; but let us not continue to muddy the waters of debate whenever it is proposed that the Federal Government exercise its right by suggesting the emotional sanction and saying it interferes with States rights. That is exactly what the majority of the committee did in its report on the pending bill.

Not one word is found in the majority report dealing with constitutional grounds, because the majority of the committee could not make such an argument on constitutional grounds.

Therefore, I repeat that the only time the States rights argument has any justifiable defense on the floor of the Senate is when someone wants to argue that a proposal by way of Federal legislation is unconstitutional because of interference with States rights.

If States rights were really at issue here, and if this were truly a case in which the Federal Government was transgressing in an area in which it had no jurisdiction, I would suggest that the majority should have reported a bill completely removing the Federal Government from this field on the ground that Federal operations were unconstitutional.

That is the only ground on which the majority could advance a legal argument which would be sound, if it could back it up with constitutional doctrine. But the majority did not do that in its report. Why? Because there is no question at all about the constitutionality of legislation which involves the Federal Government in this field. Therefore, in this instance there is no basis for the argument about States rights.

The majority knows that this program is not unconstitutional. It knows that Congress has long considered providing adequate thrift and home-financing facilities as a proper function of the Federal Government. I cite the Federal Housing Administration, the Home Owners' Loan Corporation, the insurance of bank deposits, and I could add many other examples to the list, all of which have been sustained by the courts of the land as involving a constitutional exercise of power by the Federal Government.

What the majority meant to say, but did not, in its report, was that we have a political policy question here.

I am willing to meet them on the political policy question, Mr. President, but I do not like to have them use as a political sanction, as an emotional appeal, the States rights doctrine when no legal question of States rights can possibly be involved in the legislation.

The policy question is this: Should the Federal Government exercise its constitutional powers to encourage savings and thrift or should it give deference to States policies in this area. I cannot overstress the fact that Federal operations, simply because they may affect affairs within a State, are not unconstitutional and are not interfering with States rights.

That is the law handed down by the Supreme Court time and time again.

When two policies are in conflict, the issue then is which will we choose. The answer must be that we will choose the one best supported by the facts of the case we are trying to decide.

Branch banking rests on this commonsense observation.

I happen to be one, Mr. President, who believes it is good public policy to encourage savings. In fact, I would that the American people were saving more and more rather than what I am afraid is true, that the little people are saving less and less.

There are many reasons why the little people are saving less and less, but I think branch savings facilities close to their home communities will at least help to interest them in saving more.

The hearings and the success history of the savings and loan associations also demonstrate that the associations are a vital force in our society. The facts therefore dictate that our policy should be one favoring branch privileges for Federal savings and loan associations.

Now, Mr. President, a word about restricting competition.

Another policy consideration which this legislation raises is whether or not the Congress should enact legislation which will restrict competition. Many of those who testfied in favor of the bill were in large part representatives of commercial institutions. A wire that I received from one of my constituents hit this matter of competition squarely on the head when he wrote:

"Howard T. Hardie, of Pennsylvania, vice president of the Bankers Association, recently states: "Savings and loan associations are the No. 1 problem of the ABA."

What we have to face is that commercial banks are seeking to gain ascendancy in this field by congressional legislation. Some of them have found the competition too stiff.

When the majority states that the Federal Government is sanctioning unfair competition by allowing branch operations to Federal savings and loan associations it only speaks of half the case. All through its report the majority has attempted to put State savings and loan associations and State mutual banks up as the standard against which we must judge Federal savings and loan associations. They have refused to bring in the other category of savings institutions and use them as the standard. I refer, of course, to the fact that many States which do not allow branch privileges to savings and loan associations and mutual banks to allow these privileges to commercial banks. One of the very reasons that we have Federal savings and loan association legislation is that commercial banking houses used their political influence to stop the development of savings and loan associations and mutual banking on the State level. In those instances where they could not stop this development they struck hard at a very important aspect of it, and that is the privilege to establish branches.

The majority of the committee may well say that it does not intend to "unduly restrict or inhibit the growth and development of the splendid Federal-chartered thrift gathering institutions." I say that this is not a realistic appraisal of the situation and the majority knows that when it points ou, as I have already quoted, that there are certainly occasions where branch privileges are very important. The majority adds another line of reasoning to its defense of this bill when they say:

"The institutions are mutual in nature and owned by the persons that use their facilities. The institutions should not lose their local nature, but should be encouraged to make every effort to retain their local ownership, local management, and participation."

My answer to this argument implying possible monoply is, quoting the minority report:

"Federal savings and loan associations are limited in their lending to a radius of 50 miles from their home office. They cannot become a giant monopoly or dominate the financial field in any community or area.

They are mutuals owned by the persons who use their facilities (as the majority has said) and when a mutual institution takes in branches the investors in the branches are equal owners along with the regional group."

In fact, rather than permitting monoply, the branching operations of Federal Savings and Loan Associations widens the area of service and spreads out the power.

Again, the facts dictate that we should do what we can to protect the right of the Federal home loan and building associations to engage in branching operations.

I close, Mr. President, by making clear that my vote for the amendment and my vote for the bill as amended on the floor of the Senate, whereas I voted against the bill in committee, is because I think the amendment establishes a sound public policy. The amendment completely eliminates the States' rights argument.

The amendment cannot be reconciled with the States' rights argument on the basis of which the majority, for the most part, premised its case.

I am delighted that the Senator from Illinois [Mr. DOUGLAS] was so successful in his parliamentary persuasion in a series of conferences off the floor of the Senate in getting the leadership of the majority of the committee to go along with an amendment, the principle of which will constitute the main purpose of the bill.

I congratulate the Senate from Illinois, and I think we have made some substantial progress in the Senate in protecting small investors in what I think is their clear right to have branch privileges accorded to our building and loan associations.

Mr. BENT. I do hope this committee will have an opportunity to examine this statement by Senator Morse prior to reporting this bill.

The third argument frequently advanced as justification for legislation to restrict branch offices is related to the prevention of monopoly or the prevention of the concentration of banking power. Measured by bank standards our Federal savings and loan associations are small business, but mighty in their service to the public. The savings and loan business is one of the few major industries or businesses in the country where no one unit represents as much as 1 percent of the total business. For comparison, the 10 largest commercial banks have approximately 20 percent of all commercial bank assets and the 10 largest savings banks have approximately 24 percent of all savings bank assets in the country.

I would like to call attention to the fact that the Savings & Loan Association as of December 31, 1956, had 393 branches, while the Bank of America alone opened in January its 600th branch in the State of California.

It is our understanding that this committee and this Congress feels an urgent necessity to do something about small business and about housing. I am sure that this committee agrees with the frequently advanced proposition that if ever there was a time when we need to save, it is today—particularly where such savings are channeled into the housing market.

This legislation, unwittingly perhaps, strikes a major blow at all these objectives.

About all we can do within our limited powers is to gather savings and invest them in the financing of the American home. These functions are absolutely essential to the national welfare. Unlike other institutions with funds to invest, we do not follow the money market around. If we have money to invest, we put it in homes regardless of how attractive other investments may be. This policy has resulted in our being the chief source of home mortgage funds.

Each and every individual is constantly confronted with the temptation to spend rather than save. Access to convenient facilities, with constant urging to use them, are important factors in determining his decision to save. No financial institution wants branches just for the fun of having them. They are opened only because the public requires such services. Savings and loan associations seek branches, when deemed necessary, only for the purpose of extending convenient facilities to families who wish to save and finance homes. It is in the national interest that the maximum amount of private savings be gathered to provide homes. No restrictive or discriminatory legislation should be thrown in the way of the Federal savings and loan associations in their efforts to expand savings and home ownership.

The great rank and file of savings and loan members are working people. The average savings account is small. The majority of members who come to our offices are women. It is difficult for them to leave their homes in the residential suburbs to conduct these small transactions downtown. Such trips involve considerable time and expense, and no small degree of risk in fighting their way through city traffic and parking. If they cannot conveniently reach us, then our associations must carry our services to them in the outlying shopping areas, just as the banks, merchants, post offices, doctors, and other business concerns are doing. Will anyone claim it is contrary to the national or State interest for us to do that?

Let me emphasize to this committee that we do not come here and suggest a hands-off policy with respect to the authority of the Federal Home Loan Bank Board to permit Federal associations to establish branches.

Senator ROBERTSON. We are glad to understand you do not, because that is what you have always favored.

Mr. BENT. Thank you.

Senator ROBERTSON. Naturally you do not come here to criticize what you have always advocated. You want them to be free.

Mr. BENT. That is right.

Senator ROBERTSON. As I understand your testimony, you give high praise to this bill, except where it affects you, and you want all of that to be taken out and be left just as you are. Is that correct? Is that your position?

Mr. BENT. We oppose the branch provision.

Senator ROBERTSON. You do not want any restriction and you claim that all of this complaint of the commercial banks that you get a better rate and you are competing for savings because you can pay a higher rate of interest, and you are not under the same restrictions that they are and that they are suffering from this serious competition, is just a lot of moonshine and imagination. You say under those circumstances no restrictions whatever should be placed upon you either with branch banking or any other activities, unless the Federal Home Loan Bank Board, which is made up of directors of your own organizations, is it not——

Mr. BENT. The Federal Home Loan Bank Board is the one that controls the branches.

Senator ROBERTSON. That is right. Unless they should set up some limitation on you. That is your position. You just want to be let alone.

Mr. BENT. Sir, the Board does establish very rigid rules.

Senator ROBERTSON. Let me ask you this question: The Chair has been trying to learn a little something of this disagreement. He is just an average layman. It has become quite noticeable in recent weeks that there is a disagreement between the commercial banks and your organization on the subject of competition. If a man puts his savings in one of your associations, is he a depositor or is he a shareholder?

Mr. BENT. He is a shareholder.

Senator ROBERTSON. He is a shareholder. He is not a depositor?

Mr. BENT. That is right.

Senator ROBERTSON. As a shareholder then he cannot get his money out unless you agree to let him? Is that right?

Mr. BENT. That is right.

Senator ROBERTSON. Whereas, if he deposits in a checking account bank he can get it out at any time. If he deposits in a savings account he can get it out according to the regulations on notice of 30, 60 or 90 days, or whatever the regulation is on a savings account; but at that time he gets paid. But with you he cannot get his money until you say, "We will let you have it."

Mr. BENT. We have to establish facilities to give him the money. There are regulatory controls for shareholders.

Senator ROBERTSON. I am glad to get that cleared up for the record.

Mr. BENT. What we are trying to point out is, there are competitive factors.

Senator ROBERTSON. I knew you were competent and could give me the correct answer. I thought that was the answer. Of course, some of the banks claim that it has been represented by some of your associations, and I do not know this, that you can put money in any time you want to and get it out any time you want to, and in the meantime, "We will pay you more than the banks will." But you do not claim that?

Mr. BENT. We do not, sir. I know of no savings and loan association that represents itself to be a demand institution. The practice has been they have been able to withdraw funds from savings and loan associations at will because of the practice and the ability of the institutions to maintain a liquidity of position in order for their members to be able to do so; but we have never claimed to be commercial banks or demand deposit institutions. We want to be known as savings and loan associations.

Senator ROBERTSON. We have some very able men representing your viewpoint on the advisory committee. I was very much pleased that a compromise could be reached between those representatives and the representatives of the commercial banks on a little minor change—although you say it is a major one, but the Chair thinks it is only a minor change—and all it does is say you have to be under the same law that national banks and State banks are with reference to branches unless you can get the legislature to apply some special law for your benefit on branches. But you do not want that.

The Chair though we had reached a very pleasing compromise which he thought your association would endorse, but he understands you are here opposing it.

Mr. BENT. Thank you, Senator. I wish to make this statement with respect to your committee: I think, and I feel personally that the service rendered to the banking fraternity and the savings and loan industry in particular by your advisory committee was excellent, and they were very effective in their findings. Our criticism is not directed to that committee a all. I think it was fine, but we do have certain factors, as you understand, in the field, and we are objecting strenuously only to the branch section.

Senator BENNETT. Were members of your National Savings and Loan League represented on the advisory committee?

Mr. BENT. No, they were not.

Mr. MORRISON. Yes. I was on it.

Mr. BENT. I am sorry. Mr. Morrison was on that committee. We did have two savings and loan members on it. Mr. Morrison was our representative.

Mr. ROGERS. The Advisory Committee recommended just that there be legislation on the subject. They did not go into the details of what the legislation should be.

Senator ROBERTSON. The Chair also points out Mr. Ben Wooten was deliberately put there at the request of his Arkansas friends, because of his previous connection with this type of legislation and his current interest in it, both as a commercial and as a savings and loan banker today in Texas.

Mr. BENT. Mr. Wooten has a very keen interest in savings and loan.

Senator ROBERTSON. And he gave your viewpoint adequate representation.

You may proceed.

Mr. BENT. Thank you, sir.

The branching authority of institutions chartered by the Federal Government under acts passed by Congress should be a subject of continuing interest to this committee. We do respectfully—and I might say urgently and strongly—request that you do not abdicate this prerogative by turning it over to 48 different jurisdictions. Our system was established because experience demonstrated that the provision for a sound system for thrift and home financing institutions could not be left entirely to the States.

It would be strange logic, indeed, for this committee, legislating in the public interest, to delegate what we assert is a legitimate and proper and necessary Federal function to the myriad patterns of State control, when the needs of the people are the same in all the States. Such a chaotic plan discourages thrift when and where most needed and will certainly reduce home financing capital of the Nation at a time when it is needed most.

Senator BENNETT. Are you proposing then that the States' rights to charter savings and loan associations should be taken away from them under this legislation?

Mr. BENT. No, sir. We propose just the opposite. We do want, however, to eliminate the States from interfering with the establishment of the branching facilities of the Federal savings and loan associations. Not State-chartered. They may do as they please there.

Senator BENNETT. The language you just read is a little strong. You say:

> It would be strange logic, indeed, for this committee, legislating in the public interest, to delegate what we assert is a legitimate and proper and necessary Federal function to the myriad patterns of State control, when the needs of the people are the same in all States. Such a chaotic plan discourages thrift * * *.

It seems to me you are going right to the heart of the whole thing and I would read into your testimony the idea that you want all State control of this function eliminated.

Mr. BENT. No. We would. I will admit we would like to have the State legislatures of each State review the situation and establish a proper basis, but we do not want to have the Federal law passed which would say we must conform to a State, because we have some very bad situations. Probably the worst is in Alabama, where you have regulations applying to various cities.

Senator BENNETT. Are you still talking about branching?

Mr. BENT. I am.

Senator BENNETT. And you think the present situation "reduces home financing capital"—and I will go further and read from your statement—"is a chaotic plan which discourages thrift"?

Mr. BENT. Yes, I do.

Senator BENNETT. Lack of branching is a chaotic plan?

Mr. BENT. No. The lack of ability to serve the people of the Nation on a systematic basis, and to be able to go out and reach them and render services to them, creates quite a chaotic condition in our field. In other words, in most States and many States we can establish branches to go to the people. I could, if I had the time, cite individual States where this restriction prohibits the ability to go into areas where they are badly needed. We have other situations, and I will cite the specific case of Alabama, where they have a State law which permits branching in cities of—I do not know the population figure—but let us say 100,000 they may have branches; 150,000 they may not have, and 200,000 they may have. If that is not chaotic I do not know anything that is.

In the State of Massachusetts they have a situation which is limiting the branch facilities for savings and loan associations or cooperative banks, as it is known in that State, where the same restrictions do not apply to commercial banking facilities.

You probably know yourself, in New York State they are having quite a wrangle about trying to get equality and parity for savings banks, which savings and loan would like to follow.

Senator BENNETT. That is all.

Senator ROBERTSON. You may proceed.

Conflicts of interest (title IV, sec. 19 (b), p. 200)

Mr. BENT. During the initial hearings on the agency recommendations, the Federal Deposit Insurance Corporation spokesmen, as I recall, suggested an amendment making it unlawful for any employee or former employee of the Corporation to accept employment with any insured bank except pursuant to regulations prescribed by the Corporation. This suggestion was incorporated into the committee print bill so as to cover employees of the Comptroller of the Currency, the Federal Reserve Board, the Federal Deposit Insurance Corporation, and the Federal Home Loan Bank Board.

We believe that the objectives of this language may be achieved equally well without resort to this broad delegation of continuing authority for these Federal agencies to impose conditions upon an individual's future choice and condition of employment. If the conditions imposed on Government service are too rigid, it will impair the procurement of the best talent for these positions. For this reason we suggest that such authority be limited to the first 1 or 2 years subsequent to the date on which the employee severed his connection with the agency.

We also direct the committee's attention to section 217 (ii) of title 18 of the United States Code as amended by this bill. This section imposes criminal penalties upon any officer or employee of an insured financial institution who employs or makes an offer of employment to these agency people without written approval. You will note that this section contains a 2-year limitation.

Restrictions on associations, directors, and officers (title V. sec. 7 (e), p. 213)

The next amendment we suggest is to section 7 (e) (p. 213) of the proposed Federal Savings and Loan Act, which relates to home loans by an association to its executive officers.

Under existing law and regulations promulgated by the Board, a Federal association may make loans of the security of a first lien on a home owned and occupied by a director, officer, or employee of the association or by an attorney serving the association. Detailed regulations prescribe conditions of the loan such as loan-to-value ratio and appraisal procedure. There is no dollar limitation, however, other than that imposed on members in general.

Let me say that we concur fully in the motives behind this language. We do not believe an officer of these institutions should be able to obtain financing of the home in which he intends to live on more favorable terms than the general public. At the same time we do not believe this limitation is either equitable or necessary. We do not believe a loan secured by a first mortgage on a person's home can be placed in the same category as personal, unsecured loans.

The boards of directors of Federal savings and loan associations have a very definite responsibility to scrutinize carefully loan applications submitted by executive officers. Federal examiners, you can be sure, also pay special attention to such loans.

We suggest, therefore, that section 7 (e) be amended to permit an executive officer to obtain a home mortgage loan upon the dwelling which he owns and occupies without dollar limitation other than the limitation set under section 5.

Senator ROBERTSON. May I interrupt there?

Mr. BENT. Yes.

Senator ROBERTSON. Do you admit that there were instances under the FHA when there was what was called mortgaging out?

Mr. BENT. I beg your pardon?

Senator ROBERTSON. Do you know what mortgaging out means?

Mr. BENT. Yes, sir.

Senator ROBERTSON. What does it mean?

Mr. BENT. It means you are trying to finance the entire cost of the property.

Senator ROBERTSON. Overassessed is what it means, does it not?

Mr. BENT. Yes, sir.

Senator ROBERTSON. Could it not happen if a man had to sell a $20,000 house and the safe limit would be $15,000, then could he not get a $25,000 appraisal so that he gets $20,000, which pays for the entire works? Could that happen if he were on the inside?

Mr. BENT. Sir, it could happen, but if it did happen it would place the directors of that institution in jeopardy of criminal action, which could happen in any institution.

Senator ROBERTSON. Will you not admit that we have had plenty of instances of overappraisal? We were just trying to put a little restraint on the temptation here.

Mr. BENT. I understand your motives, sir, and they are very fine.

Senator ROBERTSON. All right.

Mr. ROGERS. Could I ask you a question, Mr. Bent?

Mr. BENT. Yes, sir, Mr. Rogers.

Mr. ROGERS. You refer to the limitations under section 5. Is that the $35,000 you referred to?

Mr. BENT. Yes, sir. And it has been a varying amount. We see no reason why a director of an institution should not have the general rights of the public in general. No more, but we feel he is entitled to the same benefits.

Mr. ROGERS. The purpose of this provision was to bring savings and loans into parity with the banks. We liberalized the bank provisions in here to permit bank officers to borrow up to $5,000.

Mr. BENT That is right. We understand and recognize the necessity of your reviewing that sort of thing, but we feel there is a very definite difference between a savings and loan bank and a commercial bank, in that we have only one type of investment, which is rigidly controlled through the operations of the association. Definitely every loan is examined by the Federal examiners each year, and it has better control than probably an unsecured loan of smaller amounts.

Senator ROBERTSON. But there is not any difference in the amount of insurance that each gets. Each gets their individual accounts insured up to $10,000.

Mr. BENT. That is correct.

Senator ROBERTSON. Then each could become a potential liability in times of depression and default on mortgages, for instance.

You may proceed.

Mr. BENT. Thank you.

This amendment in no way detracts from the Board's existing authority and that granted by this section to regulate carefully this type of lending.

Equality of treatment, FSLIC—FDIC (title III, sec. 30 (b) (2); title IV, sec. 406 (b) (2)

The language of the committee print embodies a recommendation of the Advisory Committee relating to payment of insurance by the two Federal insurance corporations. One or two witnesses have recommended that this section of the bill be changed. We think the language of the committee print is quite satisfactory. If changes could be made, however, we urge the committee to give equal treatment to all insured accounts.

GENERAL COMMENTS

We feel that the occasion is appropriate for a brief statement of the basic position of the National Savings & Loan League with respect to issues which always underlie any consideration of our banking and credit structure.

In the first place, we strongly favor the continuation of the dual system of State and federally chartered savings and loan associations. Whenever Federal legislation is being considered which is going to operate directly on associations chartered by a State, such legislation must of necessity be tied in with Federal insurance of accounts or membership in the Federal Home Loan Bank System. When the Insurance Corporation insures, it naturally and very wisely is concerned about the safety and soundness of the institution. We think that concern, however, should be limited to the safety and soundness if the dual system is to be preserved. In other words, we would urge this committee to examine carefully whether the insurance concept is being used to regulate conduct in no way connected with the safety of the institution.

The strength of our system must in the final analysis lie with management itself. No amount of regulation or supervision is going to guarantee that all institutions will be run in the businesslike way that enlightened management and the supervisory agencies would prefer. Come what may, you are going to have some bad apples.

We do not object to supervision or regulation or legislation setting up ground rules designed to achieve the kind of system that the Congress, the public, and industry want. We would add just one word of caution, however. In our desire to achieve this goal, an overzealousness that leads to the imposition of too many intricate rules and a continuous broadening of supervisory inquiry beyond the field of safety can eventually reach a point of diminishing returns.

The savings and loan business is more closely regulated than any other corporate entity, financial or otherwise. Regulations governing the system exceed 100 pages of fine print. The Federal Home Loan Bank Board and the Federal Savings and Loan Insurance Corporation are doing a very fine and effective job under existing laws and regulations. Losses by the Insurance Corporation have been practically nil.

A workable and practicable solution must be established to permit conversions between State and federally chartered associations and stock and mutual associations. The Federal Government has for over 20 years fostered conversions from State to Federal charters. A few years ago, the statute was amended to permit Federal associations to convert to State charters.

About 10 of our States permit the chartering and operation of stock type savings and loan associations. Good faith if nothing more would require the Federal Government to permit conversion from a Federal association to a State stock association in those States where the latter are permitted to operate, but on a fair and equitable basis to everyone concerned.

We do not object to the imposition of reasonable agency discretion on matters of licenses, applications, and like, but we do feel that where agency action involves removal of a vested right or interest, that agency determination should then be on a basis of legal rules or a judicial determination, rather than on a basis of agency discretion.

In conclusion, I would like to make this suggestion to the committee:

We do not wish to add to the expense of printing the record of this hearing, but believe consideration might be given to printing as an appendix to this hearing the rules and regulations governing Federal savings and loan associations, and the rules and regulations governing insured associations. These demonstrate the fact not generally realized that our business is well and thoroughly regulated and supervised. In addition, it would be useful to print the conditions imposed in a typical application for insurance case to show the care that is now being exercised. In addition, it would be useful for the committee to receive and study a summary record of a typical branch application, together with the detail necessary to prosecute this application through hearing to completion. Although these transactions involve only a part of the work of the Federal Home Loan Bank Board and the Federal Savings and Loan Insurance Corporation, they do show conclusively the fine work that is being done under the present statutes.

Thank you for your attention.

Senator ROBERTSON. We thank you. Are there any further questions?

Senator BUSH. Yes, Mr. Chairman.

Senator ROBERTSON. As a reminder, the committee has available to it all of these rules and regulations, and we would not want to put two or three hundred pages of them into this record, as it will be voluminous enough anyway.

Senator BUSH. I want to ask Mr. Bent 2 or 3 questions.

You speak on page 10 of your statement of the rules and regulations governing Federal savings and loan associations, and the rules and regulations governing insured associations. What does that mean?

Mr. BENT. That would be members of the Federal Home Loan Bank, and they might not be chartered by the Federal Government; but we do have State members and probably it is much more than half of the savings and loan industry that are such members.

Senator BUSH. With insurance by the Federal Government?

Mr. BENT. Mr. Braman says there are about 1,700 of each.

Senator ROBERTSON. So that the Federal insurance organization that insures Federal savings and loan institutions also insures the State institutions?

Mr. BENT. That is right.

Mr. BRAMAN. Some of them.

Mr. BENT. Not all. I want to make that point.

Senator BUSH. Under what circumstances can you make a loan from the bank, that is, from the Federal Home Loan Bank?

Mr. BENT. Our institution borrowing from the Federal Home Loan Bank?

Senator BUSH. Yes. What privileges do you have as a member to borrow? Under what circumstances are you privileged to borrow?

Mr. BENT. Under the rules and regulations of the Federal Savings and Loan System any institution is permitted under rules established by the various banks to borrow up to a maximum of 50 percent of their share capital.

Senator BUSH. Under any circumstances?

Mr. BENT. No, sir. That is permitted by law. That is the maximum permitted by law under ground rules established by each bank, and the limitations are set.

In the Boston area, with which we are familiar, we establish lines of credit from the bank to any member institution. That had recently been established as 35 percent of their share capital, of which only 15 percent could have been used for making advances to members for mortgage loans. Since credit restrictions have been established as of a year ago in August, that was reduced to 5 percent, and in recent months with some easing it has been increased to 12 percent.

So effectively, Senator Bush, the lending of the bank for mortgage business in the New England area is limited to 12 percent of the share capital of the member.

Senator BUSH. And that limitation is placed by Washington?

Mr. BENT. No, sir. It is established by the board of directors of each regional bank, but is in conformance with credit restrictions established by the Board in Washington. The Board suggested the 12-percent limitation.

Senator BUSH. What happens to all of the rest of that borrowing power you have?

Mr. BENT. It is held as a reserve for emergency purposes for the withdrawal of funds in the case of need in any one particular area.

Senator BUSH. The reason why I raised this question is, one hears frequently from some of your competition in other fields the criticism that you have a borrowing power that they do not have.

Mr. BENT. That is right, but they could have it, you know.

Senator BUSH. In what way?

Mr. BENT. Well, any savings bank, for instance, has the privilege of becoming a member of the Federal Home Loan Bank System. A few of them do. We have had 1 or 2 in Connecticut. The Manchester Bank has, and I think they have since resigned and have actually borrowed from the bank. The manager of that institution is the ex-banking commissioner of the State.

Senator BUSH. So any savings bank could avail itself of the power you have?

Mr. BENT. And insurance companies may become members of the Home Loan Bank System.

Senator BUSH. You mean any insurance company?

Mr. BENT. That is right.

Senator BUSH. A life-insurance company?

Mr. BENT. Under the laws, the savings and loan associations, the mutual savings banks and insurance companies may be members of the Federal Home Loan Bank and join the Insurance Corporation. Is that true?

Mr. BRAMAN. No. Just members of the bank.

Senator BUSH. Members of the Federal Home Loan Bank?

Mr. BRAMAN. Have the privileges of that system.

Senator BUSH. Do any insurance companies avail themselves of that?

Mr. BENT. There are a few, but I do not know who they are. We do not have any in Connecticut.

Senator BUSH. We do not have Connecticut insurance companies who are?

Mr. BENT. A few savings banks, but no insurance companies in Connecticut.

Senator BUSH. I have no other questions.

Senator ROBERTSON. We thank you.

Mr. BENT. Thank you, Mr. Chairman.

Senator ROBERTSON. We have listed five witnesses to represent a great national organization called the United States Chamber of Commerce. I hope the witnesses will coordinate their testimony with a view to getting what they want into the record in the limitation of the next 55 minutes, because we can be in session only that long.

Our first witness will please give his name and title to the reporter and may introduce his associates.

STATEMENT OF WILLIAM A. McDONNELL, CHAIRMAN, FINANCE COMMITTEE; ACCOMPANIED BY NORFLEET TURNER, NATIONAL BANK AND COMPTROLLER OF THE CURRENCY SUBCOMMITTEE; BURNHAM YATES, CHAIRMAN, FEDERAL RESERVE SUBCOMMITTEE; AND GEORGE BLISS, CHAIRMAN, HOME LOAN BANK ACT AND THE FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION SUBCOMMITTEE, ON BEHALF OF THE UNITED STATES CHAMBER OF COMMERCE

Mr. McDONNELL. Mr. Chairman and gentlemen of the committee and Mr. Rogers, I am William A. McDonnell, chairman of the board of the First National Bank of St. Louis, Mo. My appearance today is as chairman of the finance committee of the Chamber of Commerce of the United States.

I have with me Mr. Yates, Mr. Turner and Mr. Bliss, my associates, whom I will introduce to you later.

The finance committee has been studying the many recommendations made to you and the members of the Senate Banking and Currency Committee by the various Government agencies and the Citizens Advisory Committee appointed by you. As a result of our deliberations and study we would like to present our findings and recommendations.

It is my desire to state very briefly the steps which the chamber has taken looking toward the improved functioning of the American financial system. On the original announcement of the study, the national chamber's finance committee was in session here in Washington. The committee was fully appraised of the study's scope and immediately established five subcommittees along major lines of the study. These subcommittees have been manned by oustanding businessmen and bankers from throughout the Nation, from both large and small institutions. They have worked diligently and carefully on the proposed changes in the laws.

With your permission I should like to introduce at the close of my remarks the chairmen of these subcommittees, who will discuss in detail the major aspects of the Financial Institutions Act of 1957.

The interest of the national chamber in matters pertaining to the commercial banking system, as well as other financial institutions, is of long standing. One of the national chamber's earliest membership referenda was upon the question of the establishment of the Federal Reserve System. As a result of that referendum the support of the business community was shown clearly to be back of the then pending Glass-Owen bill. The record will show that the business community took this position at a time when banking support of the measure was by no means unanimous. Since the passage of the Federal Reserve Act, numerous features of the banking system have been the subject of public reports by the national chamber, and recommendations for improvement of banking laws and practices have had our strong support.

No one, least of all business leaders, can afford to take an attitude of indifference toward money and the monetary system. Although the subject involves matters of a technical nature, this should not mean that the study of banking and financial institution laws should be left exclusively to the financial managers. While bankers are specialists in the management of money, the consequences of their decisions are of great importance for all business and for all citizens as consumers and workers. I am in the commerical banking business myself, but in the capacity in which I appear before you today I speak for American businesmen, and the recommendations which my colleagues and I shall make have the approval of the board of directors of the national chamber, who represent the entire—or at least a fair cross section of the entire—business community.

We should like to commend the work you are doing here to update the laws regulating financial institutions. By and large, we have seen it proper to endorse most of the changes and recommendations contained in the proposed Financial Institutions Act of 1957. There are, however, some few areas of disagreement.

While we understand that the purpose of this particular study is simply to recodify existing banking laws, the national chamber would like to express the hope it would be followed by a study of the financial and monetary institutions of this Nation. There should be a comprehensive and objective review of the Nation's monetary policy and financial institutions to appraise the nature, performance, and adequacy of existing financial institutions. Whether existing financial institutions and monetary policies are adequate to meet the needs of our expanding and demanding economy should be a consideration of the commission. The national chamber urges that the President be requested to establish a nonpartisan citizens' commission to conduct the study.

The national chamber further recommends the orderly and early liquidation of the Postal Savings System. This has long outlived its useful purpose and now is an undue burden on the taxpayers.

Although it was not deemed proper to include in the current study recommendations for change in the existing Treasury regulations for the establishment of adequate and realistic bad debt reserves——

Senator ROBERTSON. May I interrupt?

We were in full sympathy with that proposal, but the reason why it could not be included in our study is we do not have jurisdiction over tax laws.

Mr. McDONNELL. Yes, sir.

Senator ROBERTSON. That is the reason. Our advisory committee said we favored it, but we will recommend it to the tax committees, and the Chair respectfully suggests that he would like to see the chamber of commerce, in addition to mentioning it to us, tell the tax committees of the House and Senate that you favor it, and tell the Secretary of the Treasury you favor it.

Mr. McDONNELL. I can assure you, sir, that will be done.

Senator ROBERTSON. Thank you.

Mr. McDONNELL. Although it was not deemed proper to include in the current study recommendations for change in the existing Treasury regulations for the establishment of adequate and realistic bad debt reserves, it is the national chamber's recommendation that this be referred to the proper congressional committees for early consideration with a view toward establishing an equitable reserve formula based on today's risks and inadequacy of capital in the banking system. The committees on taxation and finance of the national chamber both urge enactment of a flat industrywide reserve of not less than 5 percent of eligible loans outstanding. We also think that the Federal rules and regulations covering the establishment of branches should be the same for Federal savings and loan associations as they are for commercial institutions.

Our position is that title V, section 6 (c), as written in the act, meets with our approval.

The following members of the finance committee will now discuss in detail the provisions of the proposed act: First we have Mr. Norfleet Turner, Memphis, Tenn., on the matters pertaining to the national banking system.

Senator ROBERTSON. We will be glad to hear from Mr. Norfleet Turner.

Mr. TURNER. My name is Norfleet Turner, and I am president of the First National Bank of Memphis.

As chairman of the national bank and comptroller of the currency subcommittee of the national chamber, I should like to emphasize we firmly believe that American banking as an essential segment of free enterprise requires the widest play of the initiative, resourcefulness, and intelligence of the management of individual banks and freedom from excessive regimentation.

The national chamber is dedicated to the principles of a dual banking system which provides checks and balances consistent with effective supervision.

In line with these beliefs we have the following recommendations as pertains to the Financial Institutions Act of 1957:

1. With reference to the amendment of section 217 of title 18 of the United States Code, page 247, the chamber believes that section 8 of the National Bank Act, titled "Conflicts of Interest Prohibited," page 3 of the committee print, provides adequate legislation to cover the employment or offer of employment to any employee of the Comptroller's office. The chamber favors the provisions of section 217 against gratuities and the granting of loans to supervisory staff members, but to impose a restriction preventing a bank offering or an examiner accepting employment for a period of 2 years following any association with the Comptroller's Office, would work an insurmountable hardship on the Comptroller, and to a degree on national banks. The recruitment of able, efficient, capable examiners has always been an acute problem for the Comptroller, but his past experiences will pale into insignificance when compared to the problems which will be encountered in trying to obtain competent men if this provision is enacted into law.

Senator BUSH. Will the gentleman pause while I ask the Chair a question?

Mr. TURNER. Yes, sir.

Senator BUSH. Did the Comptroller himself testify on this point? I did not attend that day.

Senator ROBERTSON. Do you mean last November?

Senator BUSH. Whenever he appeared. Yes.

Senator ROBERTSON. The Comptroller will appear as one of the last witnesses to conclude these hearings with the official position, which will contain his position on everything in this bill, after we hear from the Federal agencies. The Comptroller has not stated any official position yet. He gave some preliminary statement.

Senator BUSH. Have any of the Government witnesses testified on this point which Mr. Turner is discussing?

Mr. Rogers. No.

Senator Bush. All right.

Mr. Turner. Many of the fine personnel serving in the Comptroller's Office are hopeful that the experience gained in examining banks will lead ultimately to their association with a good banking institution. Bankers themselves have recognized the value of such training, and have not hesitated to recommend it to young men who seek eventual executive responsibilities in the banking field. Some of the Nation's leading bankers prepared themselves for their present careers through training as examiners.

Suppose an examiner has served 10 or 15 years with the Department and suddenly his health becomes such that he no longer can travel. His usefulness to the Department may be gone and he is legally barred for 2 years from turning to the field of endeavor for which he is best fitted. Under the present policy of the Comptroller all examiners must agree not to accept employment with a bank for a period of 2 years after leaving the Department, without the approval of the Comptroller. We know of no instances where there have been any abuses under that policy, and it does allow the Comptroller to prevent an injustice of the kind described.

To deny to the banking profession access to this field of highly trained executives or potential executives would be harmful, but the national banks would suffer a great deal more through a lowering of the standards of national bank examinations, which would be inevitable if a member of the force knew he was "locked in" and, from a practical standpoint, could never pursue the profession for which he is best qualified.

The chamber fears that the doubt now raised by the injection of this portion of the amendment will have an adverse effect on the recruitment section of the Comptroller's office until it is known that all concerned favor the deletion of this particular portion of this amendment. The chamber, therefore, recommends the deletion in subsection (ii) of section 217, page 248, of the words, "or employs or makes an offer of employment to," and in subsection (iii) of the words, "or employs or makes an offer of employment to," with the feeling that section 8 of the National Bank Act on page 3 of the committee print fully covers the situation desired to be corrected. We suggest, however, that some time limitation be contained in section 8 (b) unless it is intended that this will be covered in the regulations to be prescribed by the Comptroller.

Senator Bush. May I interrupt again?

Senator Robertson. The Senator may.

Senator Bush. I am not familiar with all of these references, so I would like to ask you a direct question. Do you favor placing any limitation on employment of the former employees of the Comptroller's office, and, if so, what?

Mr. Turner. Senator, I believe that the present practice of the Comptroller's office that it must have his permission has adequately served so far, and I believe it will in the future.

Senator Bush. In other words, you do not favor any long-term waiting period of a year or two fixed by law, but you believe it should remain as it is?

Mr. Turner. Yes, sir.

Senator Bush. Thank you.

Mr. ROGERS. That conflicts with your prepared statement here. You say that you recommend section 8 (b) be enacted.

Mr. TURNER. Section 8 (b) provides, as I recall it, Mr. Rogers, that it shall be—that the Comptroller may authorize, as he does now.

Mr. ROGERS. That is right. You do favor writing into law the present practice.

Mr. TURNER. Yes. I beg your pardon, Senator.

Senator BUSH. We are all correct. I am just asking what he thought about the principle.

Senator ROBERTSON. We are in agreement, I think.

Senator BUSH. We are all set.

Senator ROBERTSON. You may proceed.

Mr. TURNER. 2. The national chamber approves section 23 of the Federal Deposit Insurance Act, mergers and consolidations, page 162 of the committee print.

Our interest in this proposed legislation has primarily to do with that section giving authority to the three supervisory agencies, the Comptroller of the Currency, the Federal Reserve Board, and the Federal Deposit Insurance Corporation, to approve of bank mergers and consolidations.

Competition is a very important influence in our American way of life and should not be thwarted; nevertheless, it must never be the prime consideration in evaluating the merits of a merger or consolidation of banking institutions. Mergers and consolidations, per se, rarely result in a lessening of competition, but to the contrary, oftentimes stimulate it.

In a particular community a much more important factor than competition might be the preservation of a banking institution. For example, there may be 4 or 5 good banks, highly competitive, and suddenly one finds itself in a weakened condition, but still solvent. The merger with one of the stronger banks might or might not tend to lessen competition, but if this factor alone were considered, and the merger or consolidation denied, the result might be the final liquidation of the bank to the detriment of depositors, stockholders, and the public generally.

3. The national chamber offers no objection to the issuance by banks of preferred stock, but there are dangerous implications in the issuance of capital notes and debentures authorized under section 21, page 10 of the committee print. The proposed law provides that the issuance of such obligations shall be approved by the Comptroller, but we believe that somewhere in the act should be a specific provision that his approval must be granted only when in his opinion this form of temporary capital is necessary in an emergency situation.

The proposed law might place the Comptroller of the Currency in the awkward position of insisting that a bank acquire additional capital only to have it choose the issuance of notes or debentures rather than common stock. In all probability, many banks would elect this means of complying with the Comptroller's requirement. We would approve passage of this act with a provision that debentures would be authorized only in emergency cases.

Mr. ROGERS. This is the first testimony we have had on this particular point. I wonder if you might go into a little detail on these dangerous implications. Are you afraid of diluting the value of the common stock, or exactly what do you have in mind?

Mr. TURNER. No, Mr. Rogers. I feel a debenture form of capital can be only a temporary form. In issuance of debentures it must be provided that they can be paid back at some time, so it is a temporary form of capital in the opinion of those of us who have studied it, and passage of this proposed act without some reference to emergency cases might lead the Comptroller to the point where he tells the bank, "We would like you to issue more capital," and the bank says, "Under the law I have the right to issue these debentures," and the Comptroller would be in the awkward position of saying you have to issue more capital, but can't issue debentures.

We feel debentures do not represent the type of capital which should be in banks over the long pull.

Senator ROBERTSON. The Chair intends to look into that because he does not like the word "debenture," anway. It purports to be a mortgage but it is not.

Mr. TURNER. It is a debt and not an equity.

Senator ROBERTSON. No. If you are going to give something that is worth something to the man that lends something, then give a lien on the property. Otherwise you can finance it through your preferred stocks. The bill authorizes preferred stocks if you want to issue it. They have that under the RFC, but it has not been used much. We put it in here.

Senator BUSH. In many growing businesses the device of the convertible debenture has been used over many years, as you gentlemen know. Would you also rule that out here?

Mr. TURNER. Senator, I do not believe that occurred to us in our study, that is, convertible debentures. I do not believe I am prepared to answer that question.

Senator BUSH. It seems to me they have some merit even in a bank-financing operation. I do not know. I have not thought about it much either, but your statement suggested that inquiry. I think it would be interesting to hear from this organization on that point, Mr. Chairman. It is a good device for growing institutions.

Mr. MCDONNELL. May I say, Mr. Chairman, that our committee would be glad to make a study of that particular point and file a statemention on it for your benefit.

(The following was received with reference to the above:)

ADDITIONAL STATEMENT ON CONVERTIBLE PREFERRED STOCK AND CONVERTIBLE DEBENTURES ON BEHALF OF THE CHAMBER OF COMMERCE OF THE UNITED STATES

Sound banks have traditionally been able to raise necessary capital to keep pace with the growing demands of the economy through the issuance of common stocks. In the past year alone nearly $200 million of new national bank stock was sold through the common method.

Larger banks could more easily market convertible preferred stock and convertible debentures than the average American banking institution, whereas medium-sized and small banks might be administratively overburdened by the mechanics of convertible offerings.

A bank must have prestige, sound management, and a record of good earnings in order to sell its capital issues readily under the present common stock method. Even banks enjoying this position might attempt to raise capital through the convertible method if only because it is a relatively easy though unusual, way to tap new sources of investment funds.

Bank stock today is a high-grade security, understood by all buyers, not affected with varying terms, free from special features. The moment bank stock becomes convertible preferred or a convertible debenture it tends to confuse prospective stockowners. For this reason it has proved better in the past to have one class of stock; we have not, however, opposed the issuance of straight preferred stock by banks.

In considering the convertible feature of bank stock it must be determined at what price the stock is to be converted and whether it is to be converted at the time of issuance or at some later date. Actually, if conversion is utilized, the sale becomes one of common stock. If conversion is scheduled for a long time ahead a bank might conceivably hold down its common dividends and pile up values. Then, should the preferred be convertible at a value fixed at issuance, whereas the intrinsic value may have doubled between date of issuance and date of conversion? Answers to these questions call for a high degree of technical knowledge.

There may be times when the common stock market is not in too good shape and a bank may want to use the convertible preferred or convertible debenture method of raising capital. We feel, however, that the disadvantages of this procedure outweighs its advantages.

Common stock in the banking industry stays and grows and becomes a greater protection, whereas convertible preferred would be retired under a specified schedule. A certain amount of permanence in the local community is provided through the ownership of common stock. The issuance of convertible preferred or convertible debentures, which are either retired or redeemed, does not create this element of permanence.

These considerations force us to oppose bank use of these types of securities except in cases of emergency.

Senator ROBERTSON. You will have to do it with reasonable dispatch because we want to get these hearings printed within 2 days after the last witness testifies.

Mr. TURNER. When will that be?

Senator ROBERTSON. The week after next. We conclude testimony on the 18th of this month.

Mr. McDONNELL. We shall endeavor to have something in by that time.

Senator BUSH. One more question. There was no objection raised here to the preferred stock device. I see that is specifically stated here.

Mr. TURNER. Yes.

4. The liberalization of present laws pertaining to real estate loans as provided under section 36, page 28 of the committee print, is urgently needed. The present law is antiquated in the light of modern industrial development, with its shopping centers, new plants, firm commitments from responsible lenders to take permanent loans, and with its resulting problem of providing working capital loans under term-loan agreements. Furthermore, the present restriction on the total amount of construction loans a bank may legally make is unrealistic in view of other safeguards and present-day construction costs.

5. Concerning the restriction of States from subjecting national banks to examinations and licensing as proposed under section 51, page 41, of the committee print, we urge enactment of this legislation.

6. The procedure for the election of directors, provided in section 26, page 13, of the committee print, has the approval of the national chamber. Our interest is confined primarily to paragraph (*c*), making cumulative voting optional with national banks. Instances are rare indeed where the privilege of cumulative voting has been used constructively; to the contrary, those availing themselves of the privilege have in most instances done so at the expense of harmony and cooperation in the board of directors and with the management of the bank.

Senator ROBERTSON. The Chair would like to interrupt there to underscore that testimony. The Chair was a patron of the bill that passed the Senate—in fact, the bill got a majority vote in the House—to make cumulative voting permissive rather than compulsory. The testimony is that few instances have been known where it is used constructively, but plenty of them where it has been used destructively.

Mr. McDonnell. That is right.

Senator Robertson. You may proceed.

Mr. Turner. Cumulative voting may be necessary for the protection of minority stockholders in many corporations, but banking is unique in that its management, the soundness of its operation, and the quality of its assets are under constant supervision and periodic examination by supervisory authorities. Any grievance a minority stockholder might have would doubtless be investigated by one or more of the supervisory agencies and, if it had merit, ample law is provided to bring about its correction.

Senator Bush. May I ask one brief question?

Senator Robertson. You may.

Senator Bush. I would like to suggest to Mr. McDonnell that in making this supplementary statement on the question of convertible debentures, they also give their views as to the use of convertible preferred stock. You did not mention the convertible device at all. (See p. 664.)

Mr. McDonnell. Yes.

Senator Bush. You included preferred stock, but as long as you are going to study it from the debenture standpoint, I would like to have your views on the conversion of preferred stock.

Mr. McDonnell. We shall be glad to do so.

I would now like to introduce Mr. Burnham Yates, of Lincoln, Nebr.

Senator Robertson. Before he testifies, I want to thank those who have already testified and those who are going to testify for the help to the gentlemen of this committee that a group of experienced bankers and businessmen of Missouri, Tennessee, Nebraska, New York, and Alabama are giving us in this study, because the substance of their testimony after a careful study of what we propose is that on the whole, "We are endorsing what you are doing. There are a few minor changes we want to suggest to you."

To the chairman that is very gratifying and very helpful. You may proceed.

Mr. Yates. Thank you, sir.

My name is Burnham Yates, president of the First National Bank of Lincoln, Lincoln, Nebr.

May I reiterate what you just said? Our wish is to commend the committee and the Advisory Committee for the efforts they have put forth which will lead to recodification of these laws. On the whole we think that the job is a very fine one. My purpose is to talk about some of the suggested changes having to do with the Federal Reserve Act.

Recommendation 51 has to do with the location of the directors of the Federal Reserve banks. This recommendation would require such directors to be residents of the Federal Reserve district on whose bank board they are serving. The national chamber recognizes the intent of this recommendation, but feels that the principal place of business should determine membership on the board, rather than residence.

There can be cases where an individual would have a legal home residence other than his place of business, and which would cut across Federal Reserve districts, and which might prohibit him from serving on a board in that area where his major interest lies.

Mr. ROGERS. Do you know of any cases that would fall outside of the 50-mile liberalization in that provision?

Mr. YATES. Specifically, no. It has been mentioned before in 1 or 2 instances there are a few individuals who have established legal residence in Florida, although they are important in the business world, for example, in New York City, possibly for personal tax reasons. It is a minor point.

Recommendation 52 on pages 74 and 85 of the act: The recommendation would limit service of Federal Reserve Bank directors (other than the Chairman) to 2 consecutive terms of 3 years each, and the tenure of service of members of the Federal Advisory Council to 6 consecutive 1-year terms.

We realize the point here.

The national chamber recommends that the limitations on the tenure in office of members of the board of directors of the Federal Reserve banks be 3 consecutive 3-year terms and that the limitation on tenure of office for members of the Federal Advisory Council be limited to 9 consecutive 1-year terms.

We feel the additional 3-year period might be very helpful, but still provide a broader representation which you gentlemen desire.

Recommendation 54 on page 73 of the bill: Payment of Reserve bank earnings to the Treasury. The national chamber agrees with the Advisory Committee in stating that the franchise tax is probably the simplest method of clarifying the situation, but feels that a statutory directive of transfer of any specified percentage of bank earnings might at some time become an onerous and undesirable provision. We favor, instead, legislation authorizing the Federal Reserve Bank Board to transfer annually to the United States Treasury such portion of net earnings as the Board deems appropriate.

Recommendation 58 on pages 48 and 92 of the bill relative to reports by State member banks should be rewritten to make clear that in requiring the publication of reports, the Board shall not require the publication of reports of dividends or earnings and, in requiring publication of reports of condition, such publication shall be required from all State member banks on the same date. The national chamber feels that these reports are of a confidential nature and this confidence should be respected, and damage can be done to particular banks if such publication were required.

Mr. ROGERS. May I ask a question on that last point?

Mr. YATES. Yes, sir.

Mr. ROGERS. What we have done in this section on the Federal Reserve member banks is reenact into the law the present law, except for one sentence which deals with reports on a sample basis. I wonder, is your objection to the present law rather than to the bill?

Mr. YATES. The phrase has to do with payment of dividends. That is the only thing, Mr. Rogers. As long as that is not construed as earnings.

Mr. ROGERS. But that is in the present law.

Mr. YATES. Yes, sir.

Mr. ROGERS. In your report on payment of dividends do you usually report your earnings in the same report?

Mr. YATES. No, sir.

Mr. ROGERS. That is what I understood.

Mr. YATES. That is right. It is just as a matter of clarification. I regret to state I am not an attorney, but if an attorney feels it is all right, I am sure it is satisfactory with us.

Mr. ROGERS. We want the benefit of your testimony.

Mr. YATES. Yes, sir.

The national chamber has endorsed recommendation 60 of the Board of Governors which would permit State member banks, with approval of the Board of Governors, to hold temporarily stock of another bank as one step in the process of acquisition in connection with absorptions and also endorses the same proposal for national banks.

We favor that and hope it will also be put in the law as regards national banks. We think it is a very good procedure and would like to see it in the law affecting national banks also.

Mr. ROGERS. It is in the bill.

Mr. YATES. I am sorry, sir. I am now aware of that.

Recommendation 77: This section refers to that portion of the Federal Reserve Act which prohibits the payment of interest on demand deposits "directly or indirectly, by any device whatsoever." There exists today a complete lack of uniformity between this rule and the interpretation given the matter by the Federal Deposit Insurance Corporation. We believe that Congress intended that rulings should be uniform, and that no interest in any form should be paid on demand deposits. Any interpretation other than a strict one can only lead to misconstruction and inequities as between banks operating under different supervisory authorities. We therefore urge the enactment of legislation which would require the Federal Deposit Insurance Corporation to adopt the present law.

We are glad to see the section has been improved and the Federal Deposit Insurance Act in section 26 has been changed to conform.

Recommendation 81 has to do with loans of member banks to executive officers. We approve entirely the recommendations which have been put in the bill—the recommendations of the Advisory Committee. In the main we feel a tremendous job has been done, and we thank you.

Mr. McDONNELL. The next statement that is in this printed folder was to have been made by Henry A. Coleman of Daytona Beach, Fla., concerning matters pertaining to the Federal Deposit Insurance Corporation. Mr. Coleman is in the hospital for an operation and we would ask simply to file that report.

Senator ROBERTSON. Without objection, the complete statement of Mr. Coleman may be made a part of the record at this point.

(The statement of Mr. Coleman follows:)

STATEMENT OF HENRY A. COLEMAN, ON BEHALF OF THE UNITED STATES CHAMBER OF COMMERCE

I shall discuss some of the major aspects of title III of the Financial Institutions Act of 1957 as it pertains to Federal deposit insurance.

Let me first discuss sections 6 and 7 of the bill which provide for a change in the management of the Corporation from the present Board of three directors to a single Administrator and the creation of an Advisory Board of three members composed of the Comptroller of the Currency, the Chairman of the Federal

Reserve Board of Governors, and a designee of the State supervisors of banks.

We are in agreement with this proposal and feel that a single administrative head would add greatly to the efficiency and smooth operation of the Corporation. It would add representation of the State banks to the Corporation, as well as the experience and abilities of the Federal Reserve Board Chairman.

The national chamber believes that the Advisory Board should have general authority with respect to policies and operations of the Corporation and that the Administrator would be accountable to the Advisory Board.

We favor the protection of confidential records as proposed in section 10 page 153 of the act, which provides that Corporation records pertaining to any insured bank may not be disclosed without prior consent of the Corporation. This provision corresponds to the section 50 of title I as it relates to national banks.

We also favor section 16 (b) on page 157 which provides that any insured bank need not maintain records pertaining to its assessment computation for a period in excess of 5 years.

Certainly 5 years is adequate time for the Corporation to verify the correctness of assessment computations. Disposal of the records should be allowed by the insured bank after 5 years.

Section 2 (1) on page 149 restores to the law the assurance that a transferred deposit means a demand deposit in a new bank or other insured bank. We should like to state that the national chamber strongly urges that the wording "payable on demand in an insured bank" be retained in the bill.

Section 18 page 159 of the bill sets down the basis for determination of assessment credits to insured banks. The bill retains the existing provision that 40 percent of the Corporation's "net assessment income" be transferred each year to the deposit insurance fund and that the balance be credited pro rata to the insured banks.

At the present time the fund of the Corporation has exceeded $1.7 billion, which is equal to 1.41 percent of insured deposits, and through its 22 years of its operation the FDIC has disbursed for working capital purposes less than $290 million in connection with receivership and deposit assumption cases. The insurance fund of the Corporation is to insure depositors against losses resulting from ordinary institutional failures occurring through mismanagement, local disaster, defalcation, and other similar types of casualties. It would be quite unrealistic to believe that the Corporation insurance fund could possibly insure all accounts against wide-scale major economic disasters. We believe that the idea that the Corporation can insure all accounts against major calamities should be dispelled.

Further, we urge that a complete and thorough study be undertaken which would provide an accurate basis for determining the underwriting liabilities of the two Corporations, the FDIC and FSLIC. The need for such a businesslike study is apparent and should be undertaken as expeditiously as possible.

Section 23 on page 162 provides that there must be prior written consent by the appropriate Federal supervisory agency to any proposed merger, consolidation, or assumption transaction between insured banks.

The national chamber supports this legislation and urges its adoption. We believe that the authority over bank mergers correctly rests within the jurisdiction of the bank supervisory agencies and that the laws should so specifically state.

We also concur in the change in the law which proposes to shorten to 20 days from 120 days the period now permitted for the correction of unsafe and unsound practices by an insured bank in cases of insurance risk. We believe that section 29 (a) on page 165 as it pertains to the notice period will strengthen the power of the Corporation to act promptly in the public interest.

Mr. ROGERS. Mr. McDonnell, in that statement you endorse the proposal for a single Administrator for the Federal Deposit Insurance Corporation. Is that right?

Mr. McDONNELL. Yes, sir, we do.

Mr. ROGERS. It is a very important part of this bill.

Mr. McDONNELL. That is right, and we do.

Mr. ROGERS. I wonder, would you be able to discuss that a little bit, as to your reasoning?

Mr. McDONNELL. I will read that portion of his report here. It pertains to sections 6 and 7 of the bill, which provide for a change in the management of the Corporation from the present Board of 3 directors to a single Administrator and the creation of an Advisory Board of 3 members composed of the Comptroller of the Currency, the Chairman of the Federal Reserve Board of Governors, and a designee of the State supervisors of banks.

We are in agreement with this proposal and feel that a single administrative head would add greatly to the efficiency and smooth operation of the Corporation. It would add representation of the State banks to the Corporation as well as the experience and abilities of the Federal Reserve Board Chairman.

The national chamber believes that the Advisory Board should have general authority with respect to policies and operations of the Corporation and that the Administrator would be accountable to the Advisory Board.

That is our position. Do you care for any further clarification?

Senator BUSH. You say, "* * * a designee of the State supervisors of banks." How are they going to designate somebody? That seems to me like a very doubtful suggestion. That is no reflection on the supervisors, you understand.

Mr. MCDONNELL. I understand.

Senator BUSH. There are about 48 of them.

Mr. MCDONNELL. I know that Mr. Rogers investigated the operation of the machinery before this was written this way.

Mr. ROGERS. The provision of the bill concerned provides that the President is to choose from among those State supervisors.

Senator BUSH. The President of the United States?

Mr. ROGERS. That is right.

Senator BUSH. He is to do what?

Mr. ROGERS. To choose among the 48 bank commissioners.

Senator BUSH. Oh, that is different. I understand that now. That is in the bill?

Mr. ROGERS. Yes, sir.

Senator BUSH. I did not know that.

Mr. MCDONNELL. Now, gentlemen, if we may proceed I would like to introduce Mr. George L. Bliss of New York City, who will identify himself and give his report.

Senator ROBERTSON. We will be pleased to hear Mr. Bliss.

Mr. BLISS. My name is George L. Bliss and I live in Mount Vernon, N. Y. I am president of the Century Federal Savings & Loan Association of New York City.

As chairman of the chamber's subcommittee on the Federal Home Loan Bank Act, the proposed Federal Savings and Loan Association Act and the proposed Federal Savings and Loan Insurance Corporation Act, I should like to discuss briefly with you some of our recommendations as they relate to the proposed acts.

With respect to section 7 (f) on page 187, the national chamber recommends that the language be clarified to eliminate an inconsistency in providing that a "director may continue to act" in an office which has "become vacant." That is just a technical item, Mr. Chairman, and we think the staff can have no great trouble in smoothing out that language.

Mr. ROGERS. Mr. Bliss, do you agree with the thought?

Mr. BLISS. Yes. The principle is all right, but we do not see how anybody can act in an office which has been declared vacant.

A significant change in section 8A of the Federal Home Loan Bank Act eliminates all reference to the "board of trustees of the Federal Savings and Loan Insurance Corporation," with respect to the duties of the Federal Savings and Loan Advisory Council. The national chamber believes it to be important that the separate corporate status of the Federal Savings and Loan Insurance Corporation be clearly maintained by restoring the present language of this section.

Mr. ROGERS. Would you agree with me that the board of trustees is a fiction?

Mr. BLISS. Yes, but I will have something further to say on the same subject when we reach the Federal Savings and Loan Insurance Corporation Act. It is true the same persons serve in both capacities, but we regard it as quite important that they change hats and keep the corporate status of their two activities clear, separate and distinct, as a matter of principle.

In subdivision 4 (b) of section 10 of the Federal Home Loan Bank Act, page 190, we recommend that the phrase, "with respect to which the home mortgage was given, as such real estate was appraised when the home mortgage was made" be restored, on the basis that the present statute is more practical and that the proposed change could be the possible source of future abuse.

Mr. ROGERS. Is that a reference to section 4 (b) rather than section 4 (h)?

Mr. BLISS. It is subdivision 4 (b). Yes, sir.

Senator BUSH. You are not following the text we have here.

Mr. BLISS. No, sir.

Mr. McDONNELL. He is amplifying it a little bit.

Mr. BLISS. I am trying to clarify it.

Senator BUSH. Yes. It would help me a little bit if you would say, if you can, if it is consistent with what you are doing, to quote the recommendation you are discussing as it appears in the text. You could say recommendation 125 or recommendation 135. Can you do that?

Mr. BLISS. Yes, sir.

Senator BUSH. Thank you.

Mr. BLISS. The item I just spoke of related to subdivision 4 (b) of section 10 relating to recommendation 125.

Senator BUSH. Fine.

Mr. BLISS. Also under recommendation 135 we recommend that section 17 (c) be redrafted for clarity. While the national chamber endorses the objectives sought of providing parity in these areas—in the Federal Home Loan Bank Board, the Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation—it believes that the powers and authority of each of these agencies or organizations should be clearly stated in their respective statutes rather than by cross reference.

Senator ROBERTSON. The Chair interrupts to say that he has requested our drafting service, headed by Mr. Simms, to take this bill and take all of the testimony on the bill and go over the bill very carefully and help us to clarify the language of anything we want in there which we have not properly expressed. When we have finished with this, with your helpful suggestions and the suggestions we are getting from day to day, and through the work which will be continued by our own staff and the drafting staff, we hope to have a reasonably good bill ready for the Congress when we report one.

Mr. ROGERS. I wonder if you can clarify that point? Are you proposing to write into this act the provisions of the reorganization plan?

Mr. BLISS. No, sir. We are referring to section 17 (c) which says that the Federal Home Loan Bank Board shall have certain powers and authority, similar to those now accorded to the Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation. Should it be that those acts are amended sometime, it could only result in a confused situation as to what the powers of the Federal Home Loan Bank Board are. We think that the powers intended to be conveyed to the Federal Home Loan Bank Board, as a matter of draftsmanship, should be clearly set forth here rather than by cross-reference.

With respect to subdivision (b) of section 19, which deals with the subsequent employment by members of the Federal Home Loan Bank System of former employees of the Federal Home Loan Bank Board, we believe this item should be deleted from the bill. The reasons are the same as those given in earlier testimony by Mr. Norfleet Turner, when he recommended certain proposed amendments to section 217 of title 18 of the United States Code.

The bill would amend section 20, which prescribes the qualifications for examiners employed by the Federal Home Loan Bank Board, by extending these qualifications to apply to examiners under the Federal Savings and Loan Association Act and under the Federal Savings and Loan Insurance Corporation Act. Again we recommend that such provisions be placed in these acts, so that they will be where anyone looking for them would expect to find them.

Now as to the Federal savings and loan association portion of the act on page 213: Under recommendation 166F, we recommend that section 7 (e), relating to loans to officers, be replaced with the provision commonly found in savings and loan association statutes, namely, that no officer or director of a Federal savings and loan association may be directly or indirectly obligated for a mortgage loan made by the association in which he is an officer or director, other than for a first mortgage loan on a residence occupied as his own personal home.

The following statements pertain to the Federal Savings and Loan Insurance Corporation portion of the act.

Recommendation 153: We recommend that section 403 (a) be restored to the language now contained in section 402 (a), except that the number of members of the Board of Trustees be changed from 5 to 3, in conformity with the fact, to the end that the separate corporate status of the Federal Savings and Loan Insurance Corporation may be clearly maintained—a point which we have made earlier in this statement.

At page 219, in section 403 (j), the inclusion of the words "member or" might be construed to apply the provisions of this section to members of the Federal Home Loan Bank System. The national chamber believes the provisions of this section should relate only to institutions insured by the Federal Savings and Loan Insurance Corporation, and that the reference to members should be eliminated for clarity.

With respect to section 404 (c), which falls under recommendation 159, we recommend the deletion of the last two sentences—this is on page 221—because the standards to be applied by the Federal Savings and Loan Insurance Corporation are not specified and, particularly, because the authority granted might result in denying insurance of accounts to solvent and well-managed institutions.

Mr. ROGERS. Do you have any standard to suggest we put in there?

Mr. BLISS. We think that the Insurance Corporation is doing pretty well right now without a specific statement, and the language which particularly concerns us is this. It says:

> In considering applications for such insurance the Corporation shall give consideration—

among other things to—

> the need for additional insured institutions in the community, and the effect of the granting of insurance upon existing insured institutions in the community * * *

Having in mind there are 6,000 savings and loan associations in the county, of which some 3,200 or 3,300 are now insured, this language could be possibly employed to deny insurance to an existing and long-established, perfectly sound institution on the basis of some overall judgment as to the number of insured associations to be qualified in the community.

We think that is a very hazardous and dangerous authority to give to the Corporation.

Recommendation 158: We recommend that subdivisions (e) and (f) of section 404 (c), page 221, be revised to list the standards or tests to which applications for mergers will be subjected. The national chamber does not believe there is any warrant for requiring approval by the Federal Savings and Loan Insurance Corporation in mergers where liabilities of the receiving association are increased by less than 25 percent; nor that its approval should be required for the purchase or sale for cash of assets which are a legal investment for the insured association involved.

Finally, under this heading, the national chamber approves the principle set forth in recommendation 166K of the Advisory Committee that the settlement provisions of the Federal Savings and Loan Insurance Corporation Act and the Federal Deposit Insurance Corporation Act be maintained on a parity basis. Thank you.

Mr. McDONNELL. Gentlemen, that concludes the witnesses representing the United States Chamber of Commerce. May I thank you for the courteous treatment you have given us.

Senator FREAR. On behalf of the chairman, Mr. McDonnell, I assure you that the subcommittee is certainly very happy to have had you and your associates testify before the subcommittee, and very appreciative of the time and effort you have spent in preparing your testimony here today. We wish to thank you for subjecting yourself to questions by this group and also for your future assistance. It is nice to have you, and we appreciate your appearance.

Mr. McDONNELL. We thank you very much.

Senator FREAR. The committee will stand in recess until 10 a. m. tomorrow.

(Whereupon, at 11:45 a. m. the subcommittee recessed until 10 a. m. the following day, Tuesday, February 5, 1957.)

STUDY OF BANKING LAWS

(Financial Institutions Act of 1957)

TUESDAY, FEBRUARY 5, 1957

UNITED STATES SENATE,
COMMITTEE ON BANKING AND CURRENCY,
SUBCOMMITTEE ON BANKING,
Washington, D. C.

The subcommittee met, pursuant to recess, in room 301, Senate Office Building at 10:10 a. m., Senator A. Willis Robertson (chairman of the subcommittee) presiding.

Present: Senators Robertson, Monroney, Clark, Bricker, Bennett, and Bush.

Senator ROBERTSON. The subcommittee will come to order.

Our first witness today is Mr. Wallace Ely, of Rochester, N. Y., representing Robert Morris Associates.

We will be glad to hear from you.

STATEMENT OF J. WALLACE ELY, PRESIDENT, ROBERT MORRIS ASSOCIATES

Mr. ELY. I am Wallace Ely, executive vice president of the Security Trust Co., of Rochester. I appear here this morning as president of Robert Morris Associates.

May I first thank the committee for their graciousness in letting us appear to make this presentation of our thinking on this important banking matter.

I have a prepared statement which can be divided into two parts. The first part briefly summarizes the scope of the interests of the associates.

I. THE NATURE AND PURPOSES OF ROBERT MORRIS ASSOCIATES

Robert Morris Associates was conceived in June 1914, became an unincorporated association, and was incorporated as a Pennsylvania nonprofit corporation on April 19, 1921. Its central office is located in the Philadelphia National Bank Building, Philadelphia 7, Pa.

Senator ROBERTSON. I may ask you if this is named after the great Revolutionary figure?

Mr. ELY. Yes, sir, it is.

Senator ROBERTSON. He was a great money man, but unfortunately he never paid Lighthorse Harry Lee the money that Lee lent him, and that broke the Lee family.

Senator CLARK. I would like to file a comment on behalf of the Commonwealth of Pennsylvania.

Senator ROBERTSON. It is just a matter of opinion. He was a great patriot, but that is the way Robert E. Lee's family lost their colonial home down on the Rappahannock River. It was $60,000 that Light-horse Harry Lee lent to Robert Morris and he never got it back, and that was real money in those days, you know.

Senator CLARK. I am sure the Chairman will permit the record to show the pretty good taste of Robert Morris, as he had gone into it at great length, and he started this development in the State of Pennsylvania.

Senator ROBERTSON. I thought this might be an indication to this very successful financial institution named after Robert Morris, since they have tax deductions for gifts for charitable and nonprofit purposes, to make a nice contribution toward the maintenance of the Lee home that was lost by the Lee family, and now recaptured by a lot of patriotic women, and which needs contributions to keep it going.

Mr. ELY. Thank you, Senator.

May I say I believe the record shows Robert Morris lost his fortune in the financing of the Revolution.

Senator ROBERTSON. I do not question that.

Mr. ELY. The reason why the associates have chosen his name is because we felt he was a great patriot who did great work for the Revolutionary Army and was a man who put his country and his service to it before himself. We hope we are putting banking before our individual selves. That is the quick background summary of the reason why we did choose his name.

Senator ROBERTSON. I opened my comment by saying that he was a great hero and patriot, and I did not wish anything I said to be construed as an implication that he had done anything crooked when he did not repay it. It was just unfortunate from our standpoint.

Mr. ELY. Yes, sir. I can see that.

Senator CLARK. Mr. Ely, we are glad to know Robert Morris' fame has spread even to Rochester, N. Y.

Mr. ELY. It has spread much further than that, Senator.

Senator ROBERTSON. All right, sir. Without prejudice you may proceed.

Mr. ELY. Thank you.

Generally speaking, Robert Morris Associates is an organization of banks and certain related institutions which engage in the extension of credit and whose representatives in the associates are bank loan officers and credit men who are primarily or actively associated with credit work. The membership includes National and State banks and trust companies, savings banks, Federal Reserve banks, private banks and bankers, acceptance houses, commercial paper dealers and American agencies of foreign banks and trust companies located outside the United States. The organization is financed by annual dues based on a graduated schedule, according to the total resources of the respective members.

The membership of the associates comprises over 800 banks, represented in the associates by over 2,500 senior loaning officers or managers of credit departments of the member banks. There are members located in all of the several States of the United States and also in Alaska, Hawaii, and Puerto Rico. The member banks have deposits totaling approximately 80 percent of the deposits of all the banks that are members of the Federal Reserve System. Four hundred and sixty-nine national banks are members of the associates.

Among the objectives or purposes of Robert Morris Associates are the following:

1. The promotion of friendship and understanding among bank loan officers and credit men.

2. The interchange and dissemination, among members, of information concerning business and economic conditions and trends; business organization, management, functions, practices, characteristics, and problems; and other aspects of national and international economic life bearing upon the extension of credit.

3. The interchange and dissemination, among members, of information concerning loan policies, administration, techniques, and devices; legal developments affecting credit, statement analysis, credit analysis, and credit development administration practices and procedures.

II. Consideration of the Proposed Financial Institutions Act of 1957

Upon examination of the committee print bill it appears that Robert Morris Associates is particularly interested in sections 34, 35, and 36 of title I, National Bank Act. These sections I shall discuss briefly in the order named.

SECTION 34—MAXIMUM LOAN LIMITATIONS

New categories are proposed to be added to the list of loans which are now excepted from the limitation that a national bank may not lend to any 1 person more than 10 percent of the capital and 10 percent of the surplus of the bank. They are as follows:

1. Refrigerated and frozen foods (subpar. (6) (b))

Under existing law, obligations secured by documents securing title covering readily marketable staples are exempt from the 10 percent limitation. However, to qualify readily marketable staples must be nonperishable.

Under the proposed law, loans secured by refrigerated or frozen readily marketable staples are exempt provided they are fully insured, and the maximum loan to any 1 borrower does not exceed 25 prcent of the bank's capital and surplus and the maturity does not exceed 6 months.

Comment: This appears highly desirable. The frozen food market has expanded tremendously in recent years. It is a relatively simple matter to determine market prices; and the sources of outlet such as institutions, food chainstores, retailers, food brokers, wholesales, and retailers are numerous enough to enable ready liquidation. Storage and packing facilities have increased substantially and there is no reason why frozen foods should not receive the same treatment as other readily marketable staples.

2. Dairy cattle

Under existing law loans secured by liens on range animals (cattle, sheep, goats, horses, mules, etc.) are exempt from the 10 percent provision.

The proposed change would add dairy cattle to the list, provided that any such loan to any 1 dealer shall not exceed 25 percent of the bank's capital and surplus. Such obligations must carry with them the dealer's responsibility.

Comment: This change appears desirable. Certainly dairy cattle have values equivalent to other types of cattle.

3. Consumer installment-paper

Under existing law, if a bank purchases nonnegotiable consumer installment paper from a dealer and the paper is purchased on a full recourse basis, the transaction is subject to the 10 percent limitation.

Under the proposed law, obligations as endorser or guarantor of negotiable or nonnegotiable installment consumer paper carrying a full recourse endorsement or unconditional guaranty of the dealer shall be subject to a 25 percent instead of a 10 percent limitation; provided, that if an officer of the bank certifies that the bank is relying primarily upon he maker or makers (rather than upon the endorsing dealer), for the payment of the obligation, then there shall be no limitation other than the limitation of 10 percent wih respect to each maker.

Comments: The addition of nonnegotiable paper is desirable. A considerable amount of consumer installment paper is purchased not on a full recourse basis, but on a restrictive repurchaser basis under which the dealer's obligation is limited to repurchasing the repossessed goods. This type of dealer-obligation has been construed by the Comptroller to amount to a guaranty by the dealer, thus making the transaction subject to the loan limitations of this section. However, such a limited obligation of the dealer would not quality as a full recourse endorsement or unconditional guaranty and the bank would, therefore, be limited to 10 percent rather than 25 percent. These provisions should be expanded so as to include in the 25 percent limitation any dealer transaction which is subject to the general limitation provision of this section of the act, and the proviso clause should also be expanded so as to provide that it would cover all such dealer transactions.

On page 27 of the committee print the word "appreciable" in line 13 of subparagraph (12) of section 34 should read "applicable."

Mr. ROGERS. Mr. Ely, may I ask you a question?

Mr. ELY. Yes, sir.

Mr. ROGERS. At the present time on the restrictive paper you are describing here——

Mr. ELY. The repurchase paper.

Mr. ROGERS. Yes. Does the 10 percent limitation apply at the present time?

Mr. ELY. Yes. The amount of the paper which any 1 dealer could agree to repurchase would be limited to the 10 percent. However, let me point out in most of these agreements the bank could purchase from the dealer unlimited amounts which were not covered by the repurchase.

Do I make that clear?

Mr. ROGERS. No. I wish you would amplify it.

Mr. ELY. The present practical operation under repurchase involves a contract relationship between the dealer and the bank wherein the bank agrees that in order for the dealer to be liable on any repossessed paper, the bank must repossess the car and present it to the dealer.

In some cases there are maximum limits indicated to which the dealer is liable. Therefore, depending upon the individual express terms of the agreement, the amount of paper which the bank may buy from that dealer may be far in excess of any limitation, and the dealer would only have to repurchase paper which was repossessed and re-present it.

Mr. Rogers. Would you say that that type of paper represents a large proportion of the total?

Mr. Ely. Yes. I think it is a widely practiced method of operating. Have I made that clear? You did not look as though I had. I want to be sure I do.

Mr. Rogers. Yes. It is a very technical subject and I think we will want to ask the Comptroller when he comes up as to his feeling on it.

Mr. Ely. Yes. The confusing thing about it is that as a practical matter it relieves the limitation completely from the bank, but as a technical matter I believe the limitation is still there. You could not agree with the dealer that he would repurchase in excess of 10 percent.

Mr. Rogers. Thank you.

SECTION 35—MAXIMUM RATE OF INTEREST

Mr. Ely. This section, relating to maximum rate of interest permissible, contains a new clause which provides that the purchase of obligations or evidences of indebtedness from the owner shall not be deemed a loan or discount so far as interest is concerned, except to the extent they may be so construed under the laws of the State where the bank is located.

Comment: This makes it clear that in the purchase of obligations at less than par no usury can result unless by the law of the State where the bank is located. The purchase is not regarded as a loan or discount. This is obviously desirable and also equitable as the purchase, for example, of corporate bonds at less than par should never be regarded as a loan or discount, otherwise it would tend to make many obligations unsalable.

SECTION 36—REAL ESTATE LOANS

The old provision was in section 24 of the Federal Reserve Act, but as it applied only to national banks this provision is logically inserted in the new National Bank Act.

CHANGES IN EXISTING LAW

1. Leasehold loans (subpar. (a))

The existing law (sec. 24 of the Federal Reserve Act) permits loans to be made on leasehold interests, but only (*a*) if the lease is for a term not less than 99 years, which is renewable, or (*b*) if the lease has a period of 50 years to run from the date the loan is made or acquired by the bank.

The new law authorizes loans on leaseholds if the lease has at least 10 years to run after the loan matures, or if the lease may be renewed so that it will not expire for at least 10 years after the maturity date of the loan.

The proposed change would add dairy cattle to the list, provided that any such loan to any 1 dealer shall not exceed 25 percent of the bank's capital and surplus. Such obligations must carry with them the dealer's responsibility.

Comment: This change appears desirable. Certainly dairy cattle have values equivalent to other types of cattle.

3. Consumer installment-paper

Under existing law, if a bank purchases nonnegotiable consumer installment paper from a dealer and the paper is purchased on a full recourse basis, the transaction is subject to the 10 percent limitation.

Under the proposed law, obligations as endorser or guarantor of negotiable or nonnegotiable installment consumer paper carrying a full recourse endorsement or unconditional guaranty of the dealer shall be subject to a 25 percent instead of a 10 percent limitation; provided, that if an officer of the bank certifies that the bank is relying primarily upon he maker or makers (rather than upon the endorsing dealer), for the payment of the obligation, then there shall be no limitation other than the limitation of 10 percent wih respect to each maker.

Comments: The addition of nonnegotiable paper is desirable. A considerable amount of consumer installment paper is purchased not on a full recourse basis, but on a restrictive repurchaser basis under which the dealer's obligation is limited to repurchasing the repossessed goods. This type of dealer-obligation has been construed by the Comptroller to amount to a guaranty by the dealer, thus making the transaction subject to the loan limitations of this section. However, such a limited obligation of the dealer would not quality as a full recourse endorsement or unconditional guaranty and the bank would, therefore, be limited to 10 percent rather than 25 percent. These provisions should be expanded so as to include in the 25 percent limitation any dealer transaction which is subject to the general limitation provision of this section of the act, and the proviso clause should also be expanded so as to provide that it would cover all such dealer transactions.

On page 27 of the committee print the word "appreciable" in line 13 of subparagraph (12) of section 34 should read "applicable."

Mr. ROGERS. Mr. Ely, may I ask you a question?

Mr. ELY. Yes, sir.

Mr. ROGERS. At the present time on the restrictive paper you are describing here——

Mr. ELY. The repurchase paper.

Mr. ROGERS. Yes. Does the 10 percent limitation apply at the present time?

Mr. ELY. Yes. The amount of the paper which any 1 dealer could agree to repurchase would be limited to the 10 percent. However, let me point out in most of these agreements the bank could purchase from the dealer unlimited amounts which were not covered by the repurchase.

Do I make that clear?

Mr. ROGERS. No. I wish you would amplify it.

Mr. ELY. The present practical operation under repurchase involves a contract relationship between the dealer and the bank wherein the bank agrees that in order for the dealer to be liable on any repossessed paper, the bank must repossess the car and present it to the dealer.

In some cases there are maximum limits indicated to which the ... is liable. Therefore, depending upon the individual ... of the agreement, the amount of paper which the bank may ... that dealer may be far in excess of any limitation, and the ... would only have to repurchase paper which was repo... re-present it.

Mr. ROGERS. Would you say that that type of paper represents a large proportion of the total?

Mr. ELY. Yes. I think it is a widely practiced method of operat... Have I made that clear? You did not look as though I had. I ... to be sure I do.

Mr. ROGERS. Yes. It is a very technical subject and I think we ... want to ask the Comptroller when he comes up as to his feeling on ...

Mr. ELY. Yes. The confusing thing about it is that as a practical matter it relieves the limitation completely from the bank, but as a technical matter I believe the limitation is still there. You could ... agree with the dealer that he would repurchase in excess of 10 percent.

Mr. ROGERS. Thank you.

SECTION 35—MAXIMUM RATE OF INTEREST

Mr. ELY. This section, relating to maximum rate of interest permissible, contains a new clause which provides that the purchase of obligations or evidences of indebtedness from the owner shall not be deemed a loan or discount so far as interest is concerned, except to the extent they may be so construed under the laws of the State where the bank is located.

Comment: This makes it clear that in the purchase of obligations at less than par no usury can result unless by the law of the State where the bank is located. The purchase is not regarded as a loan or discount. This is obviously desirable and also equitable as the purchase, for example, of corporate bonds at less than par should never be regarded as a loan or discount, otherwise it would tend to make many obligations unsalable.

SECTION 36—REAL ESTATE LOANS

The old provision was in section 24 of the Federal Reserve Act, but as it applied only to national banks this provision is logically inserted in the new National Bank Act.

CHANGES IN EXISTING LAW

1. Leasehold loans (*subpar.* (*a*))

The existing law (sec. 24 of the Federal Reserve Act) permits loans to be made on leasehold interests, but *only* (*a*) if the lease is for a term not less than 99 years, which is *renewable*, or (*b*) if the lease has a period of 50 years to run *from the date* the loan is made or acquired by the bank.

The new law authorizes loans *on leaseholds* if the lease has at least 10 years to run after the loan *matures or* if the lease may be renewed so that it will not expire for *at least* 10 years after the maturity date of the loan.

Comment: This change would liberalize the making of loans on leasehold interests and is more realistic under present-day business practices.

2. Total amount of real estate loans (subpar. (a))

Under the existing law the aggregate of real estate loans may not exceed an amount equal to the unimpaired paid-in capital of the bank plus its unimpaired surplus, or in excess of 60 percent of its time and savings deposits, whichever is greater.

The proposed law adds a third alternative and permits loans up to 20 percent of the bank's demand deposits.

Comment: This appears desirable. As mortgages are generally on an amortization basis the privision will not tend to tie up demand moneys for an unreasonable length of time. As demand deposits do not fluctuate too widely on a long-term basis, it would appear to constitute safe banking practice.

3. Industrial and commercial construction loans (subpar. (C))

Under existing law national banks may not make loans of this type, construction loans being limited to farm and residential construction.

Under the proposed law such loans may be made to finance the construction of industrial or commercial buildings, provided the maturity does not exceed 18 months and there is a valid agreement by a financially responsible lender to advance the full amount of the bank's loan upon completion of the construction.

Comment: This appears desirable, as the experience of State banks in this field has been favorable.

4. Total amount of construction loans (subpar. (C))

Under existing law a national bank may not make construction loans in excess of 50 percent of its paid-in unimpaired capital.

Under the proposed law, a bank may lend on construction loans up to 100 percent of the bank's paid-in and unimpaired capital plus 100 percent of its unimpaired surplus.

Comment: It is submitted that the proposed increase in the permissive limit on the total amount of construction loans entails a degree of risk that suggests especial caution unless there is some additional protection, such as a requirement that a completion bond with a responsible corporate surety be furnished the bank.

Mr. ROGERS. May I ask you a question at that point?

Mr. ELY. Yes, sir.

Mr. ROGERS. Are you concerned with the construction loans for industrial and commercial purposes, or home loans, or——

Mr. ELY. I am speaking on the overall picture of the total amount of construction loans.

Mr. ROGERS. We have a provision here on construction loans for commercial and industrial purposes. There has to be a valid and binding agreement entered into by the lender to advance the full amount upon the completion of the building.

Mr. ELY. You are speaking of the take-out long-term lender?

Mr. ROGERS. Yes.

Mr. ELY. The problem which we believe bears anxious scrutiny is the possibility that the property might not be completed within the time limit or according to specifications.

Senator CLARK. And there would be no completion bond.

Mr. ELY. And if there were no completion bond——

Senator CLARK. Then the bank gets stuck.

Mr. ELY. Then the lender would be relieved of his responsibility and the bank would still have the long-term loan that it did not intend to make.

Senator CLARK. But that would be equally true under Federal law except that the restriction is more stringent.

Mr. ELY. That is true, and this particular paragraph deals with the total amount that may be so involved in these types of loans.

Senator CLARK. What restriction would you recommend?

Mr. ELY. Senator, that is a question we have thought long and hard upon and it is a hard one to answer because each bank is individual and each construction loan has its own individual problems. The limitation suggested, I believe, would be thoroughly proper in the case of a large bank that was experienced in this type of lending. I believe, however, that I would have some concern in the case of a smaller bank that had not had thorough experience in this type of lending.

Senator CLARK. Would you favor any liberalization of existing law?

Mr. ELY. Yes, I do. I think particularly in view of the fact that you are permitting construction loans to industrial and commercial concerns, you would have to think in terms of a liberalized provision in the law.

Senator MONRONEY. Does that include the FHA and the VA commitments under that category, or do they take a special category?

Mr. ELY. No, sir. I think they would be in the same category because again, if they are not completed according to specifications and time limits you would have the long-term financier relieved of his responsibility.

Senator MONRONEY. But generally you have a large number of individual housing units, at least in my part of the country, in which the commitment for the construction loan is backed up by 100 houses, you might say.

Mr. ELY. Yes.

Senator MONRONEY. Those houses represent a very small liability because the FHA or the VA have given a very definite commitment on those houses. If one happens to be bad it is an easy matter to service it and put it back into shape. However, my builders tell me that the stringency of credit very often makes it impossible to find a buyer for long-term financing, and they do not wish to be held up on the construction loan once they have found it.

Since that loan is a Government-guaranteed loan and you know an insurance company is committeed to that loan as long as it meets the not-too-difficult specifications, it seems to me it should have some more latitude than it would if you were building a $10 million office building.

Mr. ELY. Yes, sir. I do agree with that. Furthermore, in FHA construction loans that you inspect periodically, ordinarily if things are not going along properly you would have that information at hand with the least possible danger to the financier. But it would be possible for the contractor to run out of funds before he had completed and delivered in accordance with the FHA inspections.

So there does remain a real risk, although I would agree that the risk is much sounder and much less in degree than in the case of a big apartment house or office building type of construction.

Senator MONRONEY. Of course, the limitations in the act are cumulative. They include industrial plant construction loans and might run $20 million, and might include an office building, and then they get that all used up and you find this ever-increasing stringency on housing finance.

I for one am getting very worried that you are going to stall completely the whole housing operation, which took so many years to get off dead center in the early thirties. I would like to see a Government-guaranteed loan where you have a commitment from a long-term buyer given some special treatment, so that it would not be on the same basis as the large-scale industrial construction commitment.

Senator CLARK. What concerns you, Mr. Ely, is the lack of a completion bond, is it not? If you had a completion bond you would not be so concerned, would you?

Mr. ELY. That is true, or if you had a really substantial contractor. There are so many individual factors that bear on the problem that it is very difficult to generalize. I share the Senator's concern about residential housing and the feeling that it should not be throttled, but should be provided for; but some safeguards, perhaps relating the amount that could be expended on residential as distinct from commercial or industrial construction, would go part way toward answering our question.

It seems to us that some protective measures should be incorporated to make sure that the contractors' ability to perform was assured, to tie in with provisions of a takeout lender because the takeout lender is only going to take out if the building is properly built and completed within the terms.

Senator MONRONEY. But you do have a definite ironclad commitment that if the building meets inspection that this insurance company will take him out.

Mr. ELY. That is correct.

Senator MONRONEY. That is hard enough to get in today's money market. If they find that the local bank is already committed up to the limit then these fellows have to try to peddle these construction loans around in other States, and, of course, not being customers of the bank they are just told that there is no money available for them.

Mr. ELY. Senator, I trust I made it clear we were in favor of increasing the limitation. I want you to get that point.

Senator MONRONEY. I understood that, but I am wondering whether on the completely uninsured and large-scale projects, which I agree leaves the bank somewhat vulnerable providing the industrial plant might be built on the shifting sands, or some natural catastrophe happens to hold up for 6 months the completion of that construction. However, on the housing type of loan you have a diversification of the risk.

In other words, if something should happen to that contractor it would not be a catastrophe that would happen in a large-scale office building or industrial plant. Someone else could even take over without leaving the bank very badly off.

Mr. ELY. I think we are thinking along the same lines, Senator, that to some degree at least the risks are less in housing projects than they are in the other types. Therefore, I think some type of limitation which would say that you could go to 100 percent of capital on housing projects under FHA, and the other 100 percent of surplus under residential or construction-type loans would be the sort of thing I had in mind; or, you could do it by throwing in protective devices through a bonding company or some other kind of security or endorsements that are unrelated to the construction net worth. Some such protective provisions as that.

Senator MONRONEY. That is all.

Senator ROBERTSON. You may proceed.

5. Working capital loans (subpar. (C))

Mr. ELY. A new provision has been proposed which provides that loans to manufacturing and industrial businesses secured by a mortgage on the borrower's real estate shall not be considered "real-estate loans" within the meaning of the section if the bank looks for repayment out of the operations of the borrower's business, relying primarily on the borrower's general credit standing, forecast of operations with or without other security and the mortgage is taken as a precaution against contingencies.

Comment: This is an excellent provision, as it enables a bank, which would in most cases make the loan in any event, to protect itself against future adverse changes in the borrower's position. It might well be broadened to include loans to other types of business, such as merchandising and commercial.

6. Public building construction loans

A new provision is proposed which provides that loans made to finance the construction of buildings during a construction period not to exceed 36 months, upon the security of purchase contracts entered into pursuant to the Public Building Purchase Act of 1954 or the Post Office Department Property Act of 1954, shall not be subject to the provisions concerning real-estate loans.

Comment: This offers an additional field for bank loaning activity and would appear desirable if used by banks conservatively.

Senator ROBERTSON. Are there any further questions?

Senator MONRONEY. How long do those securities run?

Mr. ELY. Which securities?

Senator MONRONEY. On the Post Office and Public Buildings Purchase Act?

Mr. ELY. Not to be exceed 36 months, I believe.

Senator MONRONEY. That would be the total limitation that would be involved.

Senator ROBERTSON. We, thank you, especially for the general tenor of your remarks, which was favorable to the provisions of this bill. You think some of the lending provisions should be a little more liberal.

Mr. ELY. You see, sir, I believe the only reservation that we had was with respect to the degree of liberalization on total construction loans. Otherwise everything we have said approves thoroughly of the bill.

Senator ROBERTSON. Thank you.

Mr. ELY. And I thank you very much, sir.

Senator ROBERTSON. The next witness is Mr. John A. Adair from Kansas.

STATEMENT OF JOHN A. ADAIR, PRESIDENT, EXCHANGE NATIONAL BANK OF ATCHISON, KANS.

Mr. ADAIR. Senator, I appreciate your comments with regard to our not taking too much time. This is an awfully long speech that you see comprises 17 pages.

Senator ROBERTSON. That takes about two and a half minutes a page.

Mr. ADAIR. I will do the best I can.

First I would like to say I am here as a private individual.

Senator ROBERTSON. You have just the same right to be heard as if you represented a billion dollars.

Mr. ADAIR. Yes, sir.

Senator ROBERTSON. Your views might be better than some of the others. I cannot tell.

Mr. ADAIR. I think there are certain unique characteristics of the testimony which I will give you.

In the first place, I may allay your guessing for a moment and tell you, sir, that I am a Virginian of Virginia parentage.

Senator ROBERTSON. The Chair will not hold that against you.

Mr. ADAIR. I hope you will not hold that against me, sir. I have members of the family in business in Richmond, one of whom is Harry Augustine, whom you may know.

Senator ROBERTSON. Oh, yes. Very well.

Mr. ADAIR. President of the State Planters Bank. I want to say that especially because Mr. Augustine does not know what I am about to say, and I am certain he is a national banker and I certainly would not wish to have the Comptroller bring his house down upon him.

Senator ROBERTSON. To paraphrase, I may not endorse what you are going to say, but I will defend your right to say it—if you do not take too long.

Mr. ADAIR. Thank you, sir. I will speed up. I am going to go very quickly through a number of provisions in this situation and hope that you will not ask questions on it particularly.

Senator ROBERTSON. We will refrain from asking you questions.

Mr. ADAIR. Thank you. These relate to detailed provisions of the bill which I know you are interested in having specific comments on. Thereafter I would like to pass to the speech, if I may.

Before that I would like to say first our bank is the first bank in the Federal Reserve district to be audited by certified public accountants.

Secondly, I have had the experience of a defalcation in that bank from an employee.

Thirdly, we have had the experience of having our audit kick out a $25,000 mess of fraudulent paper.

I think in the light of that, if I overrun the time you will give me a chance to read that portion of my speech which deals with the necessity of stopping stealing in the banks, the greatest problem the banks face today, I think. There has been a failure to tackle and tangle with that problem in all of this legislation that is proposed.

First I would like to go to the bill, and in the first place I think that there is a failure to provide for proper and adequate compensation of the Comptroller. The quality of the people we have in Government stems from insufficient inducements, and the only way in which you are going to get the level of pay of the people down the line up to what it should be and attract the quality of people we are going to have to have is to start with the salary of the Comptroller. I think it has to be increased.

I am going to move over to chapter 7 of the Federal Reserve Act.

Senator ROBERTSON. I am not going to ask you a question, but just remind you of this fact: Our distinguished colleague from Oklahoma to my left helped to put through Congress a bill for uniform salaries. We do not have the control of the salaries of the Comptroller just because we have jurisdiction of national banks. That is controlled by another committee, so we did not go into that in this bill.

Mr. ADAIR. I understand, but it has a direct bearing on the quality of the supervision and management we have.

Point No. 2 is chapter 7 of the Federal Reserve Act. How in the world can you expect—and I do not mean to reflect on the quality that prevails at the present time—but how in the world can you expect to get the quality of people you need on the Federal Reserve Board when you limit the salaries to $20,000? If you go on into the salaries of the members—the heads of boards of the individual banks, which I would like to put in the record here—there is an apparent and obvious need to provide better compensation.

Here are the salaries of the presidents of the different Federal Reserve banks. I do not think that these are out of line, considering the responsibilities involved.

Senator ROBERTSON. Again I am not going to ask you a question, but I do want to comment that there are some men more interested in honor than honorariums.

Mr. ADAIR. But we cannot run a modern and one of the most important businesses in this country on the chance that they will have sufficient income to take care of honorary jobs. This is a businesslike business that we are running, and we had sure better provide the salary and income that is called for in this sort of occupation.

Senator CLARK. I assume you would favor a substantial increase in the pay of Senators and Congressmen?

Mr. ADAIR. I absolutely would, and I will tell you one of the problems in our State of Kansas stems from the fact that we do not have a level of pay that attracts the type of business leaders that we have to have in this country. The salaries of presidents of the Federal Reserve banks are these: Boston, $30,000; New York, $60,000; Philadelphia, $30,000; Cleveland, $30,000; Richmond, $30,000; Atlanta, $30,000; Chicago, $40,000; St. Louis, $30,000; Minneapolis, $28,000. I think his job up there is just as important as the man at the Federal Reserve Bank in New York. Kansas City, $30,000; Dallas, $30,000; San Francisco, $35,000.

Also I want to add I am here as a stockholder of a Federal Reserve bank of Kansas City. My wife and I own the controlling interest of this bank in Atchison, and the bank has a stock certificate which I dug out the other day and looked at for the first time, that represents an investment of $38,000. But do you know what that stock cost us, gentlemen? That stock involves the sterilization of $1 million in reserves. So that stock cost our bank $1,038,000, and I will cover that in my speech. It is worth it. Do not get me wrong. It is well worth it.

I am going to swing on over to the question of inflation. You gentlemen have had to put all sorts of emergency acts up here and you had better tie any statutory salary limit, whatever it is, to some cost-of-living index.

I will add another thing. All through your legislation you gentlemen failed to change your bonding requirements. You have had inflation in this country and you talk about a $100,000 bond back in 1913 or in 1935. It is an entirely different figure today. That is purely technical, Mr. Rogers, and I do not mean to be critical. The same thing is true of criminal penalties.

You have $1,000 criminal penalties that will encourage people, so we had better increase that figure.

While I am on that point I would like to mention the fact that the treatment that the courts are giving these people who are stealing from these banks is a major concern to this Senate in connection with this legislation. We have got to go on beyond and actually not only see that we have penalties, but do whatever is necessary to see that the penalties are brought to bear. I do not think we can continue to allow stealing from banks and then have the courts say, "My gosh, look how easy you made it to steal. Why, that poor fellow is not paid enough."

What about the bank examiners? They should have higher pay.

Take Ellenville. That thing had been going on since 1952 and it took a bright examiner to come in in 1956 and discover it had an odd smell. I do not know what kind of people had been going in there and examining that bank for those 4 years. I do not mean to be critical, as you will see when I get on. The important thing about salaries is it bears on the quality of bank examinations. If you do not start at the top and if we do not get a job done here you are not going to have the quality of people that can do the job.

I will try to be quicker.

In respect to the provisions of chapter 4, the National Banking Act, new types of capital, I think that is most desirable. I think that will have to be coupled, perhaps, with a new concept which will permit the return from corporations of some of the capital that is in there.

There are a lot of people that have money in banks and it is a problem to get it out legally. We are all familiar with that. But we have a lot of excess dollar capital actually in a number of banks. I do think preferred stock and debentures on stock options will do much for your little country bank, which is a major concern of you gentlemen, but stock options are more important to the larger banks where you have marketable stock. It is a means of providing incentives to management where there is very little opportunity for stock ownership.

Coming to section 22, in connection with dividends, I think you have a problem here when you seek to limit the dividend policy of 15,000 banks in the country. I think I would suggest to you that you differentiate between dividends in cash and "kind," for example. There are a lot of hidden equities in banks in the form of other corporate entities.

Would you prohibit the spinoff, for example, on a building corporation which would be a distribution in fact of brick and mortar? I think you differentiate between that and cash. I think you have or you may have legislation here that is designed to cure a couple of marauding situations.

The example that the Comptroller gave was one of where there had been a spinoff and apparently a substantial weakening of the bank's structure. Before you extend that to all banks, discretionary control of dividends, you should give it some further consideration.

Incidentally, in that connection, when you learn that we, in the second year of the 5-year waiting period for tax-free spinoff, do not say, "That guy has an ax to grind." Actually, our whole financial plans are predicated on the completion of creation of a separate corporation, which was short circuited by the change in the Federal tax laws of 1954.

The question of dividend limitations, I think, presents a lot of other problems, too. It is a question of definition.

As to the powers and duties of national banks, the corporate powers under chapter 6, I think you need to redo this problem of insurance on the lives of officers, which has gotten into regulatory law. There is the question of other types of insurance. There is the question of ownership of stock which may not be covered as permitted by law. The question of ownership of oil payments. The ownership of real-estate investments. Legally you might look over again the corporate powers that are involved in that section.

I would like to move on to another section, section 35, on the maximum rate of interest.

There are a lot of States in this country in which the national banks are functioning in violation of the law, actually. In the State of Kansas, as a matter of fact, the day we made our first installment loan in that State we were breaking the law and did not get it cured, or did not get it corrected, until 2 years ago. There may be a problem, and maybe it will stand some further investigation. You do not want a law requiring that banks not break laws when, as a matter of fact, they do.

On the question of bank examinations, the reason and the purpose here for the elimination of examination, gentlemen, is because they have not the people to do the job. Frankly, if we get the quality of management I think we should have—the quality of supervision—we would like to have that bank examiner around a little more frequently. That presumes he can do an effective job in helping a lot of little people in these districts that do not know this is going on.

The only way to reach them is through the American banker, but I can assure you the typical banker's desk is stacked high with good intentions and letters and periodicals that he never gets around to reading. If you get around to changing the law he is operating under, frankly, he may not know it. I would like to recommend in that connection a system of regional meetings throughout the country.

You may ask me, "Adair, what kind of man are you? Do you like to appear at public meetings?"

I went to my first meeting on the Hoover report in St. Louis 6 months ago. A gentleman from Alabama was there, by the way. The reason why I went was the possibility of putting tolls on inland-waterway shipping. We have a terrible problem in our country in providing industrialization and in the preservation of our natural resources in water. The thing that disturbed me when I went down there was the people sitting there on the other side. They were there well organized, and this involved some people who I think were—I had better hesitate in saying these things—things I am against, which is public power and a lot of other centralization and concentration of control.

The second thing that impressed me, Senator, and I hope you will be forbearing with me, was that I was given time to talk. So, having very strong feelings about this thing, I felt it might be my opportunity because I was afraid there might not be people down here to hear what I was going to say, but I knew I would be given an opportunity to talk, and also get it in the record.

On the question of the confidentiality of examination reports, gentlemen, you had better provide that your certified public accountants have access to those reports, because they have an important responsibility in the protection of our banks.

Secondly, I would like to invite your attention to the fact that there is a whole system of confidentiality that has developed within the bank-supervision system that includes material and information that is picked up from a wide variety of sources. Ninety-nine and ninety-nine one-hundredths percent of this, I am sure, is good and true, and it is important to have. But there is also evidence that misinformation can get into those confidential reports that are made by the examiners.

I was in the Navy for 4 years, gentlemen, and headed a department there. I think it was a very sound move that the Navy made when they permitted a naval officer to see his own fitness report. Somehow and by some means an individual who has been criticized should have an opportunity to be heard, and know what he is battling if there is criticism of him. That, gentlemen, is just a principle that we have got to have. I do not think it is abused.

I will be perfectly frank. We were one of those 32 banks last year that presented a problem. Nothing is wrong with us, but we are an odd duck actually. We are odd in that something should have been wrong with us, but it was not. I really would be very interested in seeing some of the information that has gotten into our report, for example, only for the purpose of eliminating things that are technically wrong.

I am going to swing over to the Federal Reserve section here, "Division of earnings."

In my opinion the earnings of the Federal Reserve banks have been derived from the member banks. There are $20 billion of reserve funds. I think those funds should be used to improve the banking system. As I am going to recommend in my speech, I think those funds should be available to pay for the cost of audits of our member banks by certified public accountants.

Secondly, we are in dire need of research. The Federal Reserve banks all over are doing a swell job in their research departments.

The study of the Federal Reserve bank, in Philadelphia, for example, relating to the ownership of banks, is tremendous. The work in agriculture is tremendous, but there is an unlimited opportunity for more research. A little bank cannot afford research, but research is the key to the future growth of our business in this country.

That is the reason why I think the big banks are concerned with it and are perfectly willing to pay this money, which is really in the nature of patronage. We have a bankers' cooperative—that is what the Federal Reserve bank is. I think the reason why the large banks are concerned about those earnings and are perfectly willing to see them go back to the Federal Government really is because they think if we started distributing these funds back to the banks, the next thing you know you would have every nonmember bank in the country wanting interest or return on his deposits with correspondents, or every nonmember bank in this country flocking to membership in the Federal Reserve System. We cannot allow that to happen in this country.

In that connection, I was shocked and surprised to find the Comptroller made a statement here some months ago that he thought it would be a good thing for all nonmember banks to ultimately join the Federal Reserve System. I should not quote him because I am sure he had some very good reasoning, and it probably did not embrace all of his thinking, but I want to go very strongly on record that I think it would be the first and greatest step toward nationalization of banks that we have ever had, if that happened.

I do not know why the banking industry should be taxed by having that money that has been made on our reserves go back to the Federal Government for roads, and for all other purposes. I just do not think it is the right concept.

On the question of the classes of directors, and I am now in chapter 4 on directors of Federal Reserve banks, class C, why should ownership of bank stock by a class C director preclude one's functioning as a director of such a bank? I just want to raise that question.

I think the recognition of the fact that the Federal Reserve agent is strictly an administrative function is fine. I was disturbed for a while to see he had to have a quality of having to be tested. I think the expression was an experienced and tested banker. We need more of those gentlemen in the Federal Reserve banks, but he is not the gentleman apparently.

On the question of removal of officers and directors, I think there needs to be a place of appeal from administrative decision before you get into the courts. I am not familiar with this Administrative Procedure Act, but we have a legal question right now, for example, with the Comptroller, which is purely technical.

We are legal now, I think, but I believe this gentleman here, Mr. Stover, says the law is one thing, and our attorneys tell us something else. There should be some administrative review. We cannot go into the courts to determine that. Some place there should be a place for review.

On the question of definition of affiliates, chapter 6, I believe that we need some further definition. This question of the stock ownership "in any other manner" leaves it entirely to administrative determination. For example the ownership of a company that is related to our bank—the control of it happens to be in my mother. My mother does not have any stock in the bank. Control of the bank is in my wife and I. The laws of attribution do not tie in my wife with my mother, but the Comptroller has an entirely different set of attributes over there. Income taxwise also.

Mr. Rogers, am I using the word "attribution" correctly? Is that correct?

Mr. Rogers. It is your testimony, sir.

Mr. Adair. I have covered chapter 7, organization and powers of the Board of Governors and their pay.

I would like to point to the fact that "no member of the Board of Governors of the Federal Reserve System shall be an officer or director of any bank, banking institution, trust company, or Federal Reserve bank, or hold stock in any bank, banking institution, or trust company."

I would like to ask why? I think there is a need for seasoned bankers in this business. Again you are going to have to provide for higher pay.

If truly the Federal Reserve banks and the Board are going to reflect some seasoned banking thinking on the banking problems, aside from the problems of controlling inflation and those other things, then I believe that we perhaps need some owner interest in banks vested in the members of that Board.

Section 42, subsection (f), relating to bank reserves, provides that member banks shall maintain the same reserves against deposits of public moneys as they are required to maintain against other deposits.

I think that is discriminatory against national banks in the State of Kansas, for example, because of the fact that public deposits are secured, and there is an exemption from the reserve requirement on those deposits. I do not think you wish to discriminate against national banks or State member banks.

Those are the technical things.

Senator, I would like to skip the first part of my prepared speech.

Senator BENNETT. Mr. Chairman, I should like just to make clear on the record that the witness has used the 30 minutes that the Chair gave him and he has not gotten to his statement.

Senator ROBERTSON. The witness seems to have a conception that he can first testify and then make a speech, but we do not divide the privileges up in that way. You can either testify or you can make a speech, but you cannot do both.

We assumed you were going to testify and put your speech in the record. Please do not read us all of your speech after testifying for 30 minutes.

Mr. ADAIR. I would not.

Senator ROBERTSON. We want to be very fair and very courteous to you, and I may assure you that there is a larger number of the committee here today to hear you than any witness previously.

Mr. ADAIR. I appreciate that.

Could I catch my topic paragraphs and read to you the one thing on defalcations? That is one thing I would like to do, if I may.

Senator ROBERTSON. You may.

Mr. ADAIR. First of all, I believe if the banking system becomes nationalized we have lost our freedom.

Secondly, as a basic concept I invite your attention to the fact that the typical bank in this country is the bank with a million and a half dollars in deposits and five employees. He is serving the farmer, gentlemen, and not in a county seat town. He is a nonmember bank and he does not have another bank in town to compete with. He is one of the problems of the revolution going on in this country, in its population and agriculture and industry. He is a public utility.

Thirdly, I would like to point out just as a concept that when this legislation was passed, gentlemen, you did not have Federal Government in the role that it is in today. The Federal Government and the Treasury Department was concerning himself with currency and money and a few things like that. Today the Treasury Department is the most important debtor of our banks, and he is the most important competitor of the banks, seeking deposits.

Then, lastly, he is responsible for our greatest expense. He collects a terrific income, over half of our earnings, or, in the case of the little banks, a third of the earnings.

I have several recommendations to make. The recommendations are these:

First, we must require at least annually unqualified audits by independent certified public accountants of all commercial banks which are members of the Federal Reserve System and Federal Deposit Insurance Corporation, to stop the terrific losses from embezzlement. That question has got to concern itself with a small bank as defined. The reason for heavy losses is money management. If you drop the price of interest on Government bond accounts you have your banks running in the red. Maybe this thing is going to go on forever.

Senator Humphrey the other day said that a continuation of the inflation and a failure to reduce taxes would give us a depression that would curl your hair. Gentlemen, if you have a few more banks in this country fail from embezzlement and you begin to develop some further operating losses in these banks, and you will have a money panic in this crisis that will make history, gentlemen.

Senator MONRONEY. For the purpose of the record, that was not Senator Humphrey, but Secretary Humphrey who said that.

Mr. ADAIR. I stand corrected.

Senator MONRONEY. I know Senator Humphrey would like to have it corrected too.

Mr. ADAIR. Excuse me. I believe it is going to take further study really to tackle the job here of the small bank. It is going to take you into the income-tax problem, and many other features.

Thirdly, I think positive banking and tax legislation must be enacted, which will encourage and facilitate the acquisition of ownership and control of the unit banks by private individuals active in the management of the banks and in the business life of the small towns and communities of this country. Legislation that would promote the regeneration of young bankers with the incentive for a private gain, which originally motivated the founders of the banks of this country, would be an epochal step forward in the economic and social history of this country, and perhaps the world.

The reorganization of the Federal income tax laws as they pertain to individuals owning bank shares, and as they pertain to banks as corporations, must necessarily be accomplished.

The best protective means a bank can have is to be owned and run by the banker that owns it. He will not be stealing from himself.

Fourth, there must be an audit of the mission and management of the several Federal bank regulatory agencies and State supervisory bodies. The purpose would be to adopt a national policy to redefine the purpose of bank supervisory industry and revitalize and adequately compensate its management. Such a program would make certain that all of the best traditions and experience and much of the authority of the office of the Comptroller of the Currency would be preserved, yet, however, transferred to a quasi-public agency such as the Federal Deposit Insurance Corporation, cooperatively owned by the banks rather than continued as a bureau of the Treasury Department, which obviously has several conflicting interests with those of banks, namely, as a borrower and debtor, as a lender and competitor for deposits, and as an income-tax collector.

You streamline the Federal Deposit Insurance Corporation and the national law, but you just have not streamlined and unified and coordinated the supervision of these banks. If you are going to keep running it with two agencies, it is all right, but not logical.

To achieve these objectives I recommend that the Banking and Currency Committee of the United States Senate assume the responsibility for the passage of enabling legislation which will result in the obtaining of appropriations designed to conduct—

(1) A thorough inventory and study of our private banking system in all of its aspects, with particular reference to the problems of the continuity of future ownership and management of banks; and

(2) An inventory and study of all of the Federal and State bank regulatory and supervisory agencies to the end that their function will be adapted to the redefined set of requirements and needs of the banking industry to insure the preservation of our private banking system and privately owned financial institutions.

It is recommended that maximum use be made of private research organizations, many of which are thoroughly experienced in economic and business research and are equipped and staffed to deal with classified or private business information.

Until such time, all contemplated changes in existing legislation should be viewed as of an interim nature, and not be allowed to establish any ultimate congressional intent.

One thing I want to read is on the problem of embezzlement.

The problem of embezzlement is the No. 1 problem of banks and of the supervisory agents, yet I have been shocked to find that it has been completely ignored in the Study of Banking Laws which includes the recommendation of the agencies. Nineteen hundred and fifty-six was a banner year in the number and dollar amount of bank embezzlements. Three situations resulted in the failure of the bank. Between January 1 and December 5, 1956, according to the Bank Shareowners Advisory League, the total of all reported embezzlements equaled $8,856,000; 23 of these exceeded $100,000; 11 embezzlements exceeded $250,000 and accounted for an aggregate loss of $6,590,000.

Here is where they were, and some of them are in your States:

West Virginia	$595,000
Pennsylvania	500,000
South Carolina	608,500
Kansas	258,000

The Kansas one broke a bank and wrecked a little community. It was a nonmember bank.

Pennsylvania	$300,000
North Carolina	826,539
Illinois	467,228
Texas	400,000

In Texas a bank was broken there.

Virginia	$300,000

Senator, you said yesterday a little restraint on temptations. I think that is a magnificent word. And checking up on people too, you should tack on to it.

Illinois	$ 934,771
New York	1,400,000

The total of those large ones is $6,590,038 in losses.

Senator MONRONEY. How much of that was tellers or other types of employees, and how much was officers?

Mr. ADAIR. I do not know, sir.

Senator MONRONEY. Was not most of it officers and bank presidents?

Mr. ADAIR. I do not know.

Senator MONRONEY. The stories I have read indicate it is the higher officers. The normal auditing procedures of the banks have caught up with most of the defalcations that are handled in a routine way.

Mr. ADAIR. I want to put in the record the summary of all those in the year.

Senator MONRONEY. I think it is good to get them all totaled together.

(The figures referred to follow:)

[American Banker, November 26, 1956]

"HAPPY" EMBEZZLEMENT DIP DIDN'T LAST LONG, 1956 MAY TOP $6 MILLION, SURVEY INDICATES

The "happy" downward turn embezzlement took last year did not last long.

An American Banker survey for the year ended September 31, indicates 1956 will be worse than the whooping $5,800,000 for calendar 1954. Survey of our news sources actually turned up $6,062,000 for the 12-month period, or close to $5,600,000 for just the first 9 months of this year.

Since there are always losses—some of them sizable—that are kept out of the press, the total figure is really larger.

American Bankers Association totals on embezzlements for first half 1956 nearly match its figures covering all of 1955. Its insurance protective committee chairman, Thomas P. Glavey, vice president of the Chase Manhattan Bank, New York, reported $3,700,000 taken in 35 losses of more than $10,000 was discovered in the 6-month period this year.

That compares with $3,900,000 for all of 1955. By the end of June last year, only 25 losses of $10,000 or more were reported, for a total of $1,500,000.

On the basis of losses so far, therefore, 1956 has a good chance of beating the 1955 record, a prospect that would set nobody cheering.

After taking a tally of 1955, the ABA was "happy to report" this May that the figure "confirms the downward trend in embezzlements." This month, the ABA wasn't picking any trends. If anything the losses looked like they were going the other way.

By comparison, the old-fashioned bank robber and burglar over the whole year ended August 31, looted banks for $1,544,000, the ABA said. Holdups dropped from 223 to 163 and burglaries from 57 to 28.

EXCESS INSURANCE PAYS OFF

The "bright side" of this year's embezzlement picture, Mr. Glavey reported, however, was that only 4 losses exceeded the amounts of fidelity insurance carried in the 1956 first half: in all 1955 there were 6.

What was new in this year's story, however, was that the idea of excess fidelity insurance, pioneered and developed by the Bank-Share Owners Advisory League, came through its baptism of fire.

League member bank, the National Bank of South Carolina, Sumter, victim of a $608,000 embezzlement discovered last May, didn't lose a dollar. Four hundred and eight thousand dollars was paid out under terms of the league policy which covers losses up to $1 million no matter when the loss started.

Losses under $10,000 are hard to gage. No agency reports them. An American Banker survey for the year through its correspondents brought out a total of $165,200. But it should be remembered, they are only the losses that are reported in the press.

Of the smaller losses under $10,000, many are never reported, or they fall into teller shorts or the familiar "mysterious disappearance." It's this type of loss that insurance men claim has soared in the postwar years and "bled" the rate up.

Expensive to track down, since most are $50 or under, the insurance firms pay, but with increasing complaints. There has been serious talk in the industry, as a result, about trying to put in a $50 deductible clause.

Though any such plan would have to buck the ABA, some of the industry hope to make it palatable by offering banks who take it a discount on their surety coverage. Others say they can't afford it—that it's either some such self-imposed deductible or a boost in rates that the bankers face.

Reported by American Banker correspondents, the list of banks hit by embezzlements over the last four quarters follows:

FOURTH QUARTER, 1955

$100,000—Bank of Ahoskie, Aulander, N. C.
$93,780—Staten Island National Bank & Trust Co., Staten Island, N. Y.
$85,601—Wichita Falls National Bank, Wichita Falls, Tex.
$38,220—Commonwealth Trust Co., Pittsburgh, Pa.
$37,000—Grace National Bank, New York, N. Y.
$24,000—Bank of Bethesda, Washington, D. C.
$22,000—First Pennsylvania Bank & Trust Co., Philadelphia, Pa.
$14,941—Davis Square Branch, Middlesex County National Bank, Sommerville, Mass.

Under $10,000:
$9,431—Bank of Fredricksburg, Richmond, Va.
$8,076—Union Market National Bank, Watertown, Md.
$6,700—Fidelity National Bank & Trust Co., Oklahoma City, Okla.
$5,681—Peoples First National Bank & Trust Co., Pittsburgh, Pa.
$5,100—Mercantile Trust Co., St. Louis, Mo.
$5,000—National Bank of Burlington, Burlington, Iowa.
$4,200—Commonwealth Trust Co., Pittsburgh, Pa.
$3,500—Farmers State Bank, Brush, Colo.
$3,200—Merchants Bank of Gallup, Gallup, La.
$2,600—First National Bank of Goshen, Goshen, Ind.
$2,000—Hudson Trust Co., Hoboken, N. J.
$1,725—National Bank of Fredricksburg, Richmond, Va.
$1,642—Commercial Bank of Lexington, Lexington, N. C.
$1,533—Second National Bank, Washington, D. C.
$1,350—Calumet National Bank, Hammond, Ind.
$1,167—Central Pennsylvania National Bank, Philadelphia, Pa.
$1,000—Teutonia Bank, Milwaukee, Wis.
$715—Whitney National Bank, New Orleans, La.
$250—First National Bank of Tarpon Springs, Tarpon Springs, Fla.

FIRST QUARTER, 1956

Over $10,000:
$595,000—Fairmont National Bank, Wheeling, W. Va.
$500,000—Girard Trust Corn Exchange Bank, Philadelphia, Pa.
$258,000—Smalon State Bank, Salina, Kans.—Failed.
$171,000—Springfield Marine Bank, Springfield, Ill.
$134,000—Commercial & Savings Bank, Santa Monica, Calif.
$75,000—Joshua Monument National Bank, Twentynine Palms, Calif.—Failed (excess over $678,000 originally reported).
$31,709—Liberty Discount & Savings Bank, Carbondale, Pa.
$22,374—Citizens State Bank, McPherson, Kans.
$19,434—First National Bank, Greeley, Colo.
$14,701—First Citizens Bank & Trust Co., Fayetteville, N. C.
$14,000—Winchester Savings Bank, Boston, Mass.
$12,479—Trade Bank & Trust Co., New York, N. Y.
$10,550—Industrial Bank of Commerce, Bronx, N. Y.

Under $10,000:

$9,762—Bank of Dahlgren, Dahlgren, Va.
$7,300—Havre de Grace Bank & Trust Co., Baltimore, Md.
$5,800—First Federal Savings & Loan Association of Shreveport, La.
$5,050—Phillipsburg Trust Co., Belvidere, N. J.
$3,354—Broad Street Trust Co., Philadelphia, Pa.
$2,000—Brotherhood State Bank, Kansas City, Kans.
$1,500—El Paso National Bank, El Paso, Tex.
$1,200—Mutual National Bank, Chicago, Ill.
$1,193—Wilkes-Barre Deposit & Savings Bank, Wilkes-Barre, Pa.
$574—Citizens National Bank (Magnolia Center branch), Riverside, Calif.
$420—Bank of St. Helens, Louisville, Ky.
$405—Dakota State Bank, Colman, S. Dak.

SECOND QUARTER 1956

Over $10,000:

$608,000—National Bank of South Carolina, Sumter.
$300,000—Girard Trust Corn Exchange Bank of Philadelphia, Pa.
$120,000—Fort Worth National Bank, Fort Worth, Tex.
$50,000—Peoples State Bank, Archbold, Ohio.
$28,231—South Carolina National Bank, Georgetown, S. C.
$25,000—Edgewater National Bank, Edgewater, N. J.
$22,774—First National Bank of Philadelphia, Pa.
$16,800—City Industrial & Savings Bank, Greensboro, N. C.
$10,000—American Bank & Trust Co., Racine, Wis.

Under $10,000:

$9,412—King George County Bank, Richmond, Va.
$9,000—Waren National Bank, Sheffield, Pa.
$7,299—Bank of Silver Spring, Silver Spring, Md.
$2,136—Security First National Bank, Los Angeles, Calif.
$2,132—Hibernia National Bank (Mid-City branch), New Orleans, La.
$1,100—St. Johns National Bank, Grand Rapids, Mich.
$930—Marine National Exchange Bank, Fort Worth, Tex.
$800—Industrial State Bank, Kalamazoo, Mich.
$701—Howard Savings Institution, Newark, N. J.
$690—First National Bank, Myrtle Beach, Fla.
$319—Peoples Bank in Zebulon, Zebulon, N. C.
$368—North Fort Worth State Bank, Fort Worth, Tex.
$360—Mechanics National Bank, Concord, N. H.
$140—First National Bank in Dallas, Dallas, Tex.

THIRD QUARTER—1956

Over $10,000:

$826,539—First-Citizens Bank & Trust Co., Kinston, N. C.
$167,228—Lawndale National Bank, Chicago, Ill.
$100,000—Farmers & Merchants Bank, Franklin, Va.
$68,000—Germantown Bank, Germantown, Md.
$50,000—Merchants & Farmers Bank, Franklin, Va.
$74,000—St. Joseph Bank & Trust Co., South Bend, Ind.
$35,000—Palo Pinto County Bank, Fort Worth, Tex.
$25,596—State & Savings Bank of Bridgeman, Bridgeman, Mich.
$22,892—Farmers Bank of Elk Creek, Roanoke, Va.
$21,000—First National Bank, Waynesburg, Pa.
$20,575—Merchandise National Bank, Chicago, Ill.
$20,000—Newton Savings Bank, Newton, Ill.
$12,340—Santa Fe National Bank, Santa Fe, N. Mex.
$10,000—First National Bank, Neenah, Wis.

Under $10,000:

- **$8,200—Bank of America, Los Angeles, Calif.**
- **$5,743—First National Bank, Niles, Mich.**
- **$3,030—Manchester Bank of St. Louis, St. Louis, Mo.**
- **$2,500—South Carolina National Bank, Charleston, S. C.**
- **$2,120—State Planters Bank of Commerce & Trusts, Richmond, Va.**
- **$1,500—International Bank of Tampa, Tampa, Fla.**
- **$750—Bank of Denver, Denver, Colo.**
- **$500—North Side Bank, Jennings, Mo.**
- **$488—Illinois National Bank, Springfield, Ill.**
- **$380—Littleton National Bank, Littleton, Colo.**
- **$350—Fort Lee Trust Co., Newark, N. J.**
- **$300—Corpus Christi National Bank, Corpus Christi, Tex.**
- **$145—Citizens & Southern National Bank, Macon, Ga.**
- **$31—State National Bank of Robstown, Robstown, Tex.**

P. S.—Have we missed any?—Editor.

Bank-Share Owners Advisory League, 33 South Clark Street, Chicago 3, Ill.—we welcome your membership and your inquiries.

Mr. Adair. I would refer the committee to some statistics available on that. Mr. Saylor of the Federal Deposit Insurance Corporation has done a very thorough job in the past of analyzing and classifying the several types of defalcation, and my impression is one of the men to watch particularly is the top man.

Senator Clark. I think quite inadvertently you read Pennsylvania in the record twice, once for $500,000 and once for $300,000. I wonder if you wanted to do that?

Mr. Adair. Yes. $300,000 for Pennsylvania. I stand corrected. No. It is in there twice. There were two situations. That is why it was read twice.

Senator Clark. That means a total of $800,000 for Pennsylvania?

Mr. Adair. No. It means the total of those I believe that were in excess of $100,000. No. I take that back. The total of those that aggregated in excess of $250,000 each.

Senator Clark. Perhaps you will clarify the record by having one figure for Pennsylvania where you have one figure for every other State?

Mr. Rogers. There are two for Illinois.

Mr. Adair. In Illinois there were two situations also. These are not figures for aggregate losses. The aggregate losses were nearly $9 billion. These cover $6½ billion.

Senator Clark. Wait a minute. Million, not billion.

Mr. Adair. Yes, sir. Inflation cannot make it that bad. I think it is significant that losses from January 1, 1953, to December 5, 1956, which is a 3-year period, aggregated $26 million, or an average annual loss of $6,546,000.

Of course, I believe the essence of supervision is to keep and preserve the capital of the banks. I invite your attention to the fact that between January 1, 1934, and 1956, there were $143 million in losses. The average annual rate was the same $6,500,000. It looks like it goes on statistically.

A reprint of the American Banker dated November 26, 1956, which carries a listing of the defalcations in the last quarter of 1955 and the first three quarters of 1956 is already in the record. This is a sickening and alarming picture, is it not?

The invisible economic losses which flow from defalcations in our commercial banks are tremendous, yet incalculable. These include lost income taxes, insurance losses, the burden of cost on the FBI and

State investigating agencies, the courts and to our penal institutions. Perhaps the worst loss is public confidence in our banks. The supervisory agencies always have an out, for printed on the bottom of each examination report of a national bank is this disclaimer. I quote:

In making this review, it should be kept in mind that an examination is not the same as an audit, and this report should not be considered to be an audit.

There is only one answer to the problem of embezzlement and defalcation. Give the audit function to private enterprise, our independent professional certified public accountants. Require an unqualified certificate, detailed definition of scope of each job, pay the accountant well, and I predict that they will get the job done at a savings to our industry and to Government. Neither the staff of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Reserve, nor State supervisors, could be expected to perform this function for which they are not especially trained.

Perhaps some legislators and certainly the public in general do not understand the difference between an examination by the bank examiners and an unqualified audit by an experienced firm of certified public accountants. Testimony can be put into the record on this matter, if the committee desires, by having testimony from a certified public accounting firm appear before the committee. The certified public accountant will insure the institution of good and uniform accounting, from which can be developed a better quality of figures, for the industry. These will assist bankers in the improvement of management techniques. An unqualified audit by a certified public accountant automatically includes tax accounting and a determination of tax liability, and corporate compliance with other law, such as usury, wage and hour and national security laws. These functions have not been properly performed by the supervisory agencies. The good certified public accountant who conducts an annual audit will, over a period of time, effect savings in taxes and reduction of operating expenses, from the institution of modern methods and systems, which will more than pay for the cost of his services.

I am certain that comes within the purview of the objectives of this committee.

The accountant's bill for audit should not be added to the banker's present costs of being regulated. The expenses are already burdensome. Here are the costs of an $11-million bank in 1956, with which I am familiar.

Senator BENNETT. We have all of those figures before us in your statement. Can they not just be put in the record?

Mr. ADAIR. I will, sir.

Senator BENNETT. That will show it.

Senator CLARK. Mr. Adair, I think we can assure you the members of this committee will give your testimony careful consideration, and perhaps we will get a chance to read it in a less hurried atmosphere.

Mr. ADAIR. Thank you. That will be all then, and I wish to say I appreciate your forbearance.

Senator ROBERTSON. You wish to have your prepared statement printed in full in the record?

Mr. ADAIR. Yes, sir.

Senator ROBERTSON. Without objection, that will be done, and if there are no other questions, we thank you.

(The prepared statement of Mr. Adair follows:)

STATEMENT OF JOHN A. ADAIR, PRESIDENT, EXCHANGE NATIONAL BANK OF ATCHISON

PREMISE

It is my understanding that:

The committee's study is limited to a consideration of legislation to (*a*) improve the basic structure of our financial system rather than (*b*) attempt to alter fundamental concepts.

The objective therefore is a constructive discussion of the issues among individuals and among organizations in the financial field.

In commencing this speech, I would like to invite the committee's attention to what I believe are fundamental concepts and premises.

First: If our banking systems become nationalized the people will have lost their freedom. The liquid portion of the wealth of the people of this Republic, either as individuals or organized for business as proprietors, partners, or as corporations, in the form of demand or savings deposits in banks and perhaps life insurance cash values is the very essence of freedom and of our capitalistic system. Any limitation whatever on the pristine right of the owner of this capital to take it down and to do with it whatsoever he might would be a threat to our system. Unrestricted access to, and the right to use, this wealth is what we mean when we say that we have a "private ownership system." The institutions in which these funds are entrusted are truly the source and the stream itself of the country's, and increasingly the world's, "credit." Wealth in this form in these financial institutions is truly an important part of the free market of private ownership. Its judgment and functioning have permitted the growth of this magnificent capitalistic system of ours which ultimately I believe will free all men in this world.

I do not mean to be too fundamental, or rather I should say elemental, but we must continuously remind ourselves that certainly two of the primary differences between our country, with its capitalistic private ownership system, and other countries is:

(*a*) Free education and a high incidence of high school and college educated people.

(*b*) The remarkable availability to, and use of, credit by the individual members of our society.

(*c*) This goes hand in hand with our unique free and privately owned financial and banking institutions.

At this point, I wish to invite your attention to some facts about our banking structure. For by being ever mindful of the nature of these institutions we can best consider modifications of Federal laws which govern the environment in which they must continue to live and breathe or wither on the vine and die. I refer to withering or death for just as some founding father once said, "The power to tax is the power to destroy," so today is it also true, "The power to regulate is the power to destroy." But more importantly I could add, "The power of constructive legislation may be the source of new life for our industry."

There were 14,247 commercial banks as of June 30, 1956. The typical bank in the Nation is comparable to the typical Kansas bank, for which I have detailed statistical data. This bank is a State bank. It is not a member of the Federal Reserve System, but it is a member of the FDIC. The bank is not in a county seat town, and it is the only bank in town. Its average deposit structure is as follows:

	Amount	Average number of accounts	Average balance per account
Time deposits	$265,000	226	$702
Demand	1,282,000	1,092	928
Total deposits	1,547,000		
Total capital, surplus and undivided	110,000		

Operating profits before taxes were $20,700, net after taxes $15,400, dividends paid to stockholders $3,600, which represented a 3.3 percent return on invested capital. This, gentlemen, is truly a picture of American small business, which will appeal particularly to Senator Sparkman of Alabama. The bank's staff is five people, 2 officers, and 3 employees. Total salaries are $20,000 an average of $4,500 per employee. It is a unique business entity; a local retail business and yet a corporation. It pays the Federal Government 30 percent of net taxable income. Comparable units are usually in proprietorship or partnership form, and probably pay less tax. These country banks are of a public-utility nature; each is vital to the proper economic functioning of its community. Their aggregate importance to the country as a whole is obvious.

The rural banks are the farmers' source of credit, and in 1954 supplied over 84 percent of all farm-production loans made by banks, production credit associations, and the Farmer's Home Administration combined for any purpose.

Certainly half of all farm equipment financed is financed by banks in contrast to dealers' and manufacturers' outlets. The rural banks have the job of financing the future mechanization of American agriculture. The rural bank is the primary source of credit for our public bodies in Kansas, particularly the small units of government. By number, 90 percent of all business loans outstanding is to small business and "most of the Midwest's bank credit for small business is extended by small rural banks."

Much of the compensation of the officers of our typical commercial bank is derived from income which does not reflect itself in bank statements of earnings. Sources are commissions on insurance and farm sales, fees as executor or trustee. Except for income from these sources, thousands of these banks would have long since been liquidated.

Second: The fundamental concept is that the Treasury Department of the United States is now the most important debtor of our banks, as well as an invincible competitor. Inevitably it must control the price it pays for money and keep rates low; correspondingly its powers are such that it can and actually is slowly but surely sucking away our deposits. This was not the case when present laws up for review were put on the statute books.

As late as 1935 when the total loans and investments of all commercial banks exceeded $30 billion, investments in Government securities amounted to less than $10 billion. This was a period of deflation when deposits and private demand for credit were low. Bank holdings of United States Governments are at a level around $55 billion at the end of 1956, while loans have climbed to over $90 billion and reflects an abnormal increase in loans occasioned by the high level of business activity and continued inflation of prices. It is only logical for this borrower to feel that his interests transcend the importance of the lender, and he is going to want to dictate his own terms notwithstanding the efforts of the Federal Reserve.

President Eisenhower, in his budget message to the Congress, has told us that "substantially lower rates on Government debt is an objective of the administration, which must be achieved in time, when he said: "Substantial reductions in interest rates cannot be expected until there is a better balance between the present pressure of heavy credit demands and the supply of savings."

But, gentlemen, if we keep on going as we are each year a few more banks will pop (and don't you think that each one of these things doesn't have its influence on public confidence), deflation will surely set in, and money rates will decline, bank earnings will drop, and this will bring a liquidation of a lot of rural banks, and this brings me to four recommendations for constructive legislation.

RECOMMENDATIONS

First: We must require, at least annually, unqualified audits by independent certified public accountants of all commercial banks which are members of the Federal Reserve System and Federal Deposit Insurance Corporation, to stop the terrific losses from embezzlement.

Second: Legislation must be passed which is designed to prevent our banks from entering a period of heavy operating losses—and I do not mean that the banking industry needs a peppercorn of subsidy. Such legislation must concern itself with the affairs and profitability of a large number, perhaps 10,000 or certainly 5,000, of the 14,000 banks in the country which have very serious problems of staying in business profitably and serving their rural communities in the uncertain years ahead. The problem, in other words, is "How best to keep our small banks profitable for bank stockholders" rather than "How to improve the laws under which regulatory agencies work to keep the banks safe for the depositors." By the latter definition our concern is primarily with 32 problem banks, according to testimony of Mr. Gidney, a few months ago, or the 7 bank cases handled by the FDIC in 1955, which were charged with unsafe or unsound banking practices or violations of law or regulation. This approach will take us nowhere. If we approach the problem capitalistically, expand the small banks' potential by eliminating the burden of Government competition and reduce their excessive tax load, the outlook for our many small banks can be profitable and favorable.

Third: Positive banking and tax legislation must be enacted which will encourage and facilitate the acquisition of ownership and control of the unit banks by private individuals active in the management of the banks and in the business life of the small towns and communities of this country. Legislation that would promote the regeneration of young bankers with the incentive for a private gain, which originally motivated the founders of the banks of this country, would be an epochal step forward in the economic and social history of this country and perhaps the world. Reorganization of Federal income tax laws as they pertain to individuals owning bank shares and as they pertain to banks as corporations must necessarily be accomplished.

Fourth: There must be an audit of the mission and management of the several Federal bank regulatory agencies and State supervisory bodies. The purpose would be to adopt a national policy to redefine the purpose of bank supervisory industry and revitalize and adequately compensate its management. Such a program would make certain that all of the best traditions and experience and much of the authority of the Office of the Comptroller of the Currency would be preserved, yet however transferred to a quasi-public agency such as the FDIC cooperatively owned by the banks rather than continued as a bureau of the Treasury Department which obviously has several conflicting interests with those of banks; namely, as a borrower and debtor, as a lender and competitor for deposits, and as an income tax collector.

Lastly, to achieve these objectives, I recommend that the Banking and Currency Committee of the United States Senate assume the responsibility for the passage of enabling legislation which will result in the obtaining of appropriations designed to conduct—

(1) A thorough inventory and study of our private banking system in all of its aspects, with particular reference to the problems of the continuity of future ownership and management of banks; and

(2) An inventory and study of all of the Federal and State bank regulatory and supervisory agencies to the end that their function will be adapted to the redefined set of requirements and needs of the banking industry to insure the preservation of our private banking system and privately owned financial institutions.

It is recommended that maximum use be made of private research organizations, many of which are thoroughly experienced in economic and business research and are equipped and staffed to deal with classified or private business information.

Until such time, all contemplated changes in existing legislation should be viewed as of an interim nature, and not be allowed to establish any ultimate congressional intent.

First. The problem of embezzlement is the No. 1 problem of banks and of the supervisory agents, yet I have been shocked to find that it has been completely ignored in the Study of Banking Laws which includes the recommendation of the agencies. 1956 was a banner year in the number and dollar amount of bank embezzlements. Three situations (*) resulted in the failure of the bank. Between January 1 and December 5, 1956, according to the Bank Shareowners Advisory League, the total of all reported embezzlements equaled $8,856,000; 23 embezzlements exceeded $100,000. 11 embezzlements exceeded $250,000, and accounted for an aggregate loss of $6,590,000. They were:

1. West Virginia	$595,000
2. Pennsylvania	500,000
3. South Carolina	608,500
4. Kansas*	258,000
5. Pennsylvania	300,000
6. North Carolina	826,539
7. Illinois	467,228
8. Texas*	400,000
9. Virginia	300,000
10. Illinois	934,771
11. New York*	1,400,000
Total	6,590,038

	Average annual loss
Losses from Jan. 1, 1953, to Dec. 5, 1956, $26,188,000	$6, 546, 000
Losses from Jan. 1, 1934, to 1956 (estimated), $143,000,000	6, 500, 000

A reprint of the American Banker dated November 26, 1956, which carries a listing of the defalcations in the last quarter of 1955 and the first three quarters of 1956 is provided for the record. This is a sickening and alarming picture, isn't it?

The invisible economic losses which flow from defalcations in our commercial banks are tremendous, yet incalculable. These include lost income taxes, insurance losses, the burden of cost on the FBI and State investigative agencies, the courts, and to our penal institutions. Perhaps the worst loss is public confidence in our banks. The supervisory agencies always have an out, for printed on the bottom of each examination report of a national bank is this disclaimer, I quote: "In making this review, it should be kept in mind that an examination is not the same as an audit, and this report should not be considered to be an audit report."

There is only one answer to the problem of embezzlement and defalcation. Give the audit function to private enterprise, our independent professional certified public accountants. Require an unqualified certificate, detailed definition of scope of each job, pay the accountant well, and I predict that they will get the job done at a savings to our industry and to government. Neither the staff of the Comptroller of the Currency, the FDIC, the Federal Reserve, nor State supervisors could be expected to perform this function for which they are not especially trained.

Now, perhaps some legislators and certainly the public in general do not understand the difference between an examination by the bank examiners and an "unqualified" audit by an experienced firm of C. P. A's. Testimony can be put into the record on this matter if the committee desires, by having testimony from a certified public accounting firm appear before the committee. The C. P. A. will insure the institution of good and uniform accounting, from which can be developed a better quality of figures for the industry. These will assist bankers in the improvement of management techniques. An unqualified audit by a C. P. A. automatically includes tax accounting and a determination of tax liability, and corporate compliance with other law, such as usury, wage and hour, and national security laws. These functions have not been properly performed by the supervisory agencies. Theg ood C. P. A. who conducts an annual audit will, over a period of time, effect savings in taxes and reduction of operating expenses, from the institution of modern methods and systems, which will more than pay for the cost of his services.

The accountant's bill for audit should not be added to the banker's present costs of being regulated. The expenses are already burdensome. Here are the costs of an $11 million bank in 1956:

Direct cost:	
Cost of FDIC insurance (net of dividend)	$4, 413
Cost of bank examination	933
Cost of fidelity bond	1, 427
Cost of audit by C. P. A.'s (percent of total)	3, 500
Cost of internal audit (operating)	2, 000
Total direct cost (4.6 percent)	12, 273
Membership in Federal Reserve System ($1,000,000 at 3 percent)	30, 000
Total expense of regulation	42, 273

The examination procedures of the bank agencies includes considerable audit work which, since it is inconclusive, represents a substantial misdirection of effort and in great measure a waste of money and time. The savings would defray a substantial portion of the cost of audits. Tax law might permit the cost of such audits to be a 100 percent credit against Federal income taxes. A credit for audit expense in the calculation of FDIC assessments of nonmember banks would be reasonable. Federal Reserve banks should absorb from profits the cost of member bank audits. The second major problem with which constructive legislation must concern itself is future bank profits.

A reduction of 1 percent of the average yield of marketable United States Government securities would cut in half (from $21,000 to $13,000) the net operating profit of the above referred to typical country bank, with $1,500,000 deposits, using its figures for the year 1955. A comparable decline in the bank's yield from loans would inevitably occur and this would reduce our typical bank's profit before taxes to $7,500. Yes, your banks in the conventional sense would commence to go broke from operating losses. The borrower, the Treasury Department, might provide a subsidy through some special issue of bonds, but no subsidized industry is free. In effect, the banking business and credit would become nationalized. A mortal blow would have been struck our capitalistic system.

Should yields rise further, many banks would technically be broke. Under present conditions, the banks become subject to stringent control of the borrower through the exercise of administrative discretion of the regulatory agencies which in the case of national banks means an office of the borrower, our United States Treasury Department. I would never suggest that this office or other regulatory agencies might exercise it improperly; certainly, however, it is a very strong medicine for a Government agency controlling finance to have around in a free enterprise country.

As national bank regulations now stand, examiners may discriminate against the credit of State and municipalities by requiring the write-off of premiums or depreciation. They may impose an entirely different set of requirements in respect to Government securities.

It is quite apparent that money management by our Federal Reserve Board has a whipsawing effect on bank profits and values, and may have produced a serious threat to the future of our entire commercial banking structure. This obviously was never the purpose of the planners and builders of our present banking system.

Under these conditions, if we are to prevent the free market of credit from becoming further dominated and controlled by the United States Treasury, it must be discouraged from banking its own debt and from competing directly for the savings and demand deposits of the public by the sale of nonmarketable Government bonds.

From the point of view of the banking system as a whole, what is the difference between the Post Office Department's sale of postal savings certificates and the Treasury Department's sales of series E, J, H and K bonds?

A thorough study should be made of the employment by the several United States Government and agency trust funds in their own and special United States or agency securities. This bootstrap operation which in 1940 involved only $7 billion of a total debt of $50 billion now involves $55 billion of a total debt of $278 billion. The only larger holder of Government debt as a class are individual investors, who own $67 billion.

Another major factor which unless stopped will contribute perhaps most to the decline in bank profits and the death of small banks is the growth in State Government banking.

In 1950 State governments had $8 billion or 13 percent of total time deposits invested in United States Government securities.

In 1956 the figure was $16 billion or 20 percent of total time deposits. This will surely result in a necessity to build a replacement mechanism in the form of an expanded Small Business Administration, Farm Credit Administration agencies, Farmers' Home Administration, and other yet unborn instrumentalities of Government who do a job which could best be done by a healthy commercial banking industry comprised of unit privately owned banks. Constructive legislation in other areas will directly improve bank profits namely:

(*a*) Permit all banks to sell credit life insurance, mortgage insurance, and insurance on all mortgaged property. The criteria limiting this authority to banks should depend upon whether other competitive lending institutions are in the business.

(*b*) Return the earnings of the Federal Reserve Banks to its members. They are derived from the earnings on the $20 billion reserve balances of member banks. To siphon these profits off to the United States Treasury imposes an additional tax, on the banks of this country, and overlooks the essence of the relationship of this banking cooperative. Such a policy would be consistent with Federal policy in respect to the Federal land banks, Federal intermediate credit banks, and banks for cooperatives.

(*c*) Increased assessment rebates or patronage refunds to the non-Federal Reserve members of the Federal Deposit Insurance Corporation. An equalization of returns to Federal Reserve members and nonmembers must be effected so that there will be no financial attraction developed which would kill our dual banking system by further increasing membership by existing banks in the Federal Reserve system.

The third problem that must be tackled now involves both positive banking and tax legislation, and it stems from the lack of equity capital in the hands of the present generation of young and middle-aged bankers who have grown up during a period of inflation, high personal income taxes, and without the benefit of a good inheritance or the good fortune of having married wealth, particularly the only daughter of a banker who owned all or a lot of his bank.

In fact, the law and regulation have both been designed to prevent many of the usual corporate, financial and tax avoidance techniques which necessarily are involved in equity acquisitions of modern corporate business. We saw in some of the recommendations of the agencies such as the proposal to control dividends and to control the investment of pension and profit-sharing plans a somewhat uncapitalistic understanding or interest in the terrific problem of helping the transfer of ownership and control of banks from the dead hands of the past to present bank management.

Gentlemen, it isn't going to happen by itself. Either chain or branch banking will inherit the problems after there has been a liquidation of thousands of small banks, if you do not get out the watering pot of capitalism "profits"—and assist the ambitious yet seasoned banker or bankers in partnership to acquire their own business. There is equity capital available for a sound economic and potentially profitable bank property. The cost, of course, is a good chance for capital gain.

Existing banking legislation has concerned itself with the dollar protection of capital, surplus, undivided profits, reserves, and fidelity insurance. In my opinion, the future of free private banking hinges more importantly on the adequacy of management capital.

Second only in importance to audits for banks as a prescription for safety is the presence of the owner-management influence on a bank.

A careful review should be made of existing tax laws in light of their effect on the continuity of owner-managers of our commercial banks. The industry if it is to be returned to health and vigor must be provided special tax benefits considerations, which would:

Exempt dividend exemptions to ownership of bank shares.
Encourage the development of pension and profit-sharing plans.
Provide for special and rapid depreciation of new buildings and equipment, most of which actually is obsolete in the light of projected bank service needs.

The corporate income-tax rate for banks with net incomes under $25,000 should be reduced. The encouragement of multiple corporate entities is a further sound means of isolating banks from risk and the unacceptable loads of income taxation. Increases in provision for bad debt reserves and new provisions for book losses in securities would appear to be reasonable.

I am very much in favor of the provision in the bill providing for bank's issuance of preferred stock and debentures, particularly if these provisions are coupled with the firm conveyance of congressional intent that capital or preferred may be issued by a bank to facilitate a revitalization of bank owner management. A debenture subordinated to the claims of depositors, deferred as to principal payments, with such only payable from earnings, would have all of the advantages of preferred stock capital, yet enjoy the advantage of interest payments being deductible for Federal income tax purposes.

The "sacred cow" of a bank now owning its stock, except building and safe deposit companies, should be changed and in this connection the hundreds of millions of dollars of hidden value in the banks in the form of such illegal assets should be given thorough airing, study, and review. In my opinion, this extends to the regulatory agencies on improper and undesirable discretionary control which is not provided for by legislation and was not the intent of Congress to convey.

The purchase by a bank of its own stock from the estate of an active officer from the proceeds of an insurance contract on his life which the corporation legally may now buy is the type of transaction that it is folly for present banking law to prohibit.

Fourth: Gentlemen, the reorganization of the supervisory agencies is going to be a terrific problem because there is right now an acute shortage of bank examiners throughout the country. Only last week, the banking editor of the

New York Times, who is now New York State superintendent of banks, pointed out that a high percentage of the examining forces are above the retirement age. The topflight career people who came into the service during the depression period and now approaching retirement cannot be counted on to stay in the service for long, and need seasoned replacements. In both State and Federal Government, it is difficult to recruit younger men for the post because they do not believe that remuneration is adequate for the responsibilities and all of the inherently unpleasant and unattractiveness of the job as it is now done. As proof of this, the 1955 Annual Report of the Chairman of the FDIC revealed that agency's personnel turnover at 14.2 percent. This situation suggests that emergency salary increases be made in the salary scale for all employees of the agencies concerned from the top down. Concurrently and immediately, a detailed management audit under the direction of this committee or the President if necessary for reference to Congress. In passing on from a discussion of this problem we must pause and take cognizance of the fact that legislation with which you are concerned overlooks the problems of the most important regulatory bodies in the country, whose problems are yours, too. These are the bank supervising agencies of our 48 States. Our dual system will absorb even greater strength if the Federal agencies will set the pace in redefining their function and assist them to obtain the money and personnel needed to do the job.

The principal of matching funds accumulated in the Federal Reserve banks or the FDIC derived from the bank's reserves or assessments should be utilized to assist the State supervisory departments. State legislatures who are committed to the principal of investing State funds in time deposits or in Government securities must be encouraged to allocate earnings from these funds for the use of the banking supervisory departments. Such earnings came from no other place than the banks.

After research has been done on the problems of all of our banks and with facts at hand as to the capabilities of the supervisory agencies, the possibilities of unification can be determined. It is reasonable to assume that the Federal Reserve banks might handle all members including national banks, and that the Federal Deposit Insurance Corporation would be responsible for State nonmember banks. Only in a country like ours could we expect to accomplish a legislative overhaul and reorganization of bureaus and agencies of this magnitude, but we can and must for our capitalistic system is at stake.

Senator ROBERTSON. The next witness is Mr. John F. Marten of Los Angeles, Calif.

Mr. Marten, we will be glad to hear from you.

STATEMENT OF JOHN F. MARTEN, PRESIDENT, GREAT WESTERN SAVINGS & LOAN ASSOCIATION, LOS ANGELES, CALIF.

Mr. MARTEN. Mr. Chairman and members of the Senate Banking and Currency Committee and Mr. Counsel, my name is John F. Marten. My business address is 4401 Crenshaw Boulevard, Los Angeles, Calif. I have been in the savings and loan and related businesses for 21 years, except for Army service time, and am now president of the Great Western Savings & Loan Association and vice president of Great Western Financial Corp. I speak for both of these organizations before you today.

All guarantee stock of Great Western Savings & Loan Association is owned by Great Western Financial Corp., as is nearly all guarantee stock of three other California savings and loan associations. Great Western Financial Corp. also owns 26 escrow companies, all operating within the State of California. None of these associations or other corporations owned by Great Western Financial Corp. has offices any place except within the State of California. While the Great Western Financial Corp. is incorporated under the laws of the State of Delaware, the four savings and loan associations and the escrow companies are all incorporated under the laws of California.

Senator BUSH. What is the definition of an escrow company?

Mr. MARTEN. Senator, they are somewhat peculiar to our southern California. They are companies that act as intermediaries to receive documents from a seller and money and incidental papers from a buyer, to act as a clearer for buyers, sellers, borrowers and lenders in real estate transactions.

Senator BENNETT. They absorb some of the functions of a trust department in a bank.

Mr. MARTEN. Yes, sir.

Senator BUSH. Did that grow up in the savings and loan business as a sort of counterpart? I mean, did they perform similar functions to those of the real estate department in a trust company?

Mr. MARTEN. Some of the functions, Senator. I might put it this way: To the best of my knowledge they only exist in the form we have them in in southern California. The title insurance companies have escrow departments, but they are not the major escrow handlers.

Senator BUSH. Does this savings and loan association, or does this escrow company, have its offices in a savings and loan association, or is it a separate entity?

Mr. MARTEN. No, because they are separate corporations and they are not in savings and loan offices.

Senator BUSH. They have their own offices?

Mr. MARTEN. Yes, sir.

Senator BUSH. They operate as separate entities?

Mr. MARTEN. Yes, sir.

Senator BUSH. Go ahead.

Mr. MARTEN. I think it might be added that banks, savings and loan associations, without exception have escrow departments. Then in addition there are these independent escrow corporations such as we have.

Senator ROBERTSON. You are a bank holding company, are you not?

Mr. MARTEN. We are a savings and loan holding company.

Senator ROBERTSON. I mean a savings and loan holding company. Are you the only one in the United States?

Mr. MARTEN. To the best of my knowledge and belief, Great Western Financial Corp. is the only one owning stock in more than one savings and loan association.

Senator ROBERTSON. So this section 409 to which you are going to address yourself in opposition affects you, but as far as you know at the present time it does not affect any other organization?

Mr. MARTEN. That is my understanding, Senator.

Senator ROBERTSON. I may say at this point that we did not get this recommendation from any Federal agency, and we did not get it from our advisory committee. The language of section 409 is the exact language of the Spence bill of last year in the House. Chairman Spence of the House Banking and Currency Committee thought that in view of the fact that we have taken action against bank holding companies, but not until after it had gotten to be almost out of hand, that it might be a good idea to be a little beforehand on a similar movement on savings and loan associations before they did get out of hand. So we inserted this provision in our bill for public comment and testimony.

We have not had any direct testimony on behalf of this legislation, but we have had an indirect endorsement in view of the fact that we have heard a number of witnesses representing savings and loan associations who did not complain. As you have pointed out, though, at the present time they were not bothered because it did not apply to them.

You are coming because it does apply to you and you do not like it.

Mr. MARTEN. Precisely.

Senator ROBERTSON. You may proceed to testify.

Senator BUSH. May I ask a question, Mr. Chairman, about this savings and loan association?

Senator ROBERTSON. Yes.

Senator BUSH. Is that a corporation?

Mr. MARTEN. Yes, Senator, it is a California corporation.

Senator BUSH. It is not a mutual operation like most of these associations in the East?

Mr. MARTEN. No, Senator, in California, like in 8 or 9 or 10 other States, we have State laws whereby all of the capital stock of the savings and loan associations——

Senator BUSH. So the financial corporation of which you are an officer owns all of the stock of this Great Western Savings and Loan Association. Is that right, sir?

Mr. MARTEN. That is correct, Senator.

Senator BUSH. Can you give me an idea as to the relationship between capital and liabilities to the depositors or shareholders? What do you call them, the people that put their savings in your place?

Mr. MARTEN. We commonly refer to them as savers. They are actually investment certificate holders.

Senator BUSH. What is the relationship between their interest in the association and the capital?

Mr. MARTEN. Let me be sure I understand you.

Senator BUSH. Well, you have so much on your statement. The savers are represented by so much in the way of deposits, or contributions, or savings, you say. How many millions of dollars is that, and how much capital is there in the business?

Mr. MARTEN. Thank you. I undestand now. We at the present time, speaking just within Great Western Savings and Loan Association, have approximately $160 million of invested savings by the public, and the underlying capital is $100,000.

Senator BUSH. Is that a capital and surplus figure?

Mr. MARTEN. No. Surplus, undivided profits and reserves altogether would add up to in excess of $11 million at the present time. There is no paid-in surplus, however.

Senator BUSH. That is all earned surplus left in the business?

Mr. MARTEN. That is correct.

Senator BUSH. So you might say the total capital funds are in the order of $11 million?

Mr. MARTEN. I do not think you would really call those capital funds, Senator. Really, the only capital is the $100,000 put in originally.

Senator BUSH. That belongs to the shareholders.

Senator BENNETT. Are those reserves for the protection of the people who have saved money, or are they for the benefit of the capital shareholders?

Mr. Marten. Those—without giving the exact figures—in excess of 90 percent of the total reserve amount of $11 million is in our so-called Federal insurance reserve, which is absolutely frozen for protection of investors. Now, should there be liquidation then those reserves would accrue to the benefit of the stockholders rather than to the savings investors.

Senator Bush. They cannot be withdrawn by the stockholders for the purpose of dividends?

Mr. Marten. No, sir. Only out of current earnings or undivided profits accumulated prior to 1951. And when and if they are paid out in dividends they would be subjected to normal taxation presently at the 52 percent rate.

Senator Bush. How do stockholders ever expect to get at that money?

Mr. Marten. It is an accumulation of wealth within the framework of the association, Senator, that there is no intent I can honestly say in our case of getting at the money.

Senator Bush. I see.

Senator Bennett. Are you talking about the 90 percent or 10 percent. You said 90 percent was a reserve for the savings investors. Does that leave 10 percent which is available to the capital shareholders for dividends?

Mr. Marten. Yes. I am happy to answer that, Senator. When Great Western Financial Corp. acquired Great Western Savings and Loan Association, there were approximately $800,000 of undivided profits accumulated prior to 1951 which could be disbursed without taxation.

Senator Bennett. I don't care about taxation. We are interested only in the question of whether they are available to the stockholders for distribution.

Mr. Marten. The only amount would be that $800,000, $400,000 of which has been disbursed. That could be paid to the parent company. So when I said 90 percent I was low. I should have said 95 or 96 percent.

Senator Bennett. You want us to understand then that your current income after you have set up your required reserves is not available for dividends for the stockholders?

Mr. Marten. Current income definitely could be paid to the stockholders in the form of dividends, but keep in mind, Senator, we are subject to the same insurance corporation—Federal Savings and Loan Insurance Corporation rules and regulations as everyone else. We must maintain our reserve ratios.

Senator Bennett. That is right.

Mr. Marten. And while we are growing we cannot possibly disburse any large percentage without jeopardizing our reserve ratio.

Senator Bennett. But you are confining your dividend payments to the funds you found in the company when you bought it?

Mr. Marten. That has been the extent of it, and we are endeavoring through the long-range point of view, through escrow companies and other entities, to earn what is needed for dividends without touching anything that is accumulated in the savings and loan associations.

Senator Bennett. Thank you, sir.

Senator Bush. When you speak of dividends you speak of stock?

Mr. Marten. In this instance, yes, Senator.

Senator BENNETT. Dividends to the controlling shareholders and not people who put money in.

Senator MONRONEY. In other words, there is no mutual interest of the so-called savers. You pay them 3 percent, or whatever the rate is, and then you are through, except the guaranty of your savings which comes out of the amount deposited in the Federal Savings and Loan Corporation.

Mr. MARTEN. That is correct.

Senator BUSH. Did you in 1956 pay any dividends to the stockholders, namely, the Great Western Financial Corp.

Mr. MARTEN. The parent corporation. Yes, sir.

Senator BUSH. How much?

Mr. MARTEN. We paid $400,000 of this $800,000 I referred to as being in there to the parent company.

Senator BRICKER. Who owns the parent company?

Mr. MARTEN. In excess of 3,700 individual stockholders, large and small, throughout the country, Senator. I just happened to check; 60.3 percent of them are in California and the rest are all over the country.

Senator ROBERTSON. You may proceed with your prepared statement.

Mr. MARTEN. Thank you, Senator.

I am also on the executive committee of, and today speak for, the savings association investors' committee. This committee, national in scope, is comprised of individuals working together in the defense of a dual system and in protection of States rights in our savings and loan business. The executive committee includes representatives from Arizona, California, Colorado, Kansas, Ohio, and Texas.

I am appearing only in opposition to Section 409; Regulation of Holding Companies, of title VI, Federal Savings and Loan Insurance Corporation Act.

First, I want very much to state our appreciation of the task which this committee is undertaking. A recodification of the financial institutions statutes is an onerous task for this committee, but one of inestimable value to the public. While, thus, I appear in opposition to the inclusion in the recodification of those new provisions which are particularly harmful to our operations, I strongly support most of the other provisions of the Financial Institutions Act of 1957.

We submit that legislation specifically affecting savings and loan holding companies should be preceded by a thorough study and analysis.

Senator ROBERTSON. May I interrupt you to say, aside from section 409, to which you object, you think it is a pretty good bill?

Mr. MARTEN. Yes. I sincerely believe that it is, Senator.

Senator ROBERTSON. Thank you.

Mr. MARTEN. Bank holding company legislation is by no means a compelling precedent. Commercial banks are stock companies. Legislation, such as the Bank Holding Company Act, which regulates the holding of stock in commercial banks, is accordingly applicable to the entire commercial banking field. But 93 percent of savings and loans, regardless of whether they have common-stock affiliates, do not themselves issue nonwithdrawable stock.

Mr. ROGERS. Is that 93 percent loaned on assets or number?

Mr. MARTEN. That is by number, and there are approximately 6,000 savings and loan associations in the United States, and approximately 400 of them are capital-stock companies.

Mr. ROGERS. Thank you.

Mr. MARTEN. By the definition of paragraph (g) of section 409, these associations, constituting 93 percent of the industry, are exempted from the regulatory effect of section 409, even though they may have the control common with affiliated-stock operations.

This is not submitted as an argument for broadening the legislation to include the rest of the industry, but rather as suggesting a lack of need for any legislation which exempts from the force of its regulation over 93 percent of the industry regulated. The fact that over half the industry, measured by assets, operates under Federal charter, and this proposed Federal statute applies only to certain State-chartered operations, and not at all to federally chartered, is also in direct contrast to the bank holding company legislation, which applies to national as well as State banks.

Senator BENNETT. Is it not true that the federally chartered institutions may not be stock companies of the type that you operate?

Mr. MARTEN. They must necessarily be mutual. That is right, Senator.

Senator BENNETT. Yes.

Mr. MARTEN. One of the principal contentions behind the bank holding company legislation was the fact that banks either directly affect or influence the volume and velocity of currency. This monetary aspect of the bank holding company legislation may be regarded as justification for Federal legislation which interferes with the operation of State laws having to do with State banks. But savings and loan associations, while they create credit, in no sense can be considered to create money as such. This basis, for Federal legislation interfering with the operation of State laws having to do with State banks, does not justify Federal legislation interfering with the operation of State laws having to do with State savings and loan associations.

We have no office outside California. All our loans are secured by California real estate. This proposed law applies to us. Nevertheless, it does not apply to the principal savings and loan operations which have offices in more than one State. Again, we feel that there is no need for regulation of this nature applicable to interstate operations. But if Federal legislation is not required to regulate interstate operations, it is certainly not needed to apply to primarily intrastate operations.

Leaving my text for just a moment, we are now subject to the Department of Justice, Federal Trade Commission, and section 7 of the Clayton Antitrust Act; also our State laws and regulations.

Should further regulation be indicated, it would seem maybe more proper for it to be imposed by our State authorities. It has been stated that the purpose of the Financial Institutions Act of 1957 was not to invade States rights. It would appear in this instance regarding savings and loan holding companies that States rights are possibly being invaded. Further, we contend that we are not restricting competition in any way by reason of having our holding company operation.

Mr. ROGERS. Mr. Marten?

Mr. MARTEN. Yes.

Mr. ROGERS. Would it be possible for your Great Western Financial Corp. to acquire savings and loan associations in other States?

Mr. MARTEN. Yes; it would be possible for us to do that. There are further reasons why bank holding company regulation is not a precedent for savings and loan holding company legislation.

The Chairman of the Board of Governors of the Federal Reserve System (84th Cong., 1st sess., U. S. Senate Banking and Currency Committee hearings, July 1955) listed control of monopoly and affiliates as the principal factors behind bank holding company legislation. These are equally two grounds on which savings and loan holding company legislation may be tested—monopoly and affiliates. The Chairman of the Board of Governors further expressed the opinion that such legislation should apply even where only one bank was involved (pp. 44–45).

However, the savings and loan holding company legislation which is now proposed attempts to exclude from the force of its regulation almost all of the savings and loan associations which have affiliates, and to limit its effect to less than 1 percent of the industry which is not dominant in any community in the country.

Clearly, then, neither of those two bases for bank holding company legislation—monopoly and affiliates—supports the proposed savings and loan holding company legislation.

But, we submit, there are strong affirmative reasons for much more thorough study before holding company legislation of this nature is enacted. Such study might well lead to the conclusion that this legislation is unnecessary.

What is the record of performance of our operations which this proposal would shackle?

The combined assets of the savings and loan associations owned by Great Western Financial Corporation exceed $240 million. Our largest California competitor, a commercial banking institution operating under 1 charter, is 40 times our size. Our total assets are less than 5 percent of the total assets of savings and loan associations located in California, and less than 1 percent of those in the Nation.

Nevertheless, we feel strongly that we are making a contribution to the welfare of our community totally disproportionate to our relative size.

Senator ROBERTSON. Let us call this the Spence bill for a second, for identification.

Mr. MARTEN. Yes, sir.

Senator ROBERTSON. You are the only holding company of this kind. That bill does not let you expand, or does not take anything away from you.

Mr. MARTEN. That is precisely correct.

Senator ROBERTSON. Does that not put you in a favored position? There could not be another like you and you are rendering fine service out in California, and there cannot be anybody who would bother you if that bill passes.

Mr. MARTEN. We have given a lot of thought to that on our board of directors and really kicked it around. We are carrying on a little errand of mercy for the capital stock companies because we do not feel it is right to have that legislation.

Senator MONRONEY. The capital stock companies want to become branch banking institutions under a savings and loan charter.

Mr. MARTEN. Could you restate that?

Senator MONRONEY. There are those capital stock companies in other States which have not gotten into branch banking and wish to become, under the guise of the savings and loan associations, branch banking institutions.

Mr. MARTEN. No; in my judgment, because as long as they are savings and loan associations they are subject to, and especially if they have insured accounts they have to stay strictly in savings and loan limits.

Senator MONRONEY. But that can get under the savings and loan guaranty to where you could establish outside of the Bank Holding Act a whole bunch of savings and loan associations, could you not, and thereby defeat the whole purpose of the Bank Holding Act?

Mr. MARTEN. I really do not see how it could happen, Senator.

Senator MONRONEY. Once they acquire enough reserves on their own to withdraw from the savings and loan insurance account, then they would be absolutely free to handle commercial and installment, or anything else, if their State charter permits.

Mr. MARTEN. Yes, but again let me speak from extensive experience, that in the West generally any association that has tried to expand and to get savings without insured accounts has found it to be quite a problem. That is a big factor today and you do not get any savings in volume without it.

Senator MONRONEY. If you have enough reserves you might be able to survive. It is not as important as it is in the commercial banking field.

Mr. MARTEN. John Q. Public thinks it is awfully important.

Senator MONRONEY. Let me ask you one more question. Under your California charter can you engage in almost any kind of banking activity?

Mr. MARTEN. No, sir. We are very strictly regulated—even more so than under the Insurance Corporation regulations as to being strictly in the savings and loan business as we know it in mutuals.

Senator MONRONEY. And in real estate loans. Is that right? You cannot have commercial loans?

Mr. MARTEN. No, sir; and taking savings from the public and making loans only on residential properties. I think we can have 5 percent of our assets in other than home loans. Nineteen fifty-six was the first full year of our operation. Only one of our savings and loan affiliates—Great Western Savings & Loan Association—was with us the full year 1956. Nineteen fifty-six was a year of shortage of money for home financing, particularly for financing of low cost homes, and above all for financing of low-cost homes for minority groups.

Nevertheless, during 1956, Great Western Savings & Loan Association translated more new savings into home financing, with one exception, than did any other single savings and loan association in the United States.

We made over $72 million of loans in 1956 on homes.

Contrary to the trend in the industry, we specialized in financing low-cost homes. And of every $8 we invested, $1 to a total of $8,600,000, was used to finance homes for minority groups.

Senator BUSH. What do you mean by "minority groups" as you use that term here?

Mr. MARTEN. I mean, Senator, Negro, Mexican, Japanese, Chinese, Korean. We have quite a large mixed population in our part of the country and it is quite a problem to finance homes for them. We happen to be the specialist in that in our part of the country.

Similar activity is indicated in 1957, and the bulk of our loan activity is in homes selling from $10,000 to $12,000.

We are proud of this record. It is in keeping with the best traditions of American private enterprise to assume the risks involved in financing home ownership of the middle and lower income groups. More than 3,700 individual and organization investors, many small and some large, have put up the risk capital for the stock of the parent company. This risk capital in turn provides the funds for ownership of the guarantee stock which enables our savings and loans to finance home ownership without risk to our savings account holders, and with diversification of the risk among all 3,700 stockholders of the parent company, no one of whom might be willing to assume this risk alone. In our opinion, our corporate and financial structure have a direct relationship to this record of achievement in a field in which many of our competitors not so organized elect not to concentrate their efforts.

I would like to add one sentence, that our parent company stands ready and able to raise capital when necessary for the assistance and support of the savings and loans, which is, let us say, a little plus that can be thrown in.

Senator BUSH. May I ask one question on that?

Mr. MARTEN. Certainly.

Senator BUSH. As to this risk capital, you say:

> This risk capital in turn provides the funds for ownership of the guarantee stock which enables our savings and loans to finance home ownership without risk to our savings account holders—

Is that true? Do you absolutely provide a nonrisk haven for those funds of your account-holders?

Mr. MARTEN. The statement is made with this thought in mind. Senator: That inasmuch as mutuals are excellent operations and doing a fine job, we contend with a capital stock type operation that that underlying capital creates an interest that these stockholders have—a real personal interest and a financial interest that they are going to go a step further toward the protection of what is there, even than a mutual might.

Senator BUSH. By your statement a little earlier you have a cushion of $10 million or something on that order on a $160 million deposit or savings. It is a nice margin of safety, but I wonder if you could say that it makes a riskless investment for the depositor?

Mr. MARTEN. Well, Senator, when we stop and analyze the records very carefully and cautiously as we are doing, I would like to agree with you 100 percent that even when you buy a Government bond there is still a certain amount of risk. There is a degree of risk.

Senator BUSH. I do not think there is a dollar's risk in a Government bond. You know there is not because you will certainly get your money. So there is no risk there. But here I cannot see how you can say it is without risk when you do have a modest reserve.

Mr. MARTEN. I will go right along wtih you and say I think you are right and qualify that to say that the risk is less than common in most savings and loan associations.

Senator BUSH. I just wanted to make sure.

Senator BENNETT. Could I inject this question? Is it not true all mutual associations also have the reserve required by the Government behind the investments of their savers?

Mr. MARTEN. Yes, they do. Senator.

Senator BENNETT. So actually the only thing you add as contrasted with the mutual type is the $100,000 plus the accumulated earnings that you found in the business when you bought it?

Mr. MARTEN. And the selfish interests of the owners to protect.

Senator BENNETT. In terms of money you have less than $1 million additional actual hard cash that is not found, or would not be found in a similar setup if it were a mutual organization?

Mr. MARTEN. That is correct, Senator.

Senator BENNETT. So in terms of added protection it is $1 million against $160 million, and what you are saying to us is that because there is a group of stockholders who have an investment in your company, that they have a greater incentive to see to it that the company does not go broke and ruin their stock ownership and that that, therefore, is something that the mutual company does not have?

Mr. MARTEN. I should have let you write my text for me.

Senator BENNETT. All right.

Senator MONRONEY. Your holding company, the Great Western Financial Corp., which is a Delaware corporation, could acquire, in any of the States permitting stock ownership of savings and loan associations, stocks in any of the existing building and loan associations in the States that permit nonmutual companies?

Mr. MARTEN. That is correct, Senator.

Senator MONRONEY. So you could expand into at least 7 or 8 other States under the holding company operation of Great Western Financial Corp.?

Mr. MARTEN. Yes, sir, we could.

Senator MONRONEY. You are not limited in your Delaware charter to California?

Mr. MARTEN. We are not limited.

Senator MONRONEY. So, consequently it is an interstate operation so far as the Great Western Financial Corp. is concerned?

Senator BENNETT. It is potentially interstate.

Senator MONRONEY. Potentially interstate.

Mr. MARTEN. Yes, sir. That is correct. Potentially.

Senator MONRONEY. So the part of your testimony that deals with the noninterstate operation exists only insofar as the company has chosen that it should?

Mr. MARTEN. That is correct.

Senator ROBERTSON. Do you have the ambition to be as large as Transamerica was before we put a little crimp in their operations last year?

Mr. MARTEN. Senator, we do not. In fact I can say that I think it was approximately 10 days ago that a very attractive offer was made to us for an association also in California, and with past acquisitions, with the problems of organization and management and everything else at the present time we were not even interested in what was a very fair price, we thought.

Senator ROBERTSON. You may proceed.

Mr. MARTEN. This subject is worthy of much study before restrictive legislation is passed. We want to cooperate in such a study. We enthusiastically support the enactment of the basic provisions of the Financial Institutions Act of 1957. But we feel that the inclusion, in this fine proposal, of the savings and loan holding company provisions is premature and that the provisions as now drafted are not in the public interest.

Thank you, gentlemen.

Senator ROBERTSON. Are there any further questions?

Thank you. This subcommittee will not be in session tomorrow. The housing subcommittee will be in session in this room tomorrow to consider, I understand, housing and maybe some other matters. Hearings before this subcommittee will be resumed at 10 o'clock on Thursday, February 7, 1957, and will be continued on Friday, at which time we will have the testimony of private witnesses.

We have had numerous requests for more appearances but unfortunately we could not grant them. We are operating sort of under a number of deadlines. The chairman of this committee graciously gave us priority but said, "You have to finish up in February. We cannot spend all of the session on just one bill."

The chairman of this subcommittee serves on 5 subcommittees of the Appropriations Committee, and those 5 handle about 95 percent of the budget. He is chairman of one subcommittee, and on the 20th of this month he has to start hearings on that, and that is a $3 billion bill in itself—Treasury and Post Office.

So, on Monday of next week, we start with the Federal witnesses in a kind of wrap-up program, so to speak. They conclude their testimony on the following Monday, the 18th. Then it is our intention to have the hearings printed.

The clerk of the full committee will furnish to every member of the committee a summary of what is in the bill. Then counsel of the subcommittee will furnish to the members a summary of what the acting chairman regards as the controversial provisions in the bill.

On February 25th the full committee will meet to vote on what goes in the official bill that we will present to the Senate.

Senator BUSH. Mr. Chairman, are you going to come to some point where you are going to have a markup session?

Senator ROBERTSON. That is the point.

Senator BUSH. That is the 25th.

Senator ROBERTSON. We finish testimony on the 18th. Then everybody gets the hearings and everybody then gets a synopsis and everybody gets an analysis of what we think are the controversial points. Then we are all supposed to be here on Monday the 25th and vote as we go down through the bill.

Senator BUSH. Section by section.

Senator ROBERTSON. Well, as we say, we will do what we call scientific reading of some—skipping over what is not objected to, and go to the heart of what the real vote is to be on, the controversial issues, although any member can make controversy out of anything he pleases, but we hope he will not make too many of them.

We hope to get this bill on the calendar by the end of this month. I read that a very distinguished Republican named Mr. Knowland said he hoped to have on the calendar by March 1 a bill known as civil rights. I have heard that there were several southern Senators who said that when that bill came up they wished to be heard.

I think it would be well for this committee, if they wish to get action completed this session over on the House side, to get our bill on the calendar by the end of this month and then ask the leaders to give us a day or two before they start in on something else. We will get this bill through because by that time we will have all the trouble ironed out and everybody will be glad to vote "aye," and we will send it on over to the House side.

That is the optimistic program of the chairman.

Without objection, we will insert at this point in the record several letters and statements which have been sent to the committee.

(The letters and statements referred to follow:)

DES MOINES 9, *January 26, 1957.*

HON. THOS. E. MARTIN,
United States Senate,
Washington, D. C.

HON. B. B. HICKENLOOPER,
United States Senate,
Washington, D. C.

MY DEAR SENATORS: It is our understanding that a bill has been submitted to Congress to do away with the present Federal Deposit Insurance Corporation Board of 3 members and to substitute 1 person for that Board.

We hope that you will oppose any such move. Thanks.

Yours very cordially and sincerely,

IOWA BANKERS ASSOCIATION,
BEN S. SUMMERWILL,
Chairman, Federal Legislative Committee.
H. C. HOUGHTON, JR.,
President.
FRANK WARNER,
Secretary.

THE ST. JOHNS NATIONAL BANK,
St. Johns, Mich., January 19, 1957.

Representative ALVIN M. BENTLEY,
House Office Building,
Washington, D. C.

DEAR REPRESENTATIVE BENTLEY: I note in various publications that recommendations are presently being prepared to revise and modernize the laws related to banking and credit institutions and that a tentative draft bill has been prepared. As I understand it, several of the provisions of the proposed bill would, first, allow the Comptroller and the Federal Reserve Board to require publication of dividend reports; second, to transfer trust powers over national banks from the Federal Reserve Board to the Comptroller.

I feel that these two provisions would be definitely detrimental to banking. The publication of dividend reports would serve no useful purpose but to create an unfriendly feeling in the bank's own community as many of our people believe that the banks, being so controlled by Government regulations already, are another Government service such as the post office. As you are well aware, we are a privately owned institution and a profit is as necessary in our business as it is in any other private business. We are much more closer controlled with regards to the use of our depositors' funds than are many union funds which, as we read in the paper, appear to be so grossly mishandled.

As a stockholder in this organization, I feel that it is my own business as to what the earnings and dividends of this bank are. A detailed breakdown is furnished our stockholders as I am sure it is furnished in all other banking institutions.

The second objection that I have is on the transfer of trust powers over national banks to the Comptroller. Approximately 5 years ago this bank was granted full trust powers on action taken by the Federal Reserve at our request because there was no organized trust company in this county, and we wished the service to be available to our customers. Our trust department is not a large department and it is more of a sevice function than a moneymaking proposition. However, we have had many requests from local citizens for this service.

The opinion of national bank examiners expressed to me many times indicates that they are not in favor of small trust departments and one indicated to me that if it had been up to the Comptroller, he doubted very much that we would have been given full trust powers because of the department's size. The proposed transfer could mean the loss to smaller communities of trust services of local competent, responsible, financial institutions. In the present period of bank mergers, it would give larger banks an unfair advantage in offering services that their local, small banks could not provide because of Government regulation.

I fully appreciate the fact that large trust companies are organized for this express purpose. However, in communities such as ours the administration of estates in some cases could go to unqualified people with results of confusion and much disatisfaction as far as errors are concerned. At the same time, what is today a small trust department can develop into a major banking service over a period of years. Anticipating what has transpired and what we read between the lines from examiners' comments, I would definitely be opposed to any action that would change the present situation in regards to the granting of trust powers for national banks.

I would be very interested in your feelings on this subject.

Respectfully,

OWENS C. TEETERS, *Cashier.*

THE LEAGUE OF TEXAS MUNICIPALITIES 1956 CONVENTION

RESOLUTION OF BANKS' UNDERWRITING REVENUE BOND ISSUES

Whereas there is needed Federal legislation which will permit national banks to underwrite and deal in nongeneral obligation or revenue bond type of public securities which are of such a quality that the banks could buy them for their own account; and

Whereas a very large percentage of the bonds of the cities of Texas which are now being issued and which will be issued in the future to provide necessary capital for many urgently needed public facilities and improvements are and will be of the nongeneral obligation and revenue type security; and

Whereas if national banks are authorized to underwrite and deal in nongeneral obligation or revenue type of municipal securities, very substantial benefits will be realized by our cities, in that the commercial banks of the country which engage in underwriting bonds issued by State and local governments have more than 30 percent of the banking capital of the Nation, which fact would make available a considerably wider market, lower interest rates, and a higher quality investment rating, in that commercial banks are subject to regulation by the State banking department, the Board of Governors of the Federal Reserve System, the Comptroller of the Currency, and the Federal Deposit Insurance Corporation; and

Whereas legislation to permit commercial bank participation in revenue bond underwriting and trading has had the approval of the United States Conference of Mayors, the American Public Power Association, representatives of the American Municipal Association, and the principle of this legislation has the approval of the legislative and administrative committees of the American Bankers Association; Now, therefore, be it

Resolved by the League of Texas Municipalities in convention assembled, That this league approve and endorse Federal legislation which will permit national banks to underwrite and deal in nongeneral obligation or revenue bond type of public securities which are of the quality that the banks could buy for their own account, and that our Senators and Representatives be respectfully urged to support such legislation; and be it further

Resolved, That copies of this resolution be furnished the United States Senators and Members of the House of Representatives from Texas.

Passed and approved at Lubbock, Tex., October 27, 1956.

Approved:

HAROLD R. DENIS, *President*.

Attest:

E. E. MCADAMS, *Executive Director*.

STATEMENT OF JOHN E. MURRAY, COMMISSIONER OF FINANCE, FOND DU LAC, WIS.

My name is John E. Murray, commissioner of the city of Fond du Lac, Wis., also finance officer of said city.

I would like to thank the Senate Banking and Currency Committee for the opportunity to present this statement. Although the subject of my statement is not now included in the bill under consideration, I have been informed your committee welcomes the chance to consider additional subjects related to the credit and banking programs within the United States. My subject concerns the need to permit commercial banks to deal and trade in public revenue bonds.

As finance officer of our city, it is my duty to arrange for the borrowing of money to finance various programs undertaken by our city. General obligation bonds floated by the city, which become a direct lien on the taxes raised by the city, have been well received and our city, having an excellent credit rating, has received bids from both banks and commercial bonding houses that have been below the average trend. However, floating revenue bonds to expand various facilities of our city, from which the bonds will be paid from the revenues produced, has met with good success.

The utilization of the revenue bond device is no longer a new concept in local government. For the last 2 years we have been attempting to float revenue bonds in connection with water utility expansion, acquisition of additional off-street parking areas, and other municipal improvements. Because of the size of our city (33,000) and because of the size of these issues, they have not been readily accepted through the normal channels. However, if our local commercial banks were allowed to underwrite such obligations, we have been assured that a much better and more attractive interest rate would be available to us. I can see that benefits can result to our State and local government because of commercial bank participation in this type of bond. First, it would broaden the market for revenue bonds and securities and thus reduce the cost of this type of public improvement. Second, it would also allow local banks to participate in local improvements watching the operation of those improvements as they progressed. Third, it would enable the banks to maintain departments capable of advising on local financing policies—advice which we, as local officials, are much in need of and must turn to local banks and bankers for sound advice.

It has been suggested that bank capital is not needed in revenue-bond financing. In support of such suggestions, it is said that there is no known instance where the lack of available dealer capital has been responsible for the abandoning of a project by a governmental authority. However, I would like to point out to your honorable committee that only as recent as 2 months ago the city of Fond du Lac had to abandon, at least for the time being, a $315,000 revenue bond for additional off-street parking spaces because the bids we received for these bonds were in excess of the safe margin that was necessary from the income that our parking lots produced. Whereas I have been reliably informed by both local banks that had they been permitted to take this issue, they would have gladly done so. They would have subscribed to it, first, because it was for local improvement. Second, because the utility was well managed and, third, because they were satisfied with the interest rate we had to offer.

I can conceivably see in the future, if municipal improvements are to continue along certain lines, that more and more we must turn to financing these improvements from revenues that are produced by the improvement. To list just a few of them that are possible in the not too far distant future:

1. Water expansion.
2. Parking lot expansion.
3. Sewer disposal expansion.
4. Highway improvement (based on gas tax).

And with the great need of additional high schools for rural areas, and vocational schools for vocational training, it is conceivable that these improvements could possibly be financed, maybe not in whole, but in part by revenues from

State-Federal aids and many other sources. In communities such as ours that are predominantly agricultural, it would work a terrific hardship on the surrounding farming areas unless we in the metropolitan areas provided junior high schools and vocational schools to train those from the rural areas about our city. All of this, gentlemen, may be a little in the future. However, it is worth, I believe, some consideration.

I wish to thank your honorable body for the opportunity of presenting this statement.

NATIONAL ASSOCIATION OF MUTUAL SAVINGS BANKS,
New York, N. Y., February 1, 1957.

DONALD ROGERS, Esq.,
Counsel, Senate Banking and Currency Committee,
Senate Office Building, Washington, D. C.

DEAR MR. ROGERS: Since Mr. William A. Lyon testified on behalf of this association last Wednesday, it has come to our attention that some ambiguity would probably result with respect to the tax status of income from Federal savings and loan shares by reenactment of the Home Owners' Loan Act of 1933, as amended, without a specific savings clause.

We have had prepared a memorandum on this subject which is enclosed with this letter.

Section 5 (g) at page 208 of the Financial Institutions Act of 1957 would reenact 12 United States Code Annotated, section 1464 (h), which gives tax exemption to the income from Federal savings and loan shares with respect to the normal tax. This exemption was removed by the enactment of section 4 of the Public Debt Act of 1941, as amended by section 6 of the Public Debt Act of 1942. If the Senate Banking and Currency Committee does not wish to reinstate the tax exemption of Federal savings and loan share income, it is recommended that a new subsection be added to section 805 of the Financial Institutions Act of 1957, at page 252, along the lines of the language contained in page 5 of the enclosed memorandum.

An examination of the statement presented to the Subcommittee on Banking by the U. S. Savings and Loan League on January 31, 1957, indicates that no recognition was given to this problem by the league spokesman.

It would be appreciated if the enclosed memorandum could be directed to the attention of the members of the Subcommittee on Banking during the current consideration of the tentative bill and be made part of the record of these hearings.

I wish to thank you again for your many courtesies to Mr. Lyon and myself.

Very truly yours,

HARRY E. PROCTOR,
Assistant General Counsel.

MEMORANDUM RE TAXABILITY OF SHARES IN FEDERAL SAVINGS AND LOAN ASSOCIATIONS

Question has arisen as to the effect of the proposed Robertson bill on the taxation of income from Federal savings and loan shares. In order to deal with this question, it is necessary to understand the history of the taxation of such income and its present status.

As part of the Home Owners' Loan Act of 1933, the organization of Federal savings and loan associations was authorized. The associations themselves were given certain exemptions from all Federal taxes and in addition it was provided: "all shares of such associations shall be exempt both as to their value and the income therefrom from all taxation (except surtaxes, estate, inheritance, and gift taxes) now or hereafter imposed by the United States * * *" (12 U. S. C. A. 1464 (h)). Thus the income from such shares was exempt from the Federal normal tax on income.

In 1941 it was decided that income on obligations of the United States should not be exempt from taxation. This intention was embodied in the Public Debt Act of 1941 (55 Stat. 7), but through apparent inadvertence, the obligations of instrumentalities of the United States were not covered. By the Public Debt Act of 1942 (56 Stat. 189), the 1941 act was amended to read:

"SEC. 4. (a) Interest upon obligations, and dividends, earnings, or other income from shares, certificates, stock, or other evidences of ownership, and gain from the sale or other disposition of such obligations and evidences of ownership issued on and after the effective date of the Public Debt Act of 1942 by the United States or any agency or instrumentality thereof shall not have any exemption, as such, and loss from the sale or other disposition of such obligations or evidences of ownership shall not have any special treatment, as such, under the Internal Revenue Code, or laws amendatory or supplementary thereto * * *."

Thus, income on Federal savings and loan shares issued after March 27, 1942, is fully subject to United States income tax. However, shares issued prior to that date continued to remain exempt from normal tax. The rules for determining the continuity of shares are somewhat complicated, see Regulations, section 1.103-2; however, basically the lowest balance since March 27, 1942, is the determining factor.

Under the 1954 Internal Revenue Code, the normal tax is the first 3 percent of the total tax otherwise determined and the surtax is the remainder (I. R. C. sec. 1 (c).

The effect of these laws on present income from a share in a Federal savings and loan association which can be traced back before March 28, 1942, is that such income is taxed at 3 percent less than other income. All income from other shares is fully taxable. A complete discussion and collection of relevant authorities on Federal taxation of this income is contained in CCH Federal Tax Service, paragraph 952.

Senator Robertson's proposed bill has not been introduced, and the only available copy at this time is a committee print dated January 7, 1957. Section 501 of this bill would reenact the Home Owners' Loan Act of 1933, as amended. As part of this reenactment, the language of section 1464 (h) quoted above, with changes not here material, would be reenacted (sec. 5, (g), p. 208).

Under familiar rules of statutory construction, this might be construed to supersede the Public Debt Act of 1942 and thus exempt from normal tax all income from Federal savings and loan association shares.

"As is true with reference to revisions, a code will likewise operate as a repeal of preexisting law, where the former covers the entire subject matter of the latter and is clearly intended by the lawmakers to be a substitute for the old law. But besides that, a code will also repeal a previous law with which it is repugnant or irreconcilably inconsistent" (Crawford, Statutory Construction p. 674).

Of course the fact that the Public Debt Act of 1942 is not mentioned in the list of statutes repealed would be an argument against such interpretation, but some risk remains. If such interpretation of repeal were accepted, all such income would receive the 3 percent reduction in rate now applied only to pre-March 28, 1942, shares.

It would probably be clear from the circumstances that Congress in adopting the Robertson bill would not intend to repeal the Public Debt Act of 1942. However, it might take litigation to establish this point, and it is not absolutely certain what the result of such litigation would be.

The Robertson bill could easily be amended to avoid any possible substantive change in the law. One route would be to amend the language of section 5 (g) to apply only to shares issued before March 28, 1942. However, since the same change should also be made in section 13 on page 196 and since the Congress will probably be disposed to interfere as little as possible with existing statutory language, we would recommend the inclusion of a specific savings clause at the end of the bill.

On the present draft, it appears that it would be appropriate to add a new subsection (e) to section 805 on page 252 reading as follows:

"Nothing in title IV or title V of this Act shall be construed to exempt from taxation income made taxable by section 4 of the Public Debt Act of 1941, as amended by section 6 of the Public Debt Act of 1942."

This language would not, of course, remove the normal tax exemption applicable to pre-March 28, 1942, shares, but there may be considerable reluctance on the part of Congress to make the Public Debt Act of 1942 retroactive as part of the Robertson bill. That act affects obligations of instrumentalities of the United States other than shares of Federal savings and loan associations.

If it proves impracticable to amend the Robertson bill as suggested above, it might be possible to have the committee report on the bill state that there is no intent to extend the exemption from normal tax to post-March 27, 1942, shares, This would probably be effective in accomplishing the aim of the suggested amendment.

INVESTMENT BANKERS ASSOCIATION OF AMERICA,
Washington, D. C., February 1, 1957.

Re Financial Institutions Act of 1957.

Hon. A. WILLIS ROBERTSON,
Chairman, Subcommittee on Banking,
Senate Committee on Banking and Currency,
Senate Office Building, Washington, D. C.

DEAR SENATOR ROBERTSON: The Investment Bankers Association of America did not request an opportunity to present testimony at the current hearings before your subcommittee on the committee print of the proposed Financial Institutions Act of 1957 because we had no comments to submit regarding the contents of the committee print. However, articles in the press today state that a witness yesterday submitted to your subcommittee a recommendation that a section be added to the proposed act to authorize national and State member banks to underwrite revenue bonds. Since our association is opposed to the proposal to authorize banks to underwrite revenue bonds, we want officially to register in the record with your subcommittee our opposition to that proposal.

Since the proposal to authorize banks to underwrite revenue bonds was submitted by the same organization at the earlier hearings by your subcommittee in November but was not included in the committee print, we assume that the subcommittee has definitely concluded not to include such a provision in the bill. Therefore, we see no need to take the time of the subcommittee to present detailed testimony in opposition to a proposal which they have already rejected. If the subcommittee should give further consideration to the proposal, we respectfully request the opportunity to present detailed testimony in opposition to that proposal.

We respectfully request that this letter be included in the record of the hearings by your subcommittee on the proposed Financial Institutions Act of 1957.

Respectfully yours,

MURRAY HANSON.

KANSAS CITY WHOLESALE CREDIT ASSOCIATION,
Kansas City, Mo., January 30, 1957.

Hon. FRANK CARLSON,
Senate Office Building,
Washington, D. C.

DEAR SENATOR: This credit association consists of 560 credit and financial departments of manufacturers, wholesalers, banks, and insurance companies, and for several years we have been making an attempt to have all banks clear their customers' checks at par. But we have never been able to secure State legislation on this matter.

The only troublesome point in Missouri is in the southeast portion, however, our members do business in States that make a practice of clipping various amounts when clearing checks for their depositors. We do not object to a bank charging their depositors for any service they render, but we do feel that when one of their depositors pay a manufacturer or jobber in the State of Missouri, this firm should receive 100 cents on a dollar, and not be penalized 10, 15, or 25 cents on each dollar.

Our entire membership is strongly in favor of passage of (title 3, sec. 26) payment of interest section of the Financial Institutions Act of 1957, and we urge your support on this legislation.

It would be appreciated if you would pass a copy of this letter to the Banking Committee members.

Sincerely yours,

J. N. HAM.

Senator ROBERTSON. The subcommittee will stand in recess until Thursday morning at 10 o'clock.

(Whereupon, at 11:55 a. m., the subcommittee recessed until 10 a. m., Thursday, February 7, 1957.)

STUDY OF BANKING LAWS

(Financial Institutions Act of 1957)

THURSDAY, FEBRUARY 7, 1957

United States Senate,
Committee on Banking and Currency,
Subcommittee on Banking,
Washington, D. C.

The subcommittee met, pursuant to recess, in room 301, Senate Office Building, at 10:00 a. m., Senator A. Willis Robertson (chairman of the subcommittee), presiding.

Present: Senators Robertson and Bennett.

Senator Robertson. The subcommittee will please come to order.

The first witness today is Mr. Fred Walker of Arlington, Va. Mr. Walker, we are glad to have you with us, and you may proceed.

STATEMENT OF FRED WALKER, DIRECTOR, FIRST NATIONAL BANK OF ARLINGTON, ARLINGTON, VA.

Mr. Walker. Thank you, Senator.

Mr. Chairman, gentlemen of the committee, I am a merchant of Arlington, Va. I am Fred Walker. I was one of the founders of First National Bank of Arlington, Arlington, Va., having represented the bank's organizing committee officially as its correspondent during its organization. I am now a director and have been so continuously since this bank was founded in 1951. I am one of its largest stockholders. I have been one of its largest stockholders from its inception.

I appeal to this committee in respectful opposition to a proposal to eliminate cumulative voting of shares of stock in the election of directors of national banking associations, unless provided for in the articles of association. In the light of my careful study, observation and experience, I oppose this proposal for the following reasons:

1. A national bank no less than any other corporation is the property of all its stockholder owners. A 49 percent minority ownership is justly entitled to a voice in the management of their investment by the same token as the 51 percent majority ownership.

2. The voice of this 49 percent ownership on the board of directors of its bank is demanded by simple justice, equity and fair play. Furthermore, it is wise and prudent (a) to exercise scrutiny and firsthand knowledge through representation on the board of how their money and that of the depositors is being used, and (b) in order to provide an exchange of ideas through a friendly discussion forum for each to weigh and consider and out of which to forge a wiser policy than would a board all of one mind.

3. Minority representation acts as a check and balance and does not permit complete one-man dictatorship of a board of directors.

4. Enactment of this proposal or recommendation removing or repealing the existing and widely used cumulative voting provision, which has proven its merit for almost a quarter century, and denying minority ownership a voice in the control of their investment would be a throwback to the horse-and-buggy era and would cause more discord, not less, as has been inferred by some proponents of this bill. It would cause more discord in the form of widespread, all-out proxy fights for complete control, because, if this proposal or recommendation is enacted, a 49 percent minority could have no voice whatsoever in the management, protection, and safeguarding of its investment without an all-out proxy fight. Such a proxy fight would itself tend to create far more discord or force the minority to resort to possibly harmful ligitation in order to protect its investment because enactment of such a proposal would remove the minority's only other alternative.

5. Moreover, the arguments advanced by some proponents of this proposal that minority representation on the board of directors will obstruct the orderly conduct of the business of the bank are as invalid and unsound as to argue that the greatest and best legislative body on earth—the Congress of the United States—should contain no minority party members whatsoever lest there be discord and obstruction of its orderly processes. A one-party system monopoly can only result in one-man dictatorship on a bank board of directors as well as in a great legislative body.

6. A minority-elected director, contrary to what has been inferred, is no more likely to improperly disclose confidential information that might tend to be imprudent or detrimental to the best interests of the bank than would a majority-elected director. In fact, less so, because for one very important reason he would, by so doing, be doing injury to his own investment to a much greater degree than does the majority director elected by management to do its bidding and dependent for election and reelection solely to management.

Let us take for a quick hypothetical illustration of the point a 5-director national bank having a $1 million capital structure of 20,000 shares selling at $50 per share.

Under the present cumulative voting dispensation, in order for a minority-elected director to be elected he must either own or be the personally chosen representative of and be held accountable for his good-management stewardship to the owners of $199,000 worth of stock in such a bank, in addition to the $1,000 stock ownership required of a director.

It is hardly likely that such a minority-elector director, owning or held personally accountable to ownership of such an investment, would disclose confidential information that might tend to be imprudent or detrimental to the best interests of the bank.

Whereas, in contrast, the management-elected puppet director need be personally accountable only to management who elected him, plus to a mere $1,000 of stock ownership required of a director.

The former is owner chosen and elected and responsible to such owners whereas the latter would be management chosen and elected and responsible solely to management.

7. Enactment of the aforesaid proposal or recommendation eliminating mandatory cumulative voting would make possible the self-

perpetuation of entrenched management and their monopoly control, even though exercise of this control may no longer be serving the best interests of the bank, its stockholders, or the public. A dictatorship-controlled, "rubber stamp" board of directors is a board that does not properly fulfill a director's oath nor does it fulfill its responsibilities as directors. This self-perpetuation of control by the majority may be accomplished in the following ways:

By management "bought" share proxies. This is done by management's utilizing the bank officers and other salaried personnel, on the bank's time, day after day, to solicit proxies for management's slate by phone, letter, and personal contact, even pressuring of borrower stockholders who are indebted to the bank, as well as bringing to bear the weight of the bank's power, prestige, and influence.

By the hiring of proxy solicitation firms, law firms, and public relations firms to wage intensive proxy solicitation campaigns at the expense of the bank and therefore, let it be noted, at the expense of minority ownership, and, moreover, all proxies so gathered to be cast, not for the two director candidate slates but rather for the management slate exclusively.

It is the duty of management to send notices of annual meetings and even with blank proxy forms attached for the shareowner to vote for his choice, but instead he is sent an already filled out proxy form with no blank for voting for other than management's proxy. In fact, only management's "proxycaster's" name is printed as an integral printed part of the management's own proxy form with no blank space left for any other. In the overwhelming majority of cases the stockholder returns management's already filled out proxy, largely because he is not usually conversant with such matters and obediently and unquestioningly signs the proxy form where the "X" appears as directed by the bank president and returns it.

Whereupon, it is then cast for the reelection exclusively of majority management's directors. Moreover, unless the stockowner should happen to be sufficiently informed regarding the proper procedure and of his rights in such matters—a large percentage of otherwise intelligent shareholders are not so informed—or if he lives in a distant city or finds it impossible to attend in person to cast his shares, he then has the choice of the following alternatives; namely, (1) not to vote his shares at all, which would redound to management's advantage, or (2) to go to the time, trouble, and expense to have printed or otherwise prepare another proxy form properly worded lest it be thrown out. Otherwise, he must endeavor to search out and find some other shareholder who must own stock in the same bank and who is going to attend in person, who is not an officer or employee of said bank, and who will agree to nominate and/or cast the proxy for a minority candidate of his own choosing who is properly qualified to become a director.

There are only a few examples of the advantages accruing to such majority in power and further illustrates how difficult it is for management to be replaced or even strengthened, no matter how justified or desirable it may be in the best interests of the bank.

Thus, management combats any efforts minority stockholders may make to replace any or all of an entrenched inefficient, moribund. or incompetent board of directors or those who may be found to have become inactive or who may not have sufficient vested interest of their own to have the bank's welfare sufficiently at heart. Often they have exhausted their credit at other banks and desire to be on the board in order to use the bank as an instrument to further their own selfish personal financial gain, by borrowing further for highly speculative investments and enterprises for which other banks have refused to extend them credit, rather than to use it as an instrumentality or institution to serve the public banking convenience and necessity and as a trustee of the public's money and to contribute to the sound, wise, and prudent stewardship as fiduciary of the investment of the bank's stockholders and of depositors' money on deposit.

In many instances these entrenched directors may have only the minimum $1,000 investment in stock required of a director and be solely concerned with the power and prestige of a national bank directorship.

8. Enactment of this proposal or recommendation would discourage investment in national bank stock by eliminating the minority director or directors from a multitude of national bank boards from coast to coast. It would, furthermore, deprive the bank of the benefits of a vigilant minority that would act as a most effective check and balance and prevent majority board management, for example, from adopting a supercilious and contemptuous attitude toward conventional tried and proven sound loan policies, policies which are based upon a wealth of cumulative loan experience gained over the years by the banking business in this country, thus eschewing experience and substituting so-called "progressive liberalized" and unsound loan policies instead.

Lester A. Pratt, an eminent and nationally recognized authority in the examining of State and national banks for 33 years and author of "Bank Frauds, Their Detection and Prevention," among other books, has frequently addressed State banking associations on the subject of bank frauds. During the past 3 or 4 years he has conducted the surveys of all the banks in the States of Iowa and Pennsylvania. The results of both these surveys were distributed to all insured banks by thhe FDIC.

This eminent authority wrote an article appearing in a banking publication, "United States Investor" on April 3, 1954, entitled "Bankers Never Die—They Just Lose Interest," from which I quote in part as follows:

> Recently there has been a suggestion made that there should be a rotation of directors as well as a rotation in the executive management. We rotate maturities in investment—why not in management? It is conceivable that a board, the individual members of which are not changed over a period of years, might avail themselves of their "oneness" and in the event of things going wrong withhold that fact from the stockholders; whereas a periodic change in the membership of the board would render this form of reticence less probable * * *
>
> * * * Unhappily, there have been some instances in the course of the past few years in which directors of banks have been guilty of conduct which would be difficult to denounce in language of sufficient emphasis * * * A board which never changes except by death or by voluntary retirement becomes self-elective, with a tendency to intellectual stagnation and impairment of business vigor.
>
> If a director becomes incompetent or ineligible by reason of age or infirmity, or any other cause, it is not only the right but the duty of shareholders to replace him * * *
>
> Where the board has become moribund, the result is usually the creation of a "one man" bank. In such a situation the principal active officer, either president or cashier, steps into the picture to dominate the situation. In other instances it may be a director who owns a controlling stock interest.

Now "one man" banks are particularly susceptible to fatal consequences as past experience has demonstrated. By reason of having uncontrolled authority and inadequate supervision by the directors, a dishonest official has uncontrolled disposition of the bank's assets over such long periods of time that the abstractions attain considerable size before they are discovered.

But it should not be inferred from this that these dominating officials are dishonest as a class. As a rule, they have rendered years of conscientious and faithful service in acquiring their position of control. But experience has shown that the most reliable of men, when exposed to the coincidence of extreme temptation and unopposed opportunity to misapply funds, may go astray, without any intention of ultimately defrauding the bank. The first step may be merely an unwise speculation with bank funds, with the object of ultimate profit to the bank rather than to the individual. Because of the risk element, the transaction is concealed from the directors. Possibly the board is so supine that no active concealment is necessary—until the speculation fails. But now there is a loss to be concealed, until restitution can be made from another "honest" speculation. Also the the bank examiner must be deceived. False entries are made. Our normally honest official has become a criminal! To the moralist there will be some difficulty in determining whether the burden of guilt rests more heavily on the officer or on his careless board of directors.

In many instances, the chief executive officer has attempted to inject new blood into the veins of the board members to revive the dying energy with new ideas; such efforts while very laudable, are not usually successful for as the Good Book states "You cannot fill old bottles with new wine." As a result, there is stagnation on the part of both the administrative and executive management, which eventually results in a merger, voluntary liquidation or disaster of the worst consequence from dishonest acts. There are many cases where the directors have left everything in the hands of the chief executive and have awakened one morning to find their bank wrecked. But it does not usually end there. As a result of their negligence they may be charged with losses which may wipe out not only their stockholding but their personal fortunes.

Enactment of the aforementioned recommendation or proposal would remove cumulative voting for directors which is the only method of voting that assures minority stockholder ownership any representation whatsoever on boards of directors, nor anyone representing their ownership to exercise scrutiny and firsthand knowledge of how their money and that of depositors is being used. Cumulative voting is necessary in order to protect economic democracy within the banking business structure of our Nation.

Economic democracy no less than political democracy is the sound and wholesome American way, with its checks and balances and giving minority stockholders in American banking a voice and representation in that which is their own, no less than political stockholders must have a voice in the political government which governs them and their property. In the absence of economic democracy, dictatorship is certain to fill the vacuum just as in government where political democracy no longer prevails. This inevitably leads to revolt bringing in its wake turbulent dire consequences as certain as night follows day.

Senator Lehman speaking as a former bank director as well as a legislator presented a forceful argument against abolishment of and conversely for mandatory cumulative voting when he said and I quote:

> Today bank boards are picked by the bank management, who select those who the management knows will be in complete accord with, and under the direction of, the management. The management will not put on a bank board anyone who it fears might differ with the philosophy or policies of the management.

As has been pointed out, the proviso clause "unless provided for in the articles of association" is completely hollow and of no real significance, inasmuch as minority ownership could not be represented on the board of directors in the management of their investment without consent of the majority management because it is self-evident that, if this inequitable and unjust proposal or recommendation should be enacted into law, then the majority management and majority alone, by reason of the fact that they are majority management, would have the sole power to exercise or not to exercise this option at their own pleasure.

I have pointed out elsewhere herein how this may be done.

Thus, entrenched majority would under this recommendation, if enacted, have the means at their disposal to perpetuate themselves in a monopoly dictatorship control. In control, let it be noted, not only of minority stock investment but of moneys and other assets deposited in national banks by the public.

There is, moreover, a rather widespread misconception that the supervision properly exercised by Federal authorities over national banks through examinations made periodically by the Federal authorities alone is a sufficient safeguard that the bank will be prudently managed and safely and soundly operated. This is not so. Though it is wise and essential, so far as it goes, it does not and in fact cannot operate the bank or take the place of sound and prudent management and, of course, does not undertake to do so, under existing law.

Lester Pratt, the eminent bank auditing authority, in the April 3, 1954, issue of the banking and investment publication, United States Investor says:

> Governmental examination of banks has for its principal purpose the appraisal of certain assets and to see whether they are complying with the law under which they operate. Consequently, the major emphasis is placed upon determining the financial condition of banks and not upon prevention of defalcations. This is evidenced by the ability of some embezzlers to cover shortages over fairly long periods, during which time several examinations may have been made, including those by directors. Often examinations by bank examiners cause shortages to be discovered, but discovery seldom occurs in the early stages of embezzlement. Most frequently, discovery by bank examiners results because the shortage has reached such proportions that the embezzler can control it no longer.

To cite briefly just one other example: National bank examiners evaluate the soundness of a loan risk on the basis of documentary evidence of the borrower's claimed assets submitted and do not under existing law undertake to investigate to ascertain whether or not such assets claimed by the borrower applicant do in fact exist. That is the sole responsibility of bank management to make such an adequate audit. Thus it may be seen that such supervision as that properly exercised by Federal authorities alone is no assurance to a 49-percent minority stockholder ownership that its investment would be adequately safeguarded by a majority management in which this minority had no representation and no voice. Such would be the case if the proposal or recommendation to abolish existing mandatory cumulative voting should be enacted into law.

Senator BENNETT. I wonder if you would not agree to put the rest of your statement into the record without reading it, Mr. Walker?

Mr. WALKER. If you like, sir.

Senator BENNETT. It will have exactly the same force and effect. You can see that most of the members of the committee are absent and will not be able to hear you read it.

Mr. WALKER. If you like, sir.

Senator BENNETT. I am very conscious of one situation we have had where a man came all the way from Utah to make a statement, and under the pressure of time he was forced to limit himself to 10 minutes and put most of his statement in the record.

I would be grateful and feel a little better in relation to my own constituent if you could give us the privilege of reading the remainder of your statement.

Mr. WALKER. I should be very glad to, sir.

Senator BENNETT. Thank you.

Senator ROBERTSON. Without objection, the witness' full statement will appear in the record as if he had delivered it in extenso.

We thank you.

Mr. WALKER. Thank you.

(The balance of Mr. Walker's prepared statement follows:)

I wish to take strong exception and to respectfully protest most vigorously to the change that has been recommended in existing banking law as proposed under item No. 21 entitled "Removed Director or Officer Voting Stock."

Any director or officer properly removed for wrongdoing should, of course, be properly punished by imprisonment, if justified, for his crime or wrongdoing in accordance with the crime committed, but he should be the one punished as in the case of any other crime; his innocent wife and/or children should not be punished for a crime that they had no part in committing by taking away their property rights, thus, to an investment in bank stock in which they have usually helped to earn the money with which said stock was purchased.

The "reasons" given for the recommendation are completely invalid; furthermore, the mythical example, cited by the proponent of the foregoing recommendation, of such a hypothetical person owning more than 50 percent of the stock of the bank being able to manage the bank through those he might theoretically be able to elect to the directorate.

Such a mythical and hypothetical instance seems so utterly unrealistic as to raise the question concerning the number of such instances anyone has ever known to occur, if indeed, any.

The writer, in addition to his having a number of years' experience as a majority-elected national bank director, had read a large number of books, monographs, and periodicals on banking, but has never heard of a single such instance as the hypothetical one cited.

In any event, furthermore, if no more valid reason for changing existing law in this matter than that put forth above exists, why was such a confiscation of property rights of stockholders as that recommended by this proponent not limited solely to such a shareholder owning more than 50 percent of a bank's outstanding shares of stock ownership, because certainly it is axiomatic that nothing less than a 51-percent vote of total shares can control a bank?

No. The proponent of this recommended change in our banking law has not made a valid case for changing existing law in this respect and such a recommended change, if it should be enacted, would be an unjust and wholly unwarranted confiscation of the already too few vested property rights of the innocent wives and children of such a hypothetical criminal.

To illustrate with an analogous figure of speech, why burn down a barn filled with priceless thoroughbred livestock on the mere hypothesis that a field mouse might conceivably exist somewhere in the cavernous reaches of the barn.

A criminal should pay by imprisonment for any wrongdoing justifying such imprisonment but his innocent wife and children should not be punished for someone else's crime.

Subject: The crying need for adequate compulsory internal audits for insured banks and the need for followthrough and enforcement by Federal authorities

The recent Illinois bank scandal, the New Jersey bank scandal, a number of very recent ones in small Maryland towns and numbers of others coast to coast have pinpointed such a need in order that the shareholding public's investment and the banking public's interests may be provided reasonable safeguards that such losses not become more and more widespread.

(1) There should be more stringent requirements in banking law to this end, whereby the Federal supervisory agencies, especially in the case of national banks, have not only the power but the stringent responsibility placed upon them to insure that their examiners' instructions and recommendations are more often complied with instead of simply ignored or accorded a contemptuous and supercilious disregard by management and with impunity.

This is done not only in the matter of "classified" (i. e., unsound or improvident loans) but in other matters pertaining to bank operations as well.

Instead of bank examiners relisting over and over, examination after examination, and year after year, the same old "classified" or improvident loans and the same old infractions, in all too many cases not corrected nor complied with by management, in addition to new ones.

In short there should be more stringent requirements in the law for followthrough by the Federal examiners to insure that bank management comply and do so with reasonable promptness.

(2) There should be not less than 2 compulsory internal audits of all FDIC-insured banks in each 12-month period. These internal audits should not be, as they now are in all too many cases, merely routine, cursory, and superficial, much too limited in scope and looked upon by management as a petty annoyance to be performed by management's handpicked committee of management-elected and management-dominated directors, only to meet the minimum letter of the law as it presently is.

There should be provisions in the banking law setting forth not only that there shall be not less than two internal audits per year but that the detailed scope of the audit should be prescribed uniformly, such, for example, as set forth by the National Association of Bank Auditors and Comptrollers as the result of an exhaustive 1955 project of the research committee of this association with headquarters at 38 South Dearborn Street, Chicago.

I have appended a copy of same herewith. (See appendix.)

It should be further set forth in banking law that if the foregoing provisions are not complied with by management in such an adequate internal audit, then the law should have provisions for requiring the examiners of the supervisory agency to have such an adequate audit made and bill the bank for same. Only in this way is provided an adequate deterrent to careless, extravagant, or fraudulent tendencies on the part of bank personnel or management.

It is no adequate answer to take the attitude, as so many bank officials do, on losses resulting from such carelessness and laxity, that the bank is insured and that thereby such losses will be recouped by the insurance underwriting agency.

It is axiomatic that the rest of the banking industry must ultimately pay for such carelessness, laxity, and indifference, in the form of increased insurance rates.

Those banks and their owners which may be operated consistent with sound banking practice, prudence, and care should not be penalized indirectly, thus, by those which are not so operated.

Governmental authorities' examination of FDIC-insured banks has for its principal purpose merely the appraisal of certain presumed or ostensible assets found in the banks' files by the governmental supervisory agencies' examiners and to ascertain whether the law, as it exists today and under which the bank presently operates, is being complied with.

Consequently, the major emphasis is placed upon determining the solvency or financial condition of the banks and not, for example, upon the prevention of defalcations. This is evidenced by the ability of some embezzlers to cover up shortages over fairly long periods during which time several examinations may have been made, by both the governmental authorities and also by the directors. The latter, all too often, is done by a management-handpicked and management-elected committee of director "puppets" who are too often disinterested and dominated by bank management on whom these "puppet" directors are solely dependent for election and reelection year after year with management-bought proxies—bought, let it be noted, at the bank's expense and therefore at the shareholder-owning public's expense.

A so-called audit by such a management-dominated committee is usually not worthy of the designation of an audit. It is usually cursory, superficial, and far too limited and inadequate in scope and barely such as to meet the minimum requirements of the letter of the inadequate provisions in this respect, of the banking law as it exists on the statute books today.

> Although often examinations by bank examiners cause shortages to be discovered, but discovery seldom occurs in the early stages of embezzlement.

says Lester A. Pratt, one of this country's most eminent bank-auditing authorities, who goes on to say—

> Most frequently, discovery by bank examiners results only because the shortage has reached such proportions that the embezzler can control it no longer.

Apropos also are the following pertinent comments on the aforementioned inadequate internal audits of insured banks as excerpted from May 2, 1955, issue of American Banker. This publication is in turn quoting an address entitled "Who Audits the Auditor," delivered by Herbert A. Wood, comptroller of the Mechanics National Bank of Worchester, Mass., at the 1955 eastern regional conference of the National Association of Bank Auditors and Comptrollers held at Scranton, Pa.

This authority had the following to say on this subject, in part:

> One of the most difficult problems facing bank directors' examining committees, particularly if no outside examination is made except those performed

by the supervisory authorities, is that the development of the audit program is delegated to the auditing committee with little followup to see that this program is sufficient and that it is properly carried out.

How many times have you heard the remark, "The auditor is only as good as the president of the bank wants him to be," or, "No one knows just what I do."

This should not be so. All other departments of the bank are examined and their systems tested to see that their operations are properly carried out.

How often is a review made with the auditor to determine (1) whether or not he is keeping up his schedules, (2) are his methods along proper audit channels, (3) could the auditor, by having so much control, be the very one to cause embarrassment to the bank.

In other words, who audits the auditor?

This responsibility is further delegated to the audit committee, whose duty it is to see that the audit functions are properly carried out.

APPENDIX

(Source: From Library of Board of Governors, Federal Reserve Bank, HG 1707 N32. Audit Program for the Smaller Bank, project of the research committee, the National Association of Bank Auditors and Comptrollers, 38 South Dearborn St., Chicago 3, Ill., copyright 1950. Ch. III, pp. 53 through 60, of the foregoing opus is entitled "Examination by Directors")

The annual or semiannual bank examinations made by examining committees or by certified public accountants at the instance of the board of directors, should cover the following suggestions:

Cash and cash items

The cash should be counted and the total compared with the books of the bank. Cash items should be scrutinized. Any improper items, such as unposted checks held for the purpose of not showing overdrafts, and other items that cannot be readily converted into cash, should be reported.

Bonds and other securities

The bonds and other securities of the bank should be examined and in every instance those not on hand should be traced. The market value and the amount at which carried on the books in the aggregate, should be shown. Any stocks held by the bank should be listed, with a statement which shows the reason the securities were taken by the bank.

Notes

The notes should be checked and their total should be compared with the general ledger. It is advisable that there be direct verification of loans mailed to borrowers together with a stamped, self-addressed envelope to be returned to the chairman of the board. The validity, value, and security of each note, and of any collateral thereto, should be determined. Any loss ascertained or probable, in the judgment of the committee, should be noted. The liabilities of each of the larger borrowers, and loans to affiliated interests, should be aggregated and considered.

The report should also show the general character of the loans; whether well distributed as to occupation of borrower and type of security so that any unfavorable conditions in one institution do not distress the bank; the general character of the collaterals; whether corporations, in which officers or directors are interested, borrow to an undue extent; and any large liabilities of the officers or directors. It should be shown whether all the paper claimed by the bank is its own property, including collaterals, is properly endorsed or assigned to it, and all mortgages recorded. Any loans exceeding the legal limit of the capital and surplus of the bank should be reported. (Look out for "colorable" loans.)

The total lines should be checked against the minute book for proper authorization. The signatures of all notemakers and endorsers should be scrutinized; any erasures and alterations or any indications of manipulation should be investigated and reported to the entire board. All overdue paper should be listed and instructions given as to definite action to be taken.

Certificates of deposit

The certificates of deposit and the cashier's checks should be verified by totaling those outstanding as shown by the register and by comparing with the general ledgers; also by comparing the canceled certificates and checks with the register and checking them against the stubs. Sequence of numbers of unissued items shoul be closely scrutinized.

Report of conditions (last call)

The copy of the report of condition made to the supervisory authority at the last call should be compared with the bank's books at that date, particularly with reference to any excessive loans and directors' and officers' liabilities reported.

Reconcilement of bank accounts

The banks's latest reconcilements of accounts with correspondent banks should be compared with the bank's books, and a transcript of the bank's account from the date of the latest reconcilement to the date of the examination should be sent to the correspondent banks with a request for verification. Balances with non-member banks in excess of the legal limit should be reported.

Individual ledgers

Individual ledger balances should be verified in such manner as the directors may deem advisable, by sending out reconcilements of certain accounts selected by the directors, or in some other suitable way. A trial balance of the ledger should be taken by some member of the committee, or at least by some person other than the clerk engaged on the ledger.

The examining committee should inquire into the arrangement for the working affairs of the bank and ascertain whether any employee who keeps the individual ledger also receives deposits or balances pass books; and whether the employees are properly bonded, and in whose custody the bonds are lodged; also whether employees are rotated from time to time.

Overdrafts

Overdrafts should be totaled and considered; the report should show any estimated losses.

Profit and loss accounts.

The committee should consider the "profit and loss" and "expense" accounts, with a view of determining whether the charges against those accounts are proper; whether the earnings of the bank warrant the expense charges; and whether the bank is making a legitimate profit.

Borrowed money

Any liability of the bank for borrowed money should be shown on the balance sheet, and the proper authority and the necessity for such borrowing ascertained. The total amount of the present liabilities of that nature should be reported to the board; the amount should include money borrowed from other banks on certificates of deposit, if any.

Securities in safekeeping

The board of directors should include in their annual examination, the verification of "Securities left for safekeeping," by direct correspondence with the customers. Since verification can be made only if there is a proper record, it is essential that adequate records of safekeeping securities be kept.

Savings accounts

Verification during a directors' examination of savings account balances, either completely or by random selection of a representative number of accounts, is recommended preferably should be by direct correspondence with the depositors.

Directors' report (in general)

The report of the directors or the examining committee should show that these points have been covered, and should recite any deficiencies discovered. The report should contain a complete statement of the total assets and liabilities of the bank with any additions or deductions that, in the judgment of the directors, should be made as a result of their investigation. A detailed statement of the loans which the directors estimate as worthless, doubtful, or insufficiently secured, should be included as should the reasons therefor, and, as nearly as possible, the real value. Carrying values of all assets should be discussed, with resultant recommendations.

A statement of any matters which, in the opinion of the committee, affect in any way the bank's solvency, stability, or prosperity should be made.

84444—57—pt. 2——19

A thorough, complete examination at least once a year, by a committee of the directors cannot fail to be of great benefit. The directors owe such examinations to the shareholders who have placed them in positions of trust.

A complete report of each examination should be preserved in the files of the bank and should be made available to the bank examiner.

GENERAL OUTLINE OF REPORT

(Examining committee, banking department)

1. Letter of transmittal to board of directors.
2. Ownership and management schedule by name:
  (a) Stockholders
  (b) Directors
  (c) Committees of the board
  (d) Officers
3. Statement of condition (condensed and comparative).
4. Statement of condition (general ledger controls as of date of examination).
5. Comments on resources (in order of general ledger accounts).
6. Schedules:
  (a) Attorneys accounts.
  (b) Claim accounts.
  (c) Direct and indirect liability of officers, directors, employees, and/or members of their families, and/or firms in which any of the foregoing have a vested interest.
  (d) Past due loans
  (e) Overdrafts
  (f) Investment securities (par, book, market)
  (g) Cash due from banks
  (h) Cash items
  (i) Furniture and fixtures (classification)
  (j) Suspense account
  (k) Other resources
7. Cash and cash items (schedule by tellers, by kinds of money held)
8. Comments on liabilities (in order of general ledger accounts)
9. Statement of current earnings and expenses (comparative)
10. Branch office (schedule of resources and liabilities serviced)
11. Schedules:
  (a) Investment securities.
  (b) Public funds.
  (c) Due to banks.
12. Examination of minute books; stock ledgers and certificates.

Senator ROBERTSON. The next witness is from North Carolina, Mr. Conrad York.

STATEMENT OF W. C. YORK, DEPUTY COMMISSIONER, STATE OF NORTH CAROLINA INSURANCE DEPARTMENT

Mr. YORK. Members of this honorable committee, Mr. Charles F. Gold asked me to express his deepest appreciation to you for granting us this time to appear here before you. He would have enjoyed it himself but he is being inaugurated today for another 4-year term, along with the Governor of our State.

Senator ROBERTSON. We will be glad to hear you, and you may proceed.

Mr. YORK. We have a prepared statement which we wish to go into the record.

Under the captioned bill, the Federal Home Loan Bank Board would be given powers much broader than now exist under present law. In our opinion, certain sections enumerated and commented on below are an invasion of States' rights and infringe on the authority of States to regulate and supervise savings and loan institutions that said States have chartered.

North Carolina has chartered and now supervises 148 savings and loan institutions, 102 of which have insurance of shares through the Federal Savings and Loan Insurance Corporation. All insured associations would be affected by this new proposed legislation.

We solicit your careful consideration of the following quoted sections and comments thereafter.

In the interest of brevity, I will leave out the part of the law that I have quoted and will only quote our comments.

The first section has to do with the membership of the Federal Home Loan Bank. We think an association should be able to identify itself with the bank in ads, on its stationery or on the office window. Many institutions are proud of their membership in the bank and should be permitted to say so.

Mr. ROGERS. Mr. York, that would permit the advertisement in the home office. It is aimed at nationwide advertising by a few associations who, through the use of the Home Loan Bank System insignia and saying they receive accounts up to $10,000 and under State Government supervision, mislead the public into thinking that they are insured.

Mr. YORK. Does it say that in the bill or just——

Mr. ROGERS. Pardon?

Mr. YORK. Does that give the board the right to say whether it should be on the window anywhere?

Mr. ROGERS. It says "off the premises on which is situated the home office." That is the only thing.

Mr. YORK. It is our understanding they would have to remove that from their stationery.

Mr. ROGERS. Well, not necessarily. That would be up to the board's regulation.

Mr. YORK. That is right.

Mr. ROGERS. We assume the board would be reasonable about this.

Mr. YORK. We would like to have it spelled out to that extent if we could.

Mr. ROGERS. How many uninsured associations do you have in North Carolina?

Mr. YORK. Forty-six, ten of which are just members. Others would like to be members but without insurance. However, the board will not take any other institutions as members without the insurance.

Mr. ROGERS. That is correct. Do you have any restriction on their advertising?

Mr. YORK. Locally? No, sir.

Mr. ROGERS. By State law?

Mr. YORK. By State law?

Mr. ROGERS. Yes.

Mr. YORK. Well, no, we have no restrictions as far as the Federal Home Loan Bank is concerned. We would have restrictions as far as State law is concerned how far they could advertise.

Mr. ROGERS. Thank you.

Mr. YORK. The second section has to do, of course, with the conversion of the Federal associations into State-chartered institutions, where a State—

shall constitute an agreement to be bound by all the requirements that the Federal Savings and Loan Insurance Corporation may legally impose under section 403 of title IV of the National Housing Act.

We are in opposition to this because we feel it is an attempt by the Federal Savings and Loan Insurance Corporation to dictate the policies of a State corporation once it has been converted to a State institution.

Senator ROBERTSON. May I interrupt to suggest that that is the provision of the present law?

Mr. YORK. Provision of the present law? According to whatever interpretation they wish to render? It has always been heretofore, until the past year, that the State had a right to regulate its own corporation.

Senator ROBERTSON. The pending bill does not change existing law.

Mr. YORK. Does not change it?

Senator ROBERTSON. That is right.

Mr. YORK. The Federal Savings and Loan Insurance Corporation Act. Part of the evidently new provision gives the Insurance Corporation the right to adopt and amend bylaws and to adopt, amend, and require the observance of such rules, regulations, and orders as may from time to time be deemed necessary for carrying out the provisions or purposes of this title or for the protection of its insurance risk. It is our opinion that the wording here is too broad, and it gives to the Corporation powers and rights which we think rightly belong to Congress. In other words, that the law should spell out what is desired and not leave such broad power in the hands of a governmental corporation. Rules and regulations could be drawn that would not infringe on State law.

Section 404 (b), page 220 of the bill.

Each applicant for such insurance shall also file with its application an agreement that during the period that the insurance is in force it will not make any loans beyond 50 miles from its principal office except with the approval of, and pursuant to regulations of, the Corporation.

The provisions of this section should be the same as granted under section 5 (c), page 204, which grants Federal associations:

Except that not exceeding 20 per centum of the assets of such associations may be loaned on other improved real estate without regard to said $35,000 limitation, and without regard to said 50-mile limit——

Senator ROBERTSON. In other words, you are recommending a change in existing law? The bill just states the existing law.

Mr. YORK. No, no. We are recommending——

Senator ROBERTSON. I think the bill states the existing law.

Mr. YORK. We are recommending that the same provisions—which haven't been interpreted as such—be extended to an insured institution.

Mr. ROGERS. Mr. York, what the Senator is trying to make clear for the record is that this provision, like the earlier one, is exactly the same as present law. The bill makes no change in it. You are recommending a change, but you are making a recommended change in the present law and not in the bill as such.

Mr. YORK. That is right.

Section 404 (c):

In considering applications for such insurance the Corporation shall give full consideration to all factors in connection with the financial condition and policies of applicants, the need for additional insured institutions in the com-

munity, and the effect of the granting of insurance upon existing insured institutions in the community, and shall have power to impose such conditions to insurance, which conditions may be conditions precedent or conditions subsequent, as it may be necessary or advisable in the public interest or for the protection of investors. Any such conditions heretofore imposed are hereby validated.

It is our opinion that under present law Congress has sufficiently spelled out the basic requirements for insurance. The amendment would place in the hands of a corporation or a board legislative powers which should remain with Congress. In other words, Congress should not allow its functions to be usurped in this manner, and it is contrary to our ideas of separation of powers under the Federal and State constitutions. Also, it might possibly result in an infringement on States rights if the rule or regulation written by the Corporation either violates the State law or puts the Corporation in a position where it could underwrite the State's decision on need or necessity for an additional association. The power sought under this section would give the Insurance Corporation complete control to regulate competition and would grant control over savings and loan associations which no other corporation could obtain by legislation; that is, the right to controlled competition or no competition.

We recommend that line 16 through line 18 of this subsection be amended by striking out the words:

The need for additional insured institutions in the community, and the effect of the granting of insurance upon existing insured institutions in the community.

Senator ROBERTSON. May I ask a question there?

Mr. YORK. Yes, sir.

Senator ROBERTSON. When you say "we" recommend, to whom do you refer?

Mr. YORK. Mr. Gold. We have prepared a joint statement.

Senator ROBERTSON. Please state his position.

Mr. YORK. Commissioner of insurance, State of North Carolina.

Senator ROBERTSON. Is that just a one-man board?

Mr. YORK. He is commissioner of insurance, and under the commissioner of insurance is the supervision of all savings and loan institutions in our State.

Senator ROBERTSON. I mean is he the last authority? In Virginia we have a division of banks, but it is under what we call the State corporation commission. The official action has to be taken by the State corporation commission.

Mr. YORK. No, he just——

Senator ROBERTSON. But the man you speak for now is the one that takes the last official action on banking in North Carolina?

Mr. YORK. Not banking. The banking is under the banking commissioner and a bank board. The savings and loan business is not under the banking laws in our State.

Senator ROBERTSON. Oh, you are just talking about savings and loan associations.

Mr. YORK. That is right; yes, sir.

Senator ROBERTSON. I just wanted to know who the "we" was.

Mr. YORK. It is a joint statement which was prepared by Mr. Gold and myself, with the backing, of course——

Senator ROBERTSON. If you will excuse the inelegant English.

Mr. YORK. Section 404 (e) has to do, of course, with the mergers.

Except with the prior approval of the Corporation by regulations or otherwise, no insured institution shall (1) be a party to any merger or consolidation; (2) purchase any assets from or sell any assets to any savings and loan, building and loan, or homestead association or cooperative bank, or any savings bank; or (3) increase its accounts of an insurable type through or in connection with any purchase of any assets.

This particular provision would bypass all State laws and give the Insurance Corporation complete authority for any type of merger. It is our opinion that where State-chartered associations are concerned, any requirement of approval by the Insurance Corporation would be an invasion into matters which should be determined by State law. Any regulation on these subjects should be concerned solely with the safety of the continuing or acquiring institution as tested by the adequacy of its reserves. We think this would be an improper delegation of power to a corporation or a governmental board and an usurpation of power properly residing in management.

The miscellaneous section. This has to do——

Mr. ROGERS. Mr. York, may I ask you a question about that last section?

Mr. YORK. Yes, sir.

Mr. ROGERS. Under this proposal would not your office still have to pass upon each merger?

Mr. YORK. Not according to the wording of the bill we would not.

Mr. ROGERS. How do you get that interpretation?

Mr. YORK. It says "except with the prior approval of the Corporation." It makes no reference to our departments at all, our State departments.

Mr. ROGERS. Could a merger take place in North Carolina without first getting your approval?

Mr. YORK. State corporations; no. But if this goes into effect, then we would have little or no say-so in it. That is our interpretation.

Senator BENNETT. Would this not have the effect of requiring the joint approval both of you and of the Insurance Corporation?

Mr. YORK. The bill does not say so.

Mr. ROGERS. Two savings and loans could never come to the Corporation without State approval; that is right.

Senator BENNETT. Without State approval.

Mr. YORK. It does not say that in the present proposed bill, does it?

Mr. ROGERS. I think that is implied in all of it.

Mr. YORK. Implied in all of it?

Mr. ROGERS. Yes, sir.

Senator BENNETT. We cannot legislate for the State of North Carolina.

Mr. YORK. I know you cannot.

Senator BENNETT. All we can legislate for is the Federal Government. And the fact that we make this proposal with respect to the Federal agency does not completely destroy your right to exercise your authority. It just imposes a second layer on the situation.

Mr. YORK. Supposing two State associations wish to merge, could they do it without the permission of the Corporation under the present proposed setup?

Senator BENNETT. They could not approach the Corporation without your permission, without first having obtained your permission. If they came to the Corporation and, in answer to a question, had to say, "We do not have permission of the commissioner of North Carolina," I am sure the Corporation would ipso facto have to refuse it.

Mr. YORK. All right. If they have our permission and they ask the Corporation's permission and the Corporation says, "We will not give it," then what? Who has control?

Mr. ROGERS. That is the situation where it could be turned down as far as insurance goes. They would be no longer insured.

Mr. YORK. In other words, they have the last say-so on whether they will join——

Mr. ROGERS. That is right as far as——

Senator BENNETT. As far as insurance goes.

Mr. ROGERS. That is right.

Senator ROBERTSON. The committee has had the same issue before us with respect to insured State banks.

Mr. YORK. Yes.

Senator ROBERTSON. On the bank merger bill the committee has construed the language to mean that the States act first and the Federal agency does not act unless the State first approves the merger. The committee takes the same position with respect to the mergers of savings and loan associations. The State on a State institution acts first and, unless it approves, the Federal agency will not consider it. That is our interpretation of what this law means.

Mr. YORK. But if they turn it down, of course, they would lose the insurance even though they merged. Is that right?

Senator BENNETT. That is right. But just to finish the concept, you do not have now the power to guarantee them their insurance. You only have the concern of approving their merger.

Mr. ROGERS. Sure.

Senator BENNETT. In any event, the responsibility for insurance rests with the Federal Government, even under the present situation.

Mr. YORK. Yes.

Under miscellaneous amendments—

> Whoever being an officer, director, or employee of a bank which is a member of the Federal Reserve System or the deposits of which are insured by the Federal Deposit Insurance Corporation or of any savings and loan, building and loan, or homestead association, cooperative bank or other institution, the accounts of which are insured by the Federal Savings and Loan Insurance Corporation—
>
> (ii) Makes or grants any loan to, or employs or makes an offer of employment to, any examiner or assistant examiner—

and so forth.

I will not finish the quotation of that because I am sure you are familiar with it. But we think this goes too far. We do not think any Federal agency should have power and authority to control and supervise State employees and make it possible to dictate their future employment if they change positions. We do not think that it is right to prevent any employee or individual from pursuing, seeking or accepting employment in his chosen field or profession, and that wherever the words "State agency" appear in this bill they should be deleted.

The Federal Home Loan Bank Board has asked for this same control over their employees under section 19 (b), page 200, of the proposed bill, of title IV, Federal Home Loan Bank Act, of this same bill.

The enactment of this legislation would not cut down the number of defalcations in financial institutions or in any manner eliminate all dishonesty. This is a direct attack on the character, the moral standards, and the integrity of all the employees of both the State and Federal supervisory authorities and would be a handicap to these agencies in obtaining new employees. For years the greatest incentive our employees have had is to be able to go into these institutions as executives.

In the interest of brevity I wish to have the rest of these remarks filed.

Senator ROBERTSON. That may be done.

(The balance of Mr. York's prepared statement follows:)

CONCLUDING REMARKS

The Federal Savings and Loan Insurance Corporation has assets of approximately $267,000,000 and the right to borrow up to $750,000,000 from the United States Treasury. This makes a total of $1,017,000,000 available for emergencies. The Corporation has insured accounts of approximately $34 billion. Thus you have $1 billion underwriting $34 billion or a potential reserve of approximately 3 percent. Is it because of this potential liability that the Federal Home Loan Bank Board and the Federal Savings and Loan Insurance Corporation have asked for powers that will give them complete control over all insured State institutions?

The loss reserve liabilities of all State-chartered institutions in North Carolina amount to 7.5 percent of total share capital, and it is one of the greatest protections the Insurance Corporation has. These loss reserves would be first used before the Corporation would have any liability for losses in North Carolina.

It is our contention that the Federal Home Loan Bank Board and the Insurance Corporation already have sufficient powers to amply protect potential losses without granting more powers. Since the liability of the Insurance Corporation is not affected until local loss reserves are exhausted, we oppose the granting of complete dictatorial powers to the Bank Board or the Insurance Corporation.

The building and loan division of the North Carolina Insurance Department is the supervisory authority of North Carolina State-chartered associations. We have consistently required good management, sound operation, and that adequate reserves be set up by all State associations. We feel that the State supervisory record in this respect speaks for itself.

It is when efforts are made by Federal agencies to further usurp States rights that we find it our duty to ask this committee to eliminate from this bill the objectionable provisions.

Mr. YORK. I appreciate the opportunity to appear before you.

Senator ROBERTSON. Any further questions?

If not, we thank you.

Mr. Maurice S. Brody, director of the Denver National Bank, was scheduled to testify this morning, but he was unable to be here. His prepared statement will be made part of the record at this point.

(The prepared statement of Mr. Brody follows:)

STATEMENT OF MAURICE S. BRODY. DIRECTOR, DENVER NATIONAL BANK

In both the 83d and 84th Congresses two unsuccessful attempts have been made to eliminate the principle of mandatory cumulative voting in the election of national bank directors. This attempted legislation was not accompanied by any objective, unbiased study as to the merits of this principle from the standpoint of the public interest. On the contrary, the attempt to change the present law carried all the earmarks of a special-interest group trying to put through legislation designed to serve its own purpose.

Accordingly, it becomes imperative for the Senate Banking and Currency Committee in making a study of our banking laws to fully explore the present method of voting in our national banks with a view of ascertaining in a careful, objective, and unbiased fashion whether the interests of the public, the bank's customers, the management, and the bank's public stockholders are all properly protected and safeguarded.

The elimination of mandatory cumulative voting in the election of our national bank directors would uproot a basic concept of Federal corporate law deeply embedded in the public interest. In this process the present property rights of more than a half million persons would be stripped from them as they would be denied their present right to elect representatives on the directorates of national banks. Probably hundreds of independent bank directors throughout the country now acting as watchdogs in the national interest would consequently be liquidated.

But more important than the disenfranchisement and destruction of the property rights of the above persons, a basic crack will have been made in our fundamental corporate bill of rights which is the essence of cumulative voting. The hundred-year struggle to secure minority representation in the conduct of our corporations will have been struck a mortal blow. The Federal Government will have set a precedent that the forces of reaction in the individual States will seize upon to repeal the corporate bill of rights (mandatory cumulative voting) presently effective in 16 States of the Union.

Furthermore, the loss of our corporate bill of rights, by removing the present legal barrier, will once more open wide the door to discrimination. The law will no longer be a protection. The group in control of each national bank can exclude stockholders from becoming directors for any reason including race, color, or religion. It is contrary to our present national conception of justice and certainly is not in keeping with the spirit of the times. It is a throwback to the days that we had hoped we had left behind forever.

Finally, the present tight control of our national banks will be further extended to the point of monopoly control with very little prospect of bringing about a change of management should the necessity arise. In the case of the Bank of America National Trust and Savings Association, the practical aspect is that the 1 percent of the stock owned by the management will completely control. The public owning 99 percent of the stock will be locked out as they will not be able to name a single director.

This, in effect monopoly control of our national banks, will further extend to other corporations since many trusts set up in the trust departments of these national banks hand over the voting control of nonbank corporations to these monopoly controlled national banks.

The above reasons cited are deeply embedded in our American national interest and certainly are by no means offset by the desire of special interests who already being strongly entrenched in the management of our national banks are calling for monopoly control power at a time when the public interest clearly is in the direction of granting these vested interests less power rather than more.

National banks, being by their nature semipublic institutions that gather together the liquid funds of the public for the purpose of safely lending and investing these funds for productive purposes, must of necessity be carefully regulated and supervised.

It is my purpose in this statement to demonstrate to the committee that the checks and balance philosophy underlying our present national banking laws, which has served America so well during the last 23 years, rests squarely on the existence of independent national bank directors. And that these independent bank directors can exist only when public stockholders can avail themselves of the principle of mandatory cumulative voting in order to elect representative directors.

Our national banking law revision in 1933 set up a supervisory system for our national banks built on the cornerstone of independent vigilant directors who are distinct and apart from the officers and management of the bank. This supervision setup can only be effective just so long as there are present on the board of directors of the bank, directors who are independent of the officers who run the bank.

The supervision extends in three directions:

1. Supervision by directors internally on an all-year-round basis.
2. Supervision by an annual examination of the bank by a committee of directors totally separate from the officers of the bank.

3. Supervision by an annual or semiannual examination made by the national bank examiner.

It is obvious that unless the relationship between the directors and the officers is conducted on an arm's length basis that the likelihood of effective supervision of the acts of officers of the bank by the directors is rather remote. Directors in effect chosen by the management officers are not likely to exercise any degree of restraint or supervision over the activities of the officers. Supervision by directors internally on an all-year-round basis thereby becomes weak and ineffective.

The required annual examination by law of the bank by a committee of directors separate from the officers of the bank soon founders on the same basic defect. Directors closely tied in with the management due to the fact that they are directors, not as a result of their stockholdings but just by virtue of the fact that the officers invited them to become directors, are unlikely to subject the bank to anything but a routine cursory examination prescribed by an officer.

Finally, let us look at the examination by the national bank examiner. He comes once or possibly twice a year and spends a few days examining the bank. Unless he finds real flagrant violations he will content himself with indicating that certain loans are substandard while other loans will be criticized for one reason or another in the hope that when he returns a year later he will find that considerable improvement in these loans has taken place. Here is where the independent director tends to make effective the national bank examiner's criticism, for in the interval of 1 year the independent bank director can follow through where the bank examiner left off. Unless there are independent watchdog directors present to act in the interval, the national bank examiner will most likely return a year later to find the same old mistakes, aggravated by time, still on the books.

Mandatory cumulative voting, by permitting the public stockholders to directly elect directors who are independent of the officers, provides the backbone to our present system of supervision. Their mere presence keeps officers on their toes and in line with sound banking practices. Their arm's length relationship with the management makes effective the present three-prong method of supervision of our national banks. Without independent directors the effective supervision of our national banks falls away like a house of cards.

In view of the effective supervisory function played by the independent director elected by the public stockholders because mandatory cumulative voting is an integral part of our national banking laws, it is understandable why the managements of our national banks are straining every nerve and fiber to eliminate mandatory cumulative voting in the election of national bank directors. If management succeeds in destroying mandatory cumulative voting, they will in one fell swoop rid themselves of effective supervision and thereby place themselves once again back in the saddle that they occupied in the 1920's and the early thirties.

To see the real significance of the necessity of maintaining the principle of mandatory cumulative voting in the election of our national bank directors, it must be clearly understood that there is a distinct line and cleavage between the management of a bank as represented by its president and executive officers, and the directors representing the owners of the bank. These two groups are separate and apart from each other with different duties and responsibilites. It is essential for the proper functioning of our national banks not to permit one group to destroy the duties and responsibilities of the other group nor for one group to usurp the functions of the other group.

The banking management fraternity made up of presidents and other executive officers of banks by pressing vigorously for the elimination of mandatory cumulative voting through their banking associations such as the American Bankers Association and the Association of Reserve City Bankers would usurp the function of independent directors of the bank to supervise the activity of these executive officers. The power presently vested in the hands of the stockholders would consequently be arrogated by these management officials to themselves. This usurpation of functions is unsound public policy and would tend to destroy the system of checks and balance in our national banks.

The recent failure of the Home National Bank of Ellenville, N. Y., clearly sets forth the necessity for a definite division between the duties and responsibilities of the management as contrasted with the duties and responsibilities of the directors. Here the Comptroller of the Currency was unable, by his external examinations, to protect the interests of the stockholders and the depositors of the bank. The present safeguard of mandatory cumulative voting could have been used by the stockholders to elect vigilant directors who, by the maintenance of strict internal supervision, could have prevented the president from dissipating the funds of the bank.

To tie the hands of the stockholders by destroying this right to protect their own interest as well as the interest of the depositors on the grounds that the Comptroller of the Currency is at present sufficiently protecting the interest of the stockholders was brought to a reductio ad absurdum by the fiasco of the Home National Bank in Ellenville, N. Y.

No law can absolutely prevent bank failures nor can any law force directors to be sufficiently prudent in their discharge of their obligation to protect the investment of the stockholders and the funds of the depositors. All the law can do is to keep the door open so that the public stockholders have the right to elect representatives of their own choosing who will act as independent directors and thereby effectively supervise the activities of the officers of the bank. Our present mandatory cumulative voting law protects this right of the stockholders. Its elimination would destroy the precious safeguard of independent internal supervision which is a basic cornerstone of our present National Banking Act.

The divergence of interest between the management and the public stockholders of our national banks is a fundamental principle which must be maintained. If mandatory cumulative voting is outlawed as some bank managers are pressing for, the bank presidents would become in effect their own bosses and will cease to be subject, particularly as time goes on, to effective internal supervision by the owners of our national banks. This is unsound public policy and should not be sanctioned by Congress.

It must be realized that our present national banking law does not require bank managements to reveal the pertinent information concerning directors of banks which at present the Securities and Exchange Commission rules provide in the case of exchange listed corporations. The stockholders in voting for their directors of national banks do not know what stake the prospective director has in the bank—whether a candidate for director owns 100 shares of capital stock of the bank or 10,000 shares of capital stock of the bank—nor is the management required to reveal any other information which would enable the stockholders to intelligently pass on the adequacy of the candidate to become a director. The national bank stockholder in effect, therefore, by signing his annual proxy, blindly presents the management of the bank with a blank check which they can use in any way they wish. They can load the board of directors with directors beholden to the management.

If, in addition to the present complete lack of information which is kept from the stockholder when he votes his proxy, he also has his present right to elect independent directors on the boards of banks taken from him, he then is completely and absolutely placed at the mercy of these bank officials. It is hard to imagine that under these circumstances, Congress would strip from a half million public stockholders their only present right to protect their investment—namely, the right of independent representation on the board of directors through the exercise of the mandatory cumulative voting principle presently available to the stockholders.

Clearly the elimination of mandatory cumulative voting is contrary to the public interest and Congress in its wisdom should not permit a clear conflict of interest on the part of the bank managers to strike down the only remaining protection which public stockholders have to safeguard their own investment and that of the depositors of our national banks.

The public interest should come first and Congress as the representative of the public interest should not permit the safeguard of mandatory cumulative voting to be destroyed regardless of the amount of pressure which the banking lobby will exert upon the representatives of the people.

The above analysis should make clear why the banking management fraternity, apart from the public stockholders of our national banks, is putting up such a desperate fight to rid themselves of mandatory cumulative voting. Their pretext is that cumulative voting has lent itself to certain isolated cases of abuse. To this the answer is definite and specific. If the Federal Reserve Board does not presently have sufficient power to deal with these cases of abuse, its power should be broadened to permit the Board to handle this phase of banking. The Federal Reserve Board, being independent and nonpartisan, is well suited to regulate in the public interest.

The 27-man advisory committee to the Senate Committee on Banking and Currency in reference to this overall bill stated clearly that in their opinion mandatory cumulative voting is sound in theory. This advisory committee, heavily loaded with men representing the bank management fraternity and without a single representative of the half-million public stockholders on whose rights they were passing, reaffirmed the soundness of the principle of mandatory cumulative voting but were unhappy with its practice in operation in some cases. Clearly the remedy for a principle that is sound in theory but imperfect in practice is to retain the basic principle but to device means to improve its practice.

The Financial Institutions Act of 1957 bill clearly proceeds to do just this. The Federal Reserve Board is given more power to remove directors considered unworthy. This is the proper method to handle cases which have interfered with the constructive and effective manner of working out the mandatory cumulative voting provision of our National Banking Act. To destroy and strip from our American system of corporate national banking law a basic principle that is sound just because its practice is imperfect is not in keeping with our American traditions of fair play and justice.

If we refuse to remedy the practice of a principle that is sound but instead reject the sound principle that is inherent and basic to our corporate national laws, we raise the question of whether we are quarreling with the practice at all but really at heart want to destroy the sound principle of protecting the public stockholders from encroachment on their inherent rights to safeguard the funds of depositors and the investment of the public stockholders.

It is sheer folly to burn down the house of mandatory cumulative voting, which permits the election of independent watchdog directors who clearly serve in the public interest, just because there happen to be a couple of mice in the basement.

In summary, therefore, this is the case for the retention of mandatory cumulative voting as a basic fundamental democratic American principle inherent and vital to the integrity of our national banking system.

Twenty-three years ago Congress in completely overhauling our national banking system established mandatory cumulative voting as a requisite principle in the election of our national bank directors. This principle has permitted the present one-half million public stockholders to have independent representation on the board of directors in our national banks. With the diffusion and widespread public ownership of bank stocks which has occurred during the last 23 years this principle is more important and necessary today than it was even 23 years ago.

The soundness of this principle has been freely recognized by both friend and foe alike and has become deeply imbedded in our Federal and State corporate law as being basic to the sound public interest of our Nation. It has become established as an inherent property right of millions of public stockholders not only in our national banking system but also in one-third of the States of the Union.

Mandatory cumulative voting has become the Nation's fundamental corporate bill of rights. Rights of the minority stockholders which the majority cannot take from them. The right of representation and a voice in the management of the corporations that they own. Repeal by the Federal Government would set a precedent that would harken the forces of reaction in 16 States of the Union and would set the wheels of progress turning backward.

In addition, the loss of our Federal corporate bill of rights by removing the present legal barrier against discrimination will once more open wide the door to discrimination on the grounds of race, color, or religion. The group in control of any national bank can reject a candidate for directorship on these grounds.

Furthermore, monopoly control will supersede our present majority control of our national banks. The practical operation of our corporate control laws will permit a tiny minority of stockholders acting through the officers of the bank to exercise monopoly control of our national banks. This should not be tolerated at a time when the public interest is clearly in the direction of granting these vested interests less power rather than more.

Finally by undermining the independent internal supervision of our national banks a death blow will be struck at the checks and balance safeguards presently operating in our national banks through the instrumentality of independent watchdog directors elected under the mandatory cumulative voting principle—the established safeguard of independent internal supervision that would have prevented the failure of the Home National Bank at Ellenville, N. Y., at the hands of its bank president.

The remedy for defects in the practical operation of mandatory cumulative voting can be easily achieved through extending the power of the Federal Reserve Board to remove unworthy directors. This the bill known as the Financial Institutions Act of 1957 does. This is the sane and proper method to use in improving the practical operation of the sound democratic principle of mandatory cumulative voting which over the years has become deeply imbedded as the bill of rights in the fabric of our National and State corporate laws comparable to the Bill of Rights in our constitutional system of law.

The ruthless outlawing of mandatory cumulative voting in our national banking system would set in motion reactionary forces in the Nation and the individual States which would challenge the corporate safeguards and property rights of millions of public stockholders. No political party in America can live to govern which espouses the selfish interest of the few by destroying the property rights of the many.

Senator ROBERTSON. The committee will stand in recess until 10 o'clock tomorrow.

(Whereupon, at 10:45 a. m., the subcommittee recessed until 10 a. m., Friday, February 8, 1957.)

STUDY OF BANKING LAWS

(Financial Institutions Act of 1957)

FRIDAY, FEBRUARY 8, 1957

UNITED STATES SENATE,
COMMITTEE ON BANKING AND CURRENCY,
SUBCOMMITTEE ON BANKING,
Washington, D. C.

The subcommittee met, pursuant to recess, in room 301, Senate Office Building, at 10: 05 a. m., Senator A. Willis Robertson (chairman of the subcommittee) presiding.

Present: Senators Robertson, Monroney, and Bennett.

Senator ROBERTSON. The subcommittee will please be in order.

The first witness today is Mr. Seaborn J. Flournoy, of Norfolk, Va. We will be glad to hear you.

STATEMENT OF SEABORN J. FLOURNOY, INVESTOR AND STOCKHOLDER, AMERICAN NATIONAL BANK, PORTSMOUTH, VA.

Mr. FLOURNOY. My name is Seaborn J. Flournoy, of Portmouth, Va. I am a Ford dealer, having been a dealer for 28 years, a Ford tractor and implement dealer, an insurance agent, in the investment business, and one of the largest stockholders of the American National Bank of Portsmouth. My appearance here before this committee is to oppose the proposal contained in title I, chapter I, section 26, subsection (C) of the committee print bill entitled "Financial Institutions Act of 1957." This proposal seeks to eliminate the cumulative voting of shares in the election of directors of national banking associations.

My reasons for opposing this proposal are as follows:

1. It is contrary to the Constitution of the United States of America. The preamble states that its purpose is to "establish justice." In what nation would the denial and abrogation of the rights of a 49.99-percent minority be defined as justice? However, injustice rather than justice would almost certainly result in many instances from the passage of this proposal. Bank management is now permitted by law to withhold from its stockholders, who own the bank, any and all pertinent information such as salaries of officers, fees paid to directors, details of the bank's investment portfolio, number of shares held by officers and directors, proposed changes in number of directors, and all operational details—because the law does not require a bank to publish information nor to make it available to its stockholders when seeking proxies for the annual meeting. Some banks voluntarily disclose some of this information, but most do not. The one in which I am most interested

never did until this year—and then only as a result of my severe criticism during 1956. Even so, the report submitted was very meager and it was not received by stockholders until 10 days after the annual meeting of stockholders and election of directors.

And yet the law does require that other corporations which sell their securities to the general public, as do most banks, abide by the regulations of the Securities and Exchange Commission, and the Securities and Exchange Commission does require that such information shall be furnished each stockholder. Why should bank management be favored over other corporate management? Is this justice?

You Senators are here to reexamine legislation that undoubtedly needs revision. It is full of anachronisms. If it were not, you, sir, my Senator, the Honorable Willis Robertson, would not have offered the bill. But you gentlemen have been sitting here for a long time to make sure that those things in the present law that "establish justice" are not eliminated to satisfy the demands of a pressure group, however numerous, however well recommended, however powerful financially. I and other bank stockholders, who have dared criticize or oppose bank management, have not been generally successful in our efforts to date. But some of us will continue our fight and we would hate to see the only pathway now open to us, that is, the right of mandatory cumulative voting, barred and padlocked against us by the adoption of this proposal. Financial slavery, although not as degrading as political slavery, should be unconstitutional. My second reason is simple equity. I am not a lawyer, as many of you gentlemen are, but I have always heard that "equity is the administration of law according to its spirit and not according to the letter." I have not only heard it, I have read it in Mr. Webster's dictionary.

Many people in this country are naive enough to believe that a corporation or banking association, since it is owned by a group of stockholders, is governed by the same rules as our Federal Government and subject to the same checks and balances. Perhaps they are in theory, but as you gentlemen know only too well, the ballot is as deadly as the bullet.

Who ever heard of a Congressman running for election and just as the polling places were being opened on election day being told by the judges of election that the number of Congressmen to be elected had been reduced from 17 to 5? And, therefore, he would need one-fifth the total vote, or the vote from 3½ districts in the State, instead of one-seventeenth, or the vote from 1 district. No one. The law forbids such highhanded, dictatorial action. But I heard of what happened to a would-be national bank director in Portsmouth, Va. He held proxies for more shares of the bank's stock than the total shares owned by all of the bank's 17 directors, who was told at the annual meeting that only 5 directors would be elected. This change in the number of directors was passed by the voting of proxies obtained by the bank's management, at the expense of the bank's stockholders, without notice to the stockholders that any such action was planned. The reason given for the reduction was "that a stockholder who had criticized the bank's management is undertaking to have himself elected with others to the board." I know, because I am the stockholder who criticized; I am the stockholder who undertook to get elected to the board so that the 43 stockholders I represented might have some say in the management of the bank, rather than leaving it entirely in the hands of the existing board. The latter had rather clearly demonstrated over the years that they were almost completely dominated by the bank's president.

Don't you gentlemen agree that such action, although perfectly legal, was not an action that fits in with the definition of equity? Especially since upon organization the 5 remaining directors appointed the 10 living former directors as an advisory board and are paying them the same attendance fees they formerly received as directors, at an annual expense of $10,400 to the bank.

The average annual profits of that bank after taxes for the last 10 years have been just $100,000.

Now that I know the rules of the game, I will conduct my campaign for proxies in the open, as I did last year, until I have enough to get elected to a 5-man board; and they won't be as hard to get as the 43 I got last year, unless the door is slammed in my face by the abolition of cumulative voting.

My third reason is that the abolition of mandatory cumulative voting, rather than promoting harmony as alleged by the American Bankers Association, would actually have a tendency to harm many national banks by fostering bitter proxy battles over a period of years; since only by controlling a majority of the stock could a shareholder obtain representation. To cite an example with which I am entirely familiar—my own case:

Why do I want to be a director of the American National Bank?

1. Because the bank has need of some ideas which, although new to the management, have been the basis of the operating policies of almost all well-run banks. These ideas have been used and proven to be sound by all of the banks with which I am familiar.

2. Because the interests of the bank's stockholders have not been placed ahead of the interests of the executive officers and directors and I want to see that this is continually brought up at meetings until it is corrected.

3. Because most of the former directors were under the domination of the bank's president.

4. Because I know, and the stockholders who gave me their proxies sincerely believe, that my motives are entirely unselfish and directed only toward seeing that our city has a national bank that is as good for the city and its people as it is for its officers and directors.

These are my motives. Now what am I—and others who want to serve their community for similar reasons? If I get licked in about 3 or 4 annual stockholders' meetings by the combined efforts of the bank officers, present and past directors, present advisory board and employees, what will be my reaction? Will I quit? I will not. Will I become bitter because my personal friends who have notes in the bank are afraid to give me their proxies? Or because employees of the bank who know that I am right and the management is wrong, and have said so, are afraid to give me their proxies because of their jobs? Or because of modest pensions paid at the pleasure of the board of directors, upon the recommendation of the president, to dear friends of mine, many mutual friends of mine and the pensioners, although agreeing with me 100 percent as to the desirability of nonmanagement representation on the board, feel that they must give their proxies to the management so that the pensions of their friends and mine will not be disturbed?

Although I am citing from a specific case, there are many hundreds of small national banks scattered throughout the entire United States of America in which smug, self-satisfied, unprogressive management could become just as well entrenched as it has in our bank in Portsmouth, and in only isolated cases can there be effective opposition. And without cumulative voting it is almost a hopeless task. Do not perpetuate dictatorship of bank management in many of the small towns and small cities of your States and mine. I know that most banks are well run, and I know also that management of those banks is rarely attacked; but many banks are not run in the interests of the depositors and stockholders and such banks should not be protected by Federal law. They should be regulated by the Comptroller's Office, not pampered.

At this point I should like to read from some graphs in my testimony before the Committee on Banking and Currency of the House of Representatives of the 84th Congress, 2d session, at the hearings on Senate bill 256. If each of you gentlemen will be good enough to turn to pages 119 through 124, you will see my testimony and 6 graphs. These graphs illustrate and prove beyond a shadow of doubt that—the first graph shows the local bank representations as to percentage of growth or loss of resources from December 31, 1945, to December 31, 1955.

The American National Bank shows a loss of 9.42 percent in resources in that 10-year period in a defense area where all other business prospered and grew mightily. The other banks increased in their resources and the increases ran from 26.07 percent to 49.54 percent, with the exception of 1 small State bank, which only grew 6.37 percent.

I might add the president of that bank is a brother of the president of the American National Bank, and they seem to think alike.

The next graph shows the dollar earnings of these banks for the years ending December 31, 1946, and December 31, 1955. The American National Bank's earnings actually declined in that period from $111,000 to $109,000, whereas the other banks grew anywhere from 30 to 100 percent in earnings.

The next graph, C, shows that this bank averaged for 10 years past earnings that are a far smaller percentage of its capital funds than any of the other banks in the area. It has averaged 8½ percent, and the other banks vary from 9.99 percent up to as high as 11.77 percent.

Graph D is next. This one they don't like at all. It shows the salary of the bank's president at $229.11 per $1,000 earned by the bank in 1955, that is, our bank, as compared with the other bank presidents in the area, whose salaries ranged from $115.34 to $40.74 per $1,000 earned by their banks.

Graph E shows the comparison in resources and earnings between our bank and the bank directly across the street in Portsmouth, Va. It is not favorable. At the end of 1945 was 2½ times as large as the other bank, but the other bank made 57 percent as much money. At the end of 1955 the other bank was 57 percent as large as our bank, but made more money by $30,000.

Graph F shows the comparison in resources and earnings between our bank and the bank in the area which was nearest in size to our bank. It is not favorable either. Ten years ago this other bank had resources of $18,600,000 against our bank of $27,900,000, but its earnings 10 years ago were $3,000 more than those of our bank. At the end of 1955 this bank had become a $27,400,000 bank, while ours had declined to $25,300,000; and whereas our earnings went down to $109,000, the other bank's earnings had increased above $200,000.

So much for the graphs shown. They may suggest questions which some of you gentlemen might care to ask me.

In reading through the testimony you will find other facts which those of you who are close to business and banking will find to be almost unbelievable. May I say that I find the entire situation fantastic, but I have not distorted a fact in either my graphs or my statement.

Gentlemen, let us be practical and factual about this matter. Proponents of this particular phase of the proposed legislation have been bankers or those closely associated with bank management. They have spoken and written at great length about the dangers of mandatory cumulative voting, but never have I read such nebulous statements. Throughout only one thing is clear—who wants protection? Bank management wants protection. From whom does bank management want protection? It wants protection from stockholders—vicious characters with the basest of motives who have dared to criticize them in some cases. Management has asserted with a perfectly straight face that you should believe that any minority opinion is, per se, contrary to the best interests of a bank; is uninformed, unqualified, and irresponsible; is prompted by personal profit motives; is loose mouthed about the confidential information so essential in banking; is a source of discord and friction; and is a nuisance generally.

I am reminded of the story of the teen-aged girls who were discussing their problem parents, and one young lady said that her principal worry was, "How did my mother find out all about the things she tells me I must not do?" Gentlemen, these witnesses may have been testifying as to the motives they would have and the general course of their conduct if they were not the management, but they have no right to assume that I, or others, must be tarred with the same brush, and who are we from whom the bank management wants protection? Just the stockholders who own the bank.

American business management, and particularly American bank management, has made a very neat reversal of corporate law in a perfectly legal way. By law the stockholders elect directors and the directors elect the bank officers, but as a matter of fact the bank's chief executive officers elect the directors through the exercise of management proxies. To whom does the director owe his job? The individual stockholder? No. Usually to the bank management, which he is supposed to control, oversee, and direct.

Gentlemen, all of this hue and cry to protect bank management has one great big hole in it. How many more bank stockholders are there in America than bank managers? I don't know, frankly, but I think it would be perfectly safe to say that the ratio is better than 1,000 to 1. I know that you gentlemen, as elected representatives of we, the people, are not going to aid and abet a small minority in its efforts to achieve complete domination of that large but inarticulate, unorganized group, the bank stockholders of this country.

Now, how did mandatory cumulative voting get into the statute books? Where was the ABA and its witnesses when mandatory cumulative voting was put into the law and for whose protection was it enacted? To the first part of the question my answer is that they were in many, many cases begging at the doorstep of the Reconstruction Finance Corporation for loans or trying to sell preferred stock to the RFC, so that they could keep their doors open; or they were sitting in the reception rooms of their Senators and Congressmen, impatiently waiting for an introduction to some RFC official, so that they could be saved. But was the United States Government, represented by the RFC, willing to buy stock in banks just to save the economy of the country? No; not as the law then stood on the books. But if Congress would make mandatory cumulative voting a prerequisite for the banks, the RFC would make the loans. And you did and they did and the ABA, if it did not say "Thank God," should have. Are all bank managers today so greatly different, so higher minded, such paragons of virtue, that this protection the RFC insisted upon is no longer needed? Is the individual stockholder of today so much richer, so much more powerful, so much less in need of protection, that he or she does not need what the RFC insisted upon?

I should like to read to you now a statement which appeared in a banker's magazine, as well as on pages 10 and 11 of the hearings before the House committee which I have furnished you, and when I finish I shall paraphrase it so that it will more accurately pinpoint the real danger that will result, not if cumulative voting is allowed to continue, but if it is allowed to be barred by statute. [Reading:]

This statement is made by Mr. Joseph E. Healy, president of Citizens National Bank of Hampton, Va. The absolute right now given to shareholders to vote stock on a cumulative basis would permit an irresponsible or unqualified individual, or one whose motives and interests might be in conflict with the best interests of a bank or the community, to acquire sufficient shares of stock in a national banking association and by means of a cumulative voting arrangement assure his election to the board of directors for his personal purposes. Situations have arisen where such minority shareholder elected as a director has conducted himself in a manner which has obstructed the orderly conduct of business of the board of directors, or which has resulted in the divulging to outsiders of confidential information about the business of the bank, its borrowing customers, and its depositors. Such directors have on occasion turned the board meeting into forums for discussion of personalities and matters detrimental to the harmonious operation of a sound bank. The responsibilities of the members of the board of directors are such that any serious discord or friction might shake the confidence of other shareholders or depositors and of the public. This is especially true in smaller communities. Minority shareholders elected to the board by virtue of cumulative voting, prompted by personal profit motives rather than by the best interests of the bank or the community, could demand the payment of excessive dividends in disregard of the condition of the bank at that time or of the better judgment of the majority of directors. They could also promote the sale or merger of a bank for the purpose of making a profit on their investments regardless as to whether the sale or merger would be in the best interests of the bank or of the welfare of the community. In addition, they could use their nuisance value to force other shareholders to buy them out at excessive prices.

The present cumulative voting provision can, under certain circumstances, give a majority representation on the board of directors of a national bank to a minority group of shareholders and thus put them in a position to obstruct the carrying out of the objectives of the majority of shareholders.

The percentage of shares held by the minority desiring to gain control of the board of directors need not be 40 percent, but could be a lesser percentage due to the fact that in larger banks with wide distribution of share ownership, many shareholders are negligent or indifferent in connection with fulfilling their voting prerogatives.

That is the end of Mr. Healy's statement. Now, here is my version:

The absolute right now given to shareholders to vote stock on a cumulative basis permits a sincere and qualified individual, whose motives are in accord with the best interests of the bank and of the community, to acquire sufficient shares of stock in a national banking association to assure his election to the board of directors so that he may serve the bank and those stockholders of the bank who, trusting him, and not being subject to the many pressures exerted by bank management, give him their proxies. Situations exist today where the majority-elected directors, under pressure from management, have entirely disregarded the best interests of their bank and the stockholders they are supposed to represent in order to keep minority-backed directors from being elected. Do they fear constructive criticism? Do they have something to hide?

Situations exist where majority-elected directors seek information and advice from the stockholder who has been denied a seat on the board of directors as to how they can make the changes that he has recommended—to date he has never failed to tell them—but wouldn't it be more efficient to have the man on the board where he could discuss the matters in detail?

Situations have arisen where such management-elected directors have conducted themselves in such a manner, namely, failure to file proper Federal income-tax returns, which has resulted in discredit, not only to the directors involved, but also to the bank. Such directors have on occasion allowed the board meetings to become meek acquiescence to all recommendations of the operating head of the bank rather than forums for the discussion of the results being achieved or not achieved by management as compared with those achieved by neighboring banks.

Majority shareholders elected to the board by the elimination of cumulative voting, prompted by personal profit motives, rather than by the best interests of the bank or community, could demand the payment of excessive dividends in disregard of the condition of the bank at that time or of the better judgment of the minority director, and the majority directors could approve such a dividend, whereas the minority director could not—he would be outvoted by the majority.

The management directors, being in the majority, could also promote the sale or merger of a bank for the purpose of making a profit on their investments regardless of whether the sale or merger would be in the interests of the bank, its stockholders, or of the welfare of the community, and if it was a two-thirds majority they could make it stick, whereas the minority director could not. In addition, they could use their control of proxies to force minority stockholders to either sell out to them at less than the real value of their shares or force the minority to pay excessively high prices for more stock in the hope that they could acquire enough to protect their already large investments.

The present cumulative voting provision cannot, under the usual existing circumstances, assure even a substantial minority of representation on the board of directors. Due to the expense involved, few men are willing to invest $15,000 in bank stock, spend $1,000 for attorney's fees and $500 to $1,000 for postage and printing bills in order to collect $675 in dividends and get involved in a proxy battle. I was, and still am, but not because of any hope for profit. I could do better buying U. S. Treasury bonds at 90 percent of par or tax-exempt bonds yielding 3 percent or better. But I am more concerned with seeing modern management methods installed in my community's national bank than I am in the profit.

The percentage of shares held by the management of many national banks is minute compared to that held by the large body of shareholders. Due to the indifference and negligence of most shareholders in exercising their voting prerogatives in person, management can effect the election of friends and those they can control as directors; management can recommend to directors that the directors receive attendance fees twice as large as those received by directors of other banks in the city; directors can vote larger salaries to the officers than those paid to the officers of banks that make twice as much money for their stockholders; management can obtain proxies at the bank's expense and use these same proxies to retain control of the bank. They not only can do this—they have done it in the American National Bank of Portsmouth, Va. Let the American Bankers Association come forward now and name one bank where a nonmanagement director has been able to get control of a bank board unless there is a case where the management was so inefficient that all directors, even management-appointed directors, turned out management. A minority cannot upset management.

The majority is entitled to control. They do at the polls on election day; they will again when your committee acts; they will again when the Congress finally acts upon this proposed bill, and they will again next election day. But in each of these instances a sincere but nonconforming minority is enttiled to be heard; their points of view compared with others presented; their basic arguments considered, and in many cases, their ideas are lifted by the majority and made a part of the majority program.

So if you gentlemen will refuse to recommend the proposed change in the National Banking Act on cumulative voting, you will be insuring the existence of democratic bank boards; if you do not, you will be inviting oligarchic bank boards to become dictatorships, which has through history generally resulted in the appearance of a tyrant. As a native Virginian, I know of no motto to equal "Sic Semper Tyrannis."

I thank you for your patience and will be happy to answer any questions to the best of my ability.

Senator ROBERTSON. Are there any questions?

Senator BENNETT. No questions.

Senator ROBERTSON. We thank you very much.

The next witness is Mr. Lewis D. Gilbert of New York. Will you please identify yourself for the record?

STATEMENT OF LEWIS D. GILBERT, NEW YORK, N. Y.

Mr. GILBERT. My name is Lewis D. Gilbert. I am appearing here today as a permanent investor in national bank shares. Together with other members of my family we own some 1,500 shares of such national banks as First National City of New York, National Bank of Detroit, National Bank of Tulsa, Okla., Wells Fargo and Crocker National of San Francisco, Fort Neck National and Rye National in suburban New York.

In addition, each year I represent a number of other public shareholders of First National City at the annual meeting, the democratic forum provided by law where the public shareholders can express their views and vote as they desire. I do so, of course, without ever charging any fee, as a public duty to my fellow owners who share my views of corporation democracy. I am not now, in the past or in the future interested in the control of any corporation or bank. I am also in correspondence with many other owners of national bank shares who have informed me on many occasions they share my general philosophy as to shareholder rights. [Reading:]

The first viewpoint I wish to present here today is that the public interest demands that the right of mandatory cumulative voting must be preserved. The interests of bank shareholders are not always the same as that of dominant bank management. Only the right to mandatory cumulative voting can provide the assurance of fair and equitable representation for all segments of the ownership.

We are now witnessing a growth of size of national banks. Expansion is in the air. In some cases it will be through the bank holding company to the extent permitted by law. In others it will be through creation of new branches in expanding city areas. This does not worry me, as I believe that the wheels of progress in our present economy must not be held back by horse-and-buggy thinking.

But this can only be safe doctrine if we are vigilant in seeing that oligarchy is not allowed to develop and maintain itself at the top of the pyramid. The channels of democratic control must remain in the hands of the ever-growing number of Americans now owning or who will own these banks in increasing numbers if the right of mandatory cumulative voting is maintained.

Experience has demonstrated that optional cumulative voting is not safe or in the public interest, because those who dislike being questioned at the meeting of the board of directors, in the manner, Senators, you question one another in the public interest, will not adopt, retain, or recommend it.

We hear much about the dangers of undesirable people coming into bank boards as a result of allowing mandatory cumulative voting to continue. I have but to recall to you the recent bank scandals at South Amboy, New Jersey, Ellenville, New York, or what happened in Illinois, as proof that we cannot have too much vigilance—and cumulative voting is one of the tools for doing just that.

I maintain that the banking authorities have the power to curb undesirable directors under other sections of this bill and, if it is not strong enough, I say to you, make it stronger. This and not the removal of the right of mandatory cumulative voting is the proper answer to the question of keeping the really undesirable people off bank boards.

Now, if I may, I should like to touch on the need for being sure that the right of the shareholders to have the list of fellow partners is maintained as it stands in the bill now before you. Some have urged on you that it should be made more difficult for owners to know who their partners are.

Let me now quote from the views of Senator Homer E. Capehart on this very subject. I am now reading from page 1328 of the recent stock-market study. Said the Senator from Indiana:

> Frankly, I would like to find some way to divulge the ownership of every share. I am a great believer that if I own one share of stock in a corporation and there is a proxy fight, then I think I ought to be able to go to the corporation before election time and receive the names and addresses of the owners of every share of stock. I believe that is a right I have as a stockholder, to know the names and addresses and the number of shares owned by every other stockholder.

Every word the Senator from Indiana stated at that hearing applies with even more vigor to the bank shareholders of the United States. They are getting so big that they are becoming sort of semipublic affairs—again borrowing the terminology of the distinguished gentleman from Indiana.

This question also brings us straight to the glaring omission of the present suggested revision of the banking laws. The time has very clearly come for putting these growing banks under the same rules in regard to proxy solicitation and full disclosure that fully listed corporations now must obey.

Therefore, on behalf of my fellow independent stockholders I ask that there be provision whereby the solicitation of proxies shall be required once a year at all national banks and the SEC or the Comptroller of the Currency or some similar agency shall be charged with the enforcement of the same kind of rules and regulations in this regard as we now have at SEC in the case of listed corporations.

This will insure for every American stockholder owning bank shares the right to know how many shares each director has in the bank, the top salaries and bonus payments, and the scale of pensions to top executives. It will insure the right of all the owners of a fair use of the proxy statement and will strengthen the confidence of shareholders in our banking system, just as it has in the case of large listed corporations.

Next, we want to be on record here as strongly protesting the granting of options to executives of banks, as provided for the first time on page 18 of the bill. There is no valid reason, in our opinion, for extending this to bank officers too. In our opinion options should never have been authorized by the Congress, in the general corporate world.

Recipients of options only exercise them if the price of the stock rises and the man who has one takes no risk. Sale of the stock results in capital-gains income, while we other taxpayers pay high income tax rates on all our earnings or from our dividends—and this includes the Senators of the United States, who get no options, for a job which is just as time-consuming, difficult, and important as the managing of the banks of the United States.

Nevertheless, if your committee and the Senators are still determined to grant the option right, then at least we should be assured that the options will not be for the purpose of encouraging speculation, but for bona fide investment. The way to insure this is to insist that they must be held for at least 3 years after exercise of the option, instead of the weak present 6-month period which enables an officer to pretend it is bought for "investment."

May I interpolate here. Senator Robertson, your most distinguished friend, Governor Battle, can emphasize what took place in the Virginia-Carolina situation, which is of great interest to you as a Senator from your State.

In conclusion, one word on yet another subject. In view of the need for encouraging more money to be on demand deposit, should we not take another look at the question of whether or not some degree of interest should be allowed on demand deposits? Now prohibited by Federal law, this makes me call to your attention that there is no other business in the country which gets its raw material for nothing—yet this is exactly what is done when a banker gets the use of money for nothing.

Certainly too high a rate of permitted interest can be very dangerous, but the absolute prohibition is equally ludicrous in the opinion of this witness.

I have now discussed the matters which the group of shareholders I represent here without compensation, as a public duty, thus exercising the citizen's right of petition, are concerned with in the pending banking legislation now before your body.

Thank you, Senator.

May I add one thing for the record for Mr. Rogers and for you? I have a statement here. This is from Mrs. Wilma Soss, who is from the Federation of Women Shareholders, who is not coming down and would like it filed in the record, with your permission.

Senator ROBERTSON. That may be filed. It has something to do with this bill?

Mr. GILBERT. It is her viewpoint and the members of the federation on the same bill.

Senator ROBERTSON. It may be filed.

(The statement of Mrs. Soss follows:)

STATEMENT OF WILMA SOSS, PRESIDENT, FEDERATION OF WOMEN SHAREHOLDERS IN AMERICAN BUSINESS, INC.

Re National Bank Act, Section 26, Subsection (c); Section 23 Shareholders' List; Listing of Bank Stocks; Regulation and Disclosure—the Platinum Curtain

Gentlemen of the Senate, the Federation of Women Shareholders in American Business, Inc., a nonprofit association of women for the protection of stockholder rights, capital, and income wishes to be recorded as opposed to the proposed elimination of the mandatory right to the cumulative voting of bank shares in the election of bank directors for the following reasons, which we ask to be made part of the printed record of these hearings.

Not to be repetitious, we also wish to be recorded as endorsing the written statement of Mr. Fred Walker, director of the First National Bank of Arlington, Arlington, Va., in opposition to the proposal to eliminate cumulative voting of the bank shares in the election of directors of national banking associations, unless provided for in the articles of association.

PROTECTING SMALL COMMUNITY BANKS

1. With the trend toward branch banks and holding companies cumulative voting is necessary for the protection of the small banks which may be absorbed through stock purchase or other means of control—otherwise ousting or overwhelming the local minority—and to help preserve the independent banking system in the United States.

SHORTCHANGING AND DISENFRANCHISING BANK SHARE OWNERS

2. The elimination of the mandatory cumulative voting right will partially disenfranchise bank share owners. Stockholders pay for the right to vote in the price of the shares they buy. Underwriters admit that stocks would have to sell for less if they did not carry voting rights. Taking away the right of cumulative voting means share owners in a national bank will not get in full what they may have paid for since, deprived of this right share owners are partially disabled—or disenfranchised—under the present proxy mechanism which concentrates power in the hands of the control group. Without a costly proxy fight it is impossible to secure so-called minority representation—that is, representation other than the minority control group—on the board; yet the directors are supposed to represent all the stockholders.

PERPETUATION OF A MINORITY-CONTROL GROUP IN THE MAJORITY OF CASES

3. Whereas cumulative voting is regarded as providing a means for minority representation, actually it also protects the majority.

"Theoretically, of course, the holders of a majority of the voting stock control a corporation but the assumption that the owners of common stock control a company is for the most part a fiction. * * * Control by a group other than the majority is the typical situation among the corporation giants.

"Minority control is much more common than majority control among the large companies. It arises where a compact group owns a substantial but minority interest which constitutes a majority of the stock actually represented at the stockholders' meetings, or to which the control group can attract a sufficient number of proxies from scattered holders to constitute a majority of such meeting. The latter rather than the former is the usual means of control.

"Once in power a minority group is difficult to dislodge. It has, of course, picked a management which is congenial and cooperative. Then the proxy machinery, with expenses paid by the company, is commonly at its disposal. The proxy committee is in effect chosen by the control group and is used as a means of perpetuating itself." Louis Loss, former assistant general counsel, SEC. Author: Securities Regulation (published, Little, Brown & Co., pp. 8, 9, 10, The American Background, Bubbles and Giants, Cupidity and Gullibility, ch. 1).

Mandatory cumulative voting rights provides a means of stockholder protection from this perpetuation of power by the minority control group which, so long as it is priviledge to vote proxies from an electroate that is allowed to get only limited disclosure, it is in a position to perpetuate itself indefinitely with social and business puppets who may be included on a board that, without cumualtive voting, is voted for as a package. No one is more keenly aware of this than those very persons who want to take away the right of cumulative voting to perpetuate in power minority-control groups which purport to represent the majority as Louis Loss has so clearly shown; and this may well be part of an effort to halt a growing demand for corporate democracy, an effort, incidentally, financed by the minority control groups out of the coffers of the public shareowners.

BEHIND THE PLATINUM CURTAIN

4. Elimination of mandatory cumulative voting rights is antidemocratic. One of the great dangers to our American way of life today is the emphasis on conformity made palatable as unity and teamwork. Unlike the Supreme Court, boards of directors never make public a minority report or dissenting opinion. In this platinum curtain of unanimity there is no indication that independent stockholder views have either representation or response. Yet, one of the arguments nearly always advanced by the management in opposition to cumulative voting is that it will impair unity or teamwork and thus be detrimental to the company when very often the opposite is true. The relentless demand for conformity frequently breeds frustration and has added to the increasing difficulty in getting men of stature to serve as directors.

DISCLOSURE

Banks must be brought under the rules and regulations of the SEC or some similarly constituted authority for banks so that full disclosure of salaries, pensions, and other data will be supplied to bank shareowners and that public stockholders will have the same rights of communication via the proxy statement as stockholders in public utilities and other industries.

We, therefore, in addition to asking for the maintaining of mandatory cumulative voting for stockholder protection, also petition this great committee to take such steps as may be within its authority to bring relief to stockholders from the platinum curtain which now exists between bank shareowners and directors and officers of their banks. They now dispense information at bank stockholder meeting concerning these matters as a matter of managerial largesse and individual choice rather than to accord it in the routine manner required under SEC rules and expected by public stockholders.

RE SECTION 23, SHARHOLDER LISTS

The proposed amendment of a statute to qualify the right of shareholders to inspect the stockholders list by providing that they may inspect the shareholders list only for a "proper purpose not inimical to the interest of the bank" is paternalistic and impractical. Who is to be the judge as to what is "inimical," the management or the shareowners, also whether the purpose of inspection is "inimical" to the bank or merely "inimical" to the minority-control group which runs the banks? This amendment might even prevent, under some circumstances, the management from having access to the stockholders lists. If lists are withheld on these grounds, it will increase litigation. What is "inimical" is a matter of judgement. Stockholders, many of whom are businessmen and women who are owners of banks, have a right as well as the management, to determine what is "inimical" to their property and their rights which must be included in the definition of "bank."

MAKE MANDATORY LISTING OF BANK STOCKS [1]

The Federation of Women Shareholders wishes to go on record as petitioning this committee to make mandatory the listing of bank stocks on the New York and other stock exchanges. When the Corn Exchange Bank of New York was merged with the Chemical Bank it was delisted from the New York Stock Exchange. In reply to protests at the Corn Exchange Bank meeting held to vote on the merger I was told that the Chemical Bank management did not wish to answer all the questions and come under the regulations required by the New York Stock Exchange, and therefore, the merged bank was not to be listed.

RE BANK MERGERS

(1) *Voting on bank mergers*

Many banks about to merge hold special meetings for stockholders to vote on the merger at the same hour and the same day in widely separated places. In this way coverage of the meetings are limited. More shareowners than you may suppose own stocks in the banks that merge. They, therefore, can attend only one of the meetings. This is also a hardship for the press and houses with financial interests; while they may be represented, quite obviously if one man is an authority or has followed a special situation, sending an alternate is irritating when mergers are in progress. There is no good reason why banks should schedule their meetings at the same time and many reasons why they should not. This apparently has to be regulated since the dictates of good public relations has failed to prevail.

(2) *Updating merged banks charters—Safeguarding voters*

When banks merge, they frequently become governed by the earliest charter or articles of incorporation which they are able to acquire. Naturally, they acquire the charter which seems to be most advantageous. It would appear that when banks are merged their charters should be updated especially in those cases where directors are allowed to vote for their own successors and shareowners continue to be disfranchised. In granting permission to banks to merge, it should also be provided that stockholders must have the right to elect directors. Therefore, we respectfully petition that this right shall be assured all shareowners of banks as a requirement that must be met before banks are allowed to merge.

Senator ROBERTSON. The next witness is Mr. William Leighton of New York. Mr. Leighton, do you have a prepared statement?

STATEMENT OF WILLIAM LEIGHTON, NEW YORK, N. Y.

Mr. LEIGHTON. No, sir. I have submitted a set of suggestions and your office has acknowledged it under your own signature. I believe it has been submitted.

Senator ROBERTSON. You want that filed?

Mr. LEIGHTON. Yes, sir; for the record.

Senator ROBERTSON. The Chair calls attention to the fact that under date of December 16, 1956, you wrote the chairman.

Mr. LEIGHTON. Yes, sir.

[1] We believe that the stock of merged banks should be listed on the stock exchange and these banks brought under the requirements for listing on the stock exchanges. When banks become bigger, they require more regulation and bank stockholders need more protection.

Senator ROBERTSON. You attached a little more than 12 single-spaced pages of suggestions which you said you made to our study after you had read the hearings of November 8, 9 and 10. In your letter, in the last paragraph, you said:

Some of my views have been preliminarily considered, at the suggestion of Senator Douglas, by Mr. William F. McKenna, counsel to the committee. None of my recommendations, however, have as yet been submitted to the staff, and I hope that you will find it possible to transmit them to Mr. Donald L. Rogers * * *.

That was done and Mr. McKenna also went into some matters referred to him by Senator Douglas at your request. I want to read a couple of paragraphs from the November 19, 1956, report of Mr. McKenna, who is counsel for our committee, to Mr. McCulloch, who is the administrative assistant to Senator Douglas.

In his November 12 memorandum to you concerning American Express Co.. Mr. William Leighton still presses for a committee investigation of the company's status as regards Federal regulation. As part of his request, he also wants each of the various Federal agencies he mentions to be compelled to make formal findings of facts concerning American Express Co.'s status vis-a-vis the particular agency. While he notes such findings of fact, if made, might afford a proper foundation for appropriate Federal legislation, he also seems to retain his opinion that in at least some of these cases the company will be found to come within the regulatory scope of present Federal statutes.

Each of the agencies he mentions—FDIC, SEC, and the Federal Reserve Board—as being in disagreement with Mr. Leighton's contentions as to the status of American Express Co., has already considered that status, but apparently not after a formal, factfinding procedure.

Mr. Leighton, as I stated, and without objection, we are going to put the 12 single-spaced pages of your recommendations in this record, but I want to ask you a frank question. Are you coming here to try to help us to write a banking law recodification, or is this a part of your vendetta on the American Express Co. on which you have asked our committee to have formal investigations of the SEC, the Federal Reserve Board, and the Federal Deposit Insurance Corporation because you do not agree with some practices of the American Express Co.?

Tell us frankly, what are you up to?

Mr. LEIGHTON. Sir, I did not come here to discuss my own, as you said, personal vendetta.

Senator ROBERTSON. Then whom do you represent?

Mr. LEIGHTON. Sir, I merely follow the request which you embodied in a press release when you asked all persons who have had the opportunity of examining your bill to present their views to this committee.

Senator ROBERTSON. Then you may proceed. However, you have heard the statement I made to other witnesses. We have to limit you and we cannot turn you loose to talk as long as you want.

Senator BENNETT. Do I understand he is going to discuss specific provisions of this bill and not discuss the problems of the American Express Co.?

Mr. LEIGHTON. Yes, Mr. Chairman. Specific provisions of this bill.

Senator ROBERTSON. He has assured us this is not a part of his fight against the American Express Co. But that is where it started and I thought it was only pertinent to know if this was a continuation of that fight.

Mr. LEIGHTON. No, sir.

Senator ROBERTSON. Or whether he is coming here to try to help us write a banking bill.

Mr. LEIGHTON. I have some specific suggestions.

Senator ROBERTSON. We went over his recommendations. We have 2 members of our advisory committee from New York—2 very splendid bankers—one being the chairman of the board of Chase-Manhattan, Mr. John J. McCloy, and the other, the executive vice president of the First National City Bank, Mr. Norris O. Johnson—both able men, and this witness never made any suggestions to them so that we could consider them in December when they met. However, he does file a statement, and one thing he wants is a trial de novo of every Federal agency. That is one thing you favor. Of course, the Federal Government never permitted that and it could not operate if every time a Federal agency does something a man could take them right into court and keep them there year after year and maybe could take them into the Supreme Court before anything they decided could become effective.

I know a lot of people say, "I am entitled to my day in court." They want to pick the court that they will have their day in, too. But as far as these banking matters are concerned, the chairman of this committee takes the position that the Federal Reserve Board in adjudicating matters under the Federal Reserve Act is the best court on those matters that we have in the Unied States and, therefore, there should be no appeal from them except under the Administrative Procedure Act, which means you can appeal from plain prejudice, bias, or illegal action, but as to the main facts you do not have a de novo trial.

Please try to be briefer than the chairman has been in introducing you.

Mr. LEIGHTON. Senator, I am very grateful to you that you have delineated the scope of my testimony. I wish to assure the committee I will not seek a hearing which I should have had in court. I will not do that.

Senator, the Supreme Court has decided only last month——

Senator BENNETT. Would the witness identify himself?

Mr. LEIGHTON. Yes. My name is William Leighton, of New York City, 15 West 74th Street.

Mr. Chairman, the Supreme Court has decided only last month the so-called doctrine of primary jurisdiction and administrative finality. It says, in the words of Mr. Justice Harlan, at title 352, United States Code, section 59, page 63:

> The doctrine of primary jurisdiction like the rule requiring exhaustion of administrative limit, is concerned with promoting proper relationships between the courts and administrative agencies charged with particularly regulatory duties.

Sir, this bill, which I think is the first time that we get a law embodying in one act all of the provisions concerning Federal banking, concerns itself with three or more administrative agencies. The first one is the Comptroller of the Currency. Section 3 says, "Office of the Comptroller of the Currency." I would most respectfully urge you, Senator, to insert a clause in the bill and state whether or not the Comptroller of the Currency is an agency of the United States and, if so, whether or not his decisions are subject to review in Federal courts under the Administrative Procedure Act.

If we would know exactly where to go and to which court we should appeal whenever the Comptroller of the Currency renders an adverse or unfavorable decision, then all doubts about the matter would be eliminated.

Mr. Fred Walker, of Arlington, Va., has introduced in the record a very long statement concerning inequities perpetrated by the Comptroller of the Currency. I most humbly suggest that the proper forum for such a complaint is the Federal court—to compel the Comptroller of the Currency to make findings of fact and reach conclusions of law upon the record developed in public hearings. That is the philosophy of the Administrative Procedure Act and, as you said in your preliminary statement, we have no quarrel with that, that is, as far as section 3 of the national bank bill is concerned.

Now section 11 says the Comptroller shall make an annual report to the Congress. My humble suggestion to that, Senator, is that the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Federal Reserve Board should make a joint annual report to the Congress at one specific time. Section 37 of the Federal Deposit Insurance Corporation Act says that they should.

Senator ROBERTSON. I was just going to say, I do not think anybody would challenge the fact that the Comptroller of the United States is an officer of the United States. It has been held that Members of Congress are officers of the United States because we take an oath. We are elected by the States but when we come into Washington we take an oath given by a Federal official to uphold and support the Constitution of the United States and we become officers of the United States.

The Comptroller of the Currency—and we will ask him about this when he comes Monday to testify before us—is granted and exercises discretion with respect to chartering national banks. You cannot take him into court to question his discretion. That is granted by law to him.

Mr. LEIGHTON. I appreciate that very much.

Senator ROBERTSON. But that is what you would like to do.

Mr. LEIGHTON. No, sir. Within the framework of the Administrative Procedure Act and no more.

Senator ROBERTSON. Well, the Administrative Procedure Act does not permit you to challenge the facts nor the discretion that is conferred upon a Federal agency or bureau or quasi-court. All it does is say they must not be arbitrary or capricious. They must be supported—they do not say by a preponderance of the evidence but they must be supported—by evidence, and that must be an action authorized by law. It cannot be illegal.

Mr. LEIGHTON. Yes, sir.

Senator ROBERTSON. To that extent I do not think there is any question about the fact that you could reach an action taken by the Comptroller of the Currency, but you cannot make out your case. That is the trouble.

Mr. LEIGHTON. Not in this particular case, sir, but I am suggesting as a matter of general law. You see, the Administrative Procedure Act is not specific as to the forum for judicial review. It says, any court of competent jurisdiction. Now which is the court of competent jurisdiction in the case of the Comptroller of the Currency.

We know in the case of the Securities and Exchange Commission we can have review in the Federal Court of Appeals; but it does not say—not in this bill and not in the present existing law—it does not say where and in which court we would have to go to reach the Comptroller of the Currency, and would it be proper——

Senator ROBERTSON. I do not know who framed that act, but maybe they did not want to encourage too much litigation and wanted to leave the matter a little in doubt. You could guess at it and if you got in the wrong court they would tell you so and you could try again. You may proceed.

Mr. LEIGHTON. Thank you. The next thing I am now coming to is section 30 of the National Bank Act as reproduced in your bill. Senator, I would humbly suggest in lieu of that section you should incorporate a provision patterned on section 42 of the Investment Company Act, which has a real punch.

The Securities and Exchange Commission is supervising now all of the Investment Company Act, which is a $9 billion a year business. The investment company business is prosperous. The investors have full confidence in the Securities and Exchange Commission's supervision and I believe section 42 of the Investment Company Act is a very wise provision, which has enabled the Commission to prevent abuses.

The Comptroller of the Currency is now complaining about abuses within the province of his jurisdiction. I suggest that section 42 of the Investment Company Act be considered.

There is another section in the Investment Company Act, Senator, which was not included in your bill and which, if I may again humbly suggest it, would greatly improve its administration. That is section 47 (a) and (b) of the Investment Company Act, which makes every contract drawn in violation of the act liable to be voided by a court of competent jurisdiction. That has eliminated a lot of litigation.

Senator ROBERTSON. How would you know what court it was if that language was not specific enough as to the court of competent jurisdiction?

Mr. LEIGHTON. Under the Investment Company Act and the competent Securities and Exchange Commission regulation we can go either to a State or a Federal court—preferably to a Federal court—because we have the Federal Rules of Civil Procedure and we do not have to post security for costs under applicable Federal causes of action and, therefore, we do feel much better in the Federal courts.

Sir, then we come to Section 31 (a) (7). The Comptroller there will decide I suppose within the area of his discretion what constitutes deposits. Now your bill, Senator, provides for the Federal Reserve Board to define deposits in section 41 of their own act, and for the Federal Deposit Insurance Corporation to define deposits under their section 2 (j) of their own act.

Senator ROBERTSON. May I ask you, do you enjoy litigation? Do you want to help us frame a bill which would promote litigation?

Mr. LEIGHTON. No, sir. I am merely suggesting——

Senator ROBERTSON. Your recommendations are aimed at opening up opportunities for litigation here.

Mr. LEIGHTON. No, sir.

Senator ROBERTSON. You may proceed.

Mr. LEIGHTON. But if I might suggest uniformity of definition, would you be agreeable to that, sir? Uniformity of definition of the word "deposit." Right now we have three independent agencies, each defining the word deposit in its own particular way. Your bill, so far as I understand it, sir, would make the Federal Reserve the ——

Senator ROBERTSON. The chairman is not going to interrupt the witness any more and will let him make his statement, but I would call attention to the fact that we are not legislating at this time on the Securities and Exchange Commission, and that has entirely different functions from the Federal Reserve Board, the Comptroller of the Currency, and the Federal Deposit Insurance Corporation, on whom we are legislating.

Please proceed, but with some expedition I suggest.

Mr. LEIGHTON. Sir, section 32 of the National Bank Act also defines the term "investment securities." National banks are going to be prohibited by law from dealing in investment securities. I humbly suggest that the Comptroller should jointly with the Federal Reserve Board and other agencies define the term "investment securities." We should not have one definition for the securities registration and another definition for the National Bank Act.

Uniformity of definition, Senator, I believe, is very much desirable in order to prevent litigation in the Federal courts, because otherwise we have to grope around and find out just what we mean by the word "securities." Right now we have five different definitions of securities.

Senator ROBERTSON. That is the existing law.

Mr. LEIGHTON. I beg your pardon.

Senator ROBERTSON. You are complaining of the existing law and not what we are trying to do here. You are asking us to change existing law.

Mr. LEIGHTON. Yes, sir.

Senator ROBERTSON. All right. Go ahead.

Mr. LEIGHTON. Now, the Comptroller has complained in his recommendation No. 43, that an organization in Texas, a corporation incorporated under the laws of Texas, had to accept deposits under his own definition of deposits and then the corporation went bankrupt; and the Comptroller suggests in his recommendation 43, I believe, that the law be strengthened in that respect.

Sir, the word "deposits" can mean a lot of things. Again I suggest that the Comptroller should be required to define by regulation, jointly with the Federal Reserve Board and the Federal Deposit Insurance Corporation, just what constitutes "deposit." They should define whether or not it is a money deposit for the purpose of section 44 of the Comptroller's Act, or whether it is an assessable deposit for the purpose of the Federal Deposit Insurance Corporation Act, or whether it is a deposit for the purpose of section 45 of the Federal Reserve Board's Act, or for the purpose of section 41 of the Federal Reserve Board's Act.

There should be a joint definition of the word "deposit" uniformly arrived at.

I believe that the best way to bring that result about is to require the agencies to get together and define that word—that simple word—"deposits." Right now they each define it in their own particular way.

When Mr. Coburn was testifying before this committee during the November hearings he objected to a thorough examination being made of the Federal Deposit Insurance Corporation insured banks. He said, "An examination will do." I most humbly suggest, Senator, that the word "thorough" should be left where it is now. The examination should be thorough. You cannot too thoroughly examine the affairs of banks.

As Mr. Gilbert just said, several things did happen in Ellenville although the Federal Deposit Insurance Corporation did examine them and the Comptroller had examined the national bank. Apparently even a thorough examination will not detect certain manipulations in customer deposits.

I come now to section 66 of the Comptroller's bill which says:

(a) The actions, regulations, rules, licenses, orders, and proclamations heretofore or hereafter taken, promulgated, made, or issued by the President of the United States or the Secretary of the Treasury since March 4, 1933, pursuant to the authority conferred by subdivision (b) of section 5 of the act of October 6, 1917, as amended, are hereby approved and confirmed.

That is the Trading With the Enemy Act, and I believe I should bring this to your notice. I have just taken this matter up with the State Department because on May 25, 1946, there was signed in Washington, D. C., a so-called act between the United States, France, Great Britain, and Switzerland, that disposed of the German assets in Switzerland, but it had a little clause, and you will not find that accord in the United States Statutes translation.

Senator ROBERTSON. Did you have some financial interest in those assets?

Mr. LEIGHTON. No, sir; not at all, but it is just a matter of interest.

Senator ROBERTSON. You are taking the issue up with the State Department as a matter of interest?

Mr. LEIGHTON. No. I am merely pointing out the fact that an international agreement other than the treaty has not been published in the United States Statutes at Large pursuant to law.

Senator ROBERTSON. All right.

Mr. LEIGHTON. That agreement, which you will find at 14 Department of State Bulletin 1121, states as follows:

PARAGRAPH 41. The Government of the United States will unblock Swiss assets in the United States. The necessary procedure will be determined without delay.

Similar agreements with Sweden and Spain have been published in the United States Statutes at Large because it was a requirement of law. This agreement was not so published for reasons which the State Department says as follows: It has never been intended to publish it.

Senator ROBERTSON. Is my inference correct that you take sort of a dim view of the way a lot of our Federal agencies function?

Mr. LEIGHTON. No, sir. I am merely pointing out, shall I say, gaps in the administration of the laws. The purpose of this committee, I believe, is to improve the administration of the laws, and that is all I am pointing out, sir.

Senator ROBERTSON. You may proceed.

Mr. LEIGHTON. Thank you, sir. The Secretary of the Treasury then prescribes a procedure 6 months later whereby Swiss citizens were entitled to claim their blocked assets in the United States. He did not publish that procedure in the Federal Register as required by the Administrative Procedure Act. He published it in the Swiss Government's official publications.

84444—57—pt. 2——21

Section 69 provides for the venue of actions. May I respectfully suggest that the proper forum for convenience be prescribed by the Congress whenever dealing with a Federal law. This section 69 of the Comptroller's bill is apt to be interpreted under State rules of procedure. I would humbly suggest that the State courts should be required to apply the Federal Rules of Civil Procedure to actions based on Federal statute.

Senator BENNETT. Again is that not far outside the scope of this bank law?

Senator ROBERTSON. I think he is soon going to conclude so I will not interrupt him any further.

Senator BENNETT. May I ask you if section 69 is a continuation of existing law?

Mr. ROGERS. Yes, sir.

Senator BENNETT. Thank you.

Mr. LEIGHTON. Now the Board of Governors of the Federal Reserve System is or is not a suitable entity. The Administrative Procedure Act does provide for remedy at law. That has to be exhausted. That is the holding of the Supreme Court. Right now under the Bank Holding Company Act of 1956 the Board's actions and decisions, and so forth, may be challenged before the United States court of appeals. What happens under section 45 of the Board's bill? There is no provision in that bill as to whether or not the Board's actions under such section 45 are similarly challengeable before a United States court of appeals, and that, sir, is a very important section.

The Federal Reserve Act, section 25 (a), has been the object of 2 years' debate, during 1918 and 1919. It became what is known as the Edge Act. The late Senator Edge considered it as the milestone in his career. The various Senators who had participated in the debates—and I have gone through the congressional hearings very carefully—the very Senators considered that it would affect the foreign banking business of the United States to the greatest extent. The Board will be the administrative agency charged with supervising this foreign banking business.

Thirty-three years later, sir, the Board has licensed three corporations altogether under section 25 (a), one of which was licensed only in 1955.

Now my humble recommendation, sir, or suggestion, if I may correct the record, is that the Congress should enact a declaration of policy modeled on section 1 of the Investment Company Act. It is for the Congress to declare the policy and it is not for the Board. The Board can recommend the policy; the Congress should declare it.

This committee has jurisdiction over the interstate and foreign banking business of the United States. It has jurisdiction over interstate and foreign commerce. It should not entrust lawmaking activities to the Board. The Board should not tell whether or not a particular act of Congress applies. It is for the Congress to decide that. If there is any doubt at all about the importance of the present effect of section 25 (a) of the Federal Reserve Act then I humbly suggest the Congress should decide the extent of the applicable area where that legislation should be enforced, and not the Board. Right now the Board has done nothing in that respect—absolutely nothing.

The Board has two corporations licensed prior to 1955. It has licensed a third corporation since 1955. Everybody else is operating under particular State law.

I am submitting most humbly to this committee the question as to whether or not the regulation of interstate and foreign banking should come under the jurisdiction of Congress or the jurisdiction of the several States. Again that is a question to be decided by the Congress, and I am merely presenting it, sir.

Senator BENNETT. We have the question now before us. The witness has tended a little occasionally to repeat himself a number of times, and I am looking at the clock. I hope he can hurry along without repetition.

Mr. LEIGHTON. I am sorry, Senator. I will try to be brief.

Now we come to our old friend, "Deposits." The Federal Reserve Board will define deposits for the purpose of section 41 of its own act. The Federal Deposit Insurance Corporation will define deposits——

Senator BENNETT. I think the witness made it perfectly clear as to his interest in that particular question. Is this not repetitive to what we have already heard?

Mr. LEIGHTON. It is not.

Senator BENNETT. You raised the question of the Federal Reserve's definition at the time you raised the question of the Comptroller's definition.

Mr. LEIGHTON. I would like to point out that several deposits upon which a bank is primarily liable these days include travelers' checks, that is, upon which a bank is primarily liable. There is quite a wide area of discretion given the Administrator of the Federal Deposit Insurance Corporation in this bill. I would humbly suggest that a $3 billion a year business, and an interstate business, should be regulated more closely than it is now.

Senator BENNETT. Are we coming back into the area of your quarrel with the American Express Co.?

Mr. LEIGHTON. I have not mentioned it yet, sir. I am merely keeping within the scope of the chairman's direction.

Senator ROBERTSON. The Chair will ask the witness to try to summarize the remainder of his oral observations in 10 minutes. He has already taken nearly 25 minutes, and we have in the record his full statement, which gives the present law. the proposed changes, and the reasons for the proposed changes. They will appear in full in the record.

Mr. LEIGHTON. All right, sir.

Senator ROBERTSON. The witness is now summarizing what will be printed in full, and is just putting it in the record twice and doing it at the expense of members of the committee who have a lot of other things pending.

Mr. LEIGHTON. Sir, there is an Advisory Committee Recommendation 115–F. That is the old question of the payment of interest on demand deposits. The Federal Deposit Insurance Corporation reached one conclusion of law; the Federal Reserve Board reached another conclusion of law. The two agencies could not agree. They want this committee to recommend corrective legislation.

Sir, if I may humbly suggest that the Administrative Procedure Act now provides the proper procedure for reconciling the conflicting viewpoints of the Federal Reserve Board and the Federal Deposit

Insurance Corporation with respect to demand deposits, payment of interest on demand deposits and the absorption of charges. Again I wish respectfully to suggest that this committee should not consider additional legislation if existing legislation is not complied with by the two Federal agencies. They can sort out their differences in a Federal Court of Appeals. The Federal Court of Appeals will then decide which agency has jurisdiction in which particular field, just as the Interstate Commerce Commission has been sued by the United States Department of Justice in 337 U. S., and so forth.

Senator ROBERTSON. Which would you prefer? To have the Federal Reserve Board sue the Federal Deposit Insurance Corporation, or have the Federal Deposit Insurance Corporation sue the Federal Reserve Board?

Mr. LEIGHTON. No, sir. I would just like to have a declaratory judgment by a competent court as to just what is the area of jurisdiction right now.

Senator ROBERTSON. We thank you very much.

Mr. LEIGHTON. Thank you.

Senator ROBERTSON. The letter of Mr. Leighton to me with the accompanying recommendations without objection will be made a part of the record at this point.

(The documents referred to follow:)

NEW YORK, N. Y., *December 16, 1956.*

Hon. A. WILLIS ROBERTSON,
Committee on Banking and Currency,
United States Senate, Washington, D. C.

DEAR SENATOR ROBERTSON: After reading the transcript of the hearings held on November 9 and 10 under your chairmanship, I have compiled the enclosed recommendations based upon my practical experience with the Federal regulatory agencies. I know that many of my views will be the subject of controversy. However, I feel that the thorough revision of the banking laws which is contemplated by the Senate Resolution 155 would be nullified if certain aspects of interstate banking are not considered and investigated.

I respectfully request to be heard by the committee at any time during the hearings in January and February and trust that I shall be privileged to offer the benefit of my practical experience with the Federal regulatory agencies in furtherance of the committee's purpose.

Some of my views have been preliminarily considered, at the suggestion of Senator Douglas, by Mr. William F. McKenna, counsel to the committee. None of my recommendations, however, have as yet been submitted to the staff, and I hope that you will find it possible to transmit them to Mr. Donald L. Rogers, for inclusion in the committee print of the bill, which as you said on November 9, would merely serve as the basis for public hearings.

Very truly yours,

WILLIAM LEIGHTON.

RECOMMENDATIONS OF WILLIAM LEIGHTON

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

1. The Board as a suable entity

Existing Law: Section 9 of the Bank Holding Company Act of 1956. Section 11 of the Clayton Anti-Trust Act as amended. Judicial Review Act of 1950, 64 Stat. 1129. Administrative Procedure Act of 1946.

Controlling litigation: *Board of Governors of the Federal Reserve System* v. *Transamerica Corporation* (346 U. S. 901, 206 F.2d 163), *Leighton* v. *Ravndal et al.*, Civil No. 5439–55 (U. S. D. C., D. C. (unreported)).

Recommendation: Amend section 10 of the Federal Reserve Act (12 U. S. C. Section 241) by specifically providing that the Board is a suable entity in the manner provided by section 9 of the Federal Deposit Insurance Act with respect to F. D. I. C. and the securities laws with respect to the S. E. C.

Amend Judicial Review Act of 1950 by specifically providing for judisdiction of U. S. Courts of Appeals in cases where the board's orders, rules, regulations or other type of "agency action" within the meaning of Administrative Procedure Act is challenged in the courts.

Reasons: As a suable entity, the Board was a party litigant in Transamerica but it is not clear whether the Board defended through the office of the U. S. Attorney or appeared in court eo nomine.

In *Leighton* v. *Ravndal et al.*, the Board maintained that it was not a suable entity and this view was upheld by Judge McGarraghy. The case involved "agency action" by the Board under section 25 (a) of the Federal Reserve Act and, absent an express provision for judicial review by a U. S. Court of Appeals, District Court's jurisdiction was not challenged by the parties.

It seems anomalous that the Board should be a "suable entity" for the purpose of the Bank Holding Company Act of 1956 and the Clayton Act, but not for the purpose of judicial review of its "agency action" taken under the Federal Reserve Act. It is also anomalous that the Board should require that petitions for the review of such agency actions should be served on the U. S. Attorney. A review proceeding is civil in nature and does not require the concurrence of the U. S. Justice Department as to the correctness of the agency action in issue.

2. Banking corporations authorized to do foreign banking business

Existing law: Section 25 (a) of the Federal Reserve Act (12 U. S. C., secs. 611–631, 41 Stat. 378, commonly known as the Edge Act).

Recommendation: Amend section to include a declaration of policy modeled on section 1 of the Investment Company Act of 1940 (15 U. S. C., sec. 80a), and on section 302 of the Trust Indenture Act of 1939 (15 U. S. C., sec. 77bbb).

Amend section to include a provision modeled on section 47 (a) and (b) of the Investment Company Act designed to invalidate contracts made in violation of statute.

Amend section to provide for appellate review of Board's orders, rules, and regulations issued thereunder, patterned on section 9 of the Bank Holding Company Act of 1956.

Controlling litigation: *Apfel* v. *Mellon* (33 F. 2d 805); *Travis* v. *National City Bank of New York* (23 F. Supp. 363); *Leighton* v. *Ravndal et al.*, Civil No. 5439–55 (U. S. D. C., D. C. (unreported)), transferred to the southern district of New York under Civil No. 107–345 (unreported).

Reasons: Although enacted in 1919, only 2 corporations were licensed by the Board prior to 1955 and 1 corporation has been licensed during that year. The Board has recently proposed to amend its regulation K (12 C. F. R., pt. 211; see 21 F. R. 1867 (Mar. 26, 1956)).

Contrary to the plain intent of the statute (as found by the court in *Travis*), the Board has taken the position that incorporation thereunder is permissive and not mandatory. In doing so, the Board has declared the meaning of legislation enacted by Congress pursuant to its commerce power. This the Board is without jurisdiction to do because "the interpretation of the meaning of statutes as applied to justiciable controversies is exclusively a judicial function. This duty requires one body of public servants, the judges, to construe the meaning that another body, the legislators, said," *United States* v. *American Trucking Association* (310 U. S. 534, 544).

The suggested enactment of a declaration of policy will, in effect, revert to Congress the power to declare the meaning of the statute. The Board should be enjoined, by suitable legislative language, from declaring the meaning of legislation otherwise than by order, rule, or regulation formulated in accordance with the requirements of the Administrative Procedure Act.

The inclusion of a provision modeled on section 47 (a) and (b) of the Investment Company Act will result in the enactment into positive law of the proposition that contracts which are contrary to the requirements of the statute are void whether expressly made so by statute or not, *Lakos* v. *Saliaris* (116 F. 2d. 440).

In *Leighton* v. *Ravndal et al.*, supra (U. S. D. C., S. D. N. Y.), Judge Palmieri dismissed a cause of action based on the violation of the Edge Act by an unincorporated aggregation of individuals who have made and sold obligations or contracts contrary to the registration requirements of the act. No opinion was filed by the court in this case.

3. Member banks of the Federal Reserve System as prime obligors on securities not issued by them

A. *As a result of the endorsement by such banks of instruments submitted for clearance through the Federal Reserve banks.—*

Existing law: Regulation J (12 C. F. R. 210, based on 12 U. S. C., sec. 360 and 342; Trust Indenture Act of 1939 (15 U. S. C., sec. 77aaa).

Recommendation: Amend Federal Reserve Act to provide that member banks may endorse and collect through regulation J facilities only—

(i) obligations of other member banks or checks and drafts drawn on such banks; and

(ii) obligations of member banks of the FDIC subject to the $10,000 insurance limitation on each account; and

(iii) such other obligations of nonmember institutions as are payable through a member bank or member of the FDIC where such member has been appointed as "paying agent" under an indenture effective pursuant to the Trust Indenture Act of 1939.

Reasons: During 1955, $2,300,000,000 worth of travelers checks have been sold and redeemed in interstate commerce, largely through the use of regulation J facilities, by the major issuer of such checks, which is an unincorporated aggregation of individuals. Member banks having redeemed such checks as a matter of choice, collect their par value through regulation J facilities, for which purpose they endorse the instruments. Having done so, member banks become a prime obligor on the instrument vis-a-vis the Federal Reserve banks in the event payment is refused by the nonmember drawee. Since the individual having cashed such checks at the member bank is not always a depositor and, in the great majority of redemptions, cash is issued by the member bank against the instrument, it follows that during the process of collection, such bank is but a common creditor of the unincorporated aggregation of individuals. In the absence of an effective indenture under the Trust Indenture Act as to such instruments, it follows that member banks are presently financing, at their own risk, the redemptions of these instruments.

The travelers' checks of this particular issuer have been held to be evidences of indebtedness and obligations to pay money for the purpose of the Trading With the Enemy Act (see vesting order 9022, 12 F. R. 3880, vesting order 7814, 11 F. R. 13919, vesting order 7665, 11 F. R. 13951, vesting order 11116, 13 F. R. 2502). Since the issuer has complied with such orders, it follows that he has conceded the legal definition of the instruments and the nature of the transaction. This definition should be followed for the purpose of the suggested amendment.

For member banks' liability in this respect under the Federal Deposit Insurance Act, see recommendations under that heading.

B. *As a result of the issuance by certain member banks of securities registered under the Securities Act of 1933.—*

Existing law: Securities Act of 1933; section 25 (a) of the Federal Reserve Act.

Recommendation: Amend section 25 (a) of the Federal Reserve Act to define the liability of any member bank having issued negotiable certificates for the deposit of securities against the deposit of such securities in foreign countries.

Reason: Since May 1955, three member banks of the Federal Reserve System have issued such certificates. In November 1955, after they have been traded over the counter for almost 6 months, SEC ruled that such certificates are securities subject to registration under the Securities Act of 1933 and required their registration.

The issuance of these certificates is designed to facilitate trading in the foreign securties which they represent, as well as the collection of dividends and the exercise of any accruing rights. Example: An American investor wishes to own stock in Montecatini S. A., the leading Italian chemical concern. He buys over the counter a certificate for the deposit of Montecatini shares, issued by J. P. Morgan, Inc. In turn, J. P. Morgan holds the original security on deposit with its correspondent in Italy. Dividends and accruing rights are credited to J. P. Morgan's account in Italy and disbursed to the American holder of the certificate in the United States.

In the event Italian assets in the United States would be blocked under the Trading With the Enemy Act (as they have been during World War II), J. P. Morgan's security account in Italy would almost certainly be blocked by the Italian authorities. Hence, the American holder of the J. P. Morgan certificate would have a claim against J. P. Morgan, and not against Montecatini.

As originally enacted, the Edge Act did not envisage such types of operations by banks engaged in the foreign banking business. The statute should be amended to define the maximum liability of the issuers of certificates for the deposit of securities as well as their fiduciary duties toward holders of such certificates.

4. *Foreign banking operations of corporations organized under the laws of the United States*

Existing law: Section 25 (b) of the Federal Reserve Act (12 U. S. C., sec. 632); Banking Act of 1933, as amended; Federal Reserve Act of 1913; Federal Deposit Insurance Act.

Recommendation: Amend section 25 (b) of the Federal Reserve Act to define the term "corporations organized under the laws of the United States."

Controlling litigation: *Travis* v. *National City Bank of the New York* (23 F. Supp. 363); *Leighton* v. *Ravndal et al.*, Civil No. 107-345 (U. S. D. C., S. D. N. Y. (unreported)).

Reasons: In analyzing the legislative history of sections 25 (a) and (b) of the Federal Reserve Act, Judge Galston held in Travis that the jurisdiction of Federal courts over the foreign banking operations of corporations organized under the laws of the United States obtains even though such corporations are not organized under the Edge Act.

An important policy question appears as a result of the membership of the several banks in the Federal Reserve System and in the FDIC. Are such member banks, to the extent that they are incorporated, "corporations organized under the laws of the United States"?

In this respect, the following colloquy between Senator Robertson, acting chairman of the Senate Banking and Currency Committee for a study of the Federal statutes governing financial institutions, and Mr. Neil G. Greensides, acting assistant to the Chairman of the FDIC, has been reported in the committee's record of the hearings held on November 10, 1956:

Senator ROBERTSON. I understand we have 13,439 banks that are insured.

Mr. GREENSIDES. Yes, sir.

Senator ROBERTSON. And the Supreme Court has held that whenever a bank voluntarily comes into your control program they submit to the jurisdiction of the Federal Government.

Mr. GREENSIDES. Yes, sir (p. 307).

If it be the sense of the Senate, and ultimately of the Congress, that corporations which are members of the FDIC are organized under the laws of the United States, then such corporations' foreign banking operations come under the jurisdiction of the Federal courts under section 25 (b). The Federal Deposit Insurance Act has been enacted long after section 25 (b) of the Federal Reserve Act conferred jurisdiction on Federal courts "notwithstanding any other law." Such other law would appear to be any law of the several States permitting the incorporation of a business unit for the purpose of engaging in the banking business.

Essentially, any foreign banking operation involves the deposit of money with a bank in the United States for the performance of certain obligations by the bank's correspondent abroad, or the reverse. Since the interpretation of treaties, such as the double taxation agreements with foreign countries may be involved, or questions relating to the foreign equivalent of the Trading With the Enemy Act may arise, jurisdiction over suits involving such matters should be expressly conferred on the Federal courts.

The courts give particular weight to statements by legislators as indicating the sense of the Congress in enacting a particular law. Senator Robertson's question, as affirmatively answered by Mr. Greensides, would indicate his understanding that banks which are members of the FDIC are subject to the jurisdiction of the Federal Government, in the sense that they are corporations organized under the laws of the United States. The enactment into positive law of the Senator's understanding would eliminate considerable uncertainty as to the jurisdictional scope of section 25 (b). Such uncertainty is indicated by Judge Palmieri's dismissal, without opinion, of a count alleging violation of the Federal Deposit Insurance Act by a corporation engaged in the foreign banking business by virtue of the laws of Connecticut, rather than pursuant to the Edge Act, *Leighton* v. *Ravndal*, *supra*.

5. *Applicability of the doctrine of primary jurisdiction and administrative finality to suits based on the Federal Reserve Act and the regulations promulgated thereunder*

Existing law: Administrative Procedure Act of 1946.

Controlling litigation: *Far Eastern Conference* v. *United States* (342 U. S. 570 (1952)); *Rochester Telephone Corporation* v. *United States* (307 U. S. 125 (1939)); *Philadelphia Co.* v. *S. E. C.* (164 F. 2d 889, certiorari denied, 333 U. S. 828. and 175 F. 2d 808, vacated as moot, 337 U. S. 901).

Recommendation: Amend Federal Reserve Act to confer mandatory jurisdiction on the Board of Governors of the Federal Reserve System for the performance of factfinding duties in specified matters which do not fall within the conventional experience of judges.

Amend Federal Reserve Act to require the Board, upon the complaint of any aggrieved person, to reach primary conclusions of law by order, upon the consideration of such findings of fact.

Amend Federal Reserve Act to provide for the judicial review of the Board's orders in such cases in the Federal district courts consistent with the doctrine of split review.

Reasons: The proposed amendments would enact into positive law the sweeping doctrine of Far Eastern Conference, which the Board has failed to follow. Practically any suit under the Federal Reserve Act, or the regulations promulgated thereunder, is bound to allege the violation of some statutory provision or the enforcement of certain rights based on the statute. If the policy of the Congress is to require the courts and the Federal agencies to act as related and interdependent instrumentalities of justice, the Board, as one such agency, should be required by statute to perform the duties of making findings of fact either directly, or through the Federal Reserve agents, or through hearing examiners sitting in the several Federal Reserve districts.

Judicial review of the Board's orders in such cases should be performed by the Federal district courts consistent with the doctrine of split review (*General Protective Committee* v. *S. E. C.*, 346 U. S. 521 (1953)). This procedure would enable the aggrieved person to allege causes of actions not based on the Federal Reserve Act but arising out of the same set of facts. A consolidation of actions is then possible under rule 42 (a) of the Federal Rules of Civil Procedure. thus reducing the volume of litigation in the Federal courts.

FEDERAL DEPOSIT INSURANCE CORPORATION

1. *Definition of the term "deposit," section 3 (1) of the Federal Deposit Insurance Act*

Existing law: Section 3 (1) of the act as set forth under FDIC recommendation No. 89 to the committee.

Controlling litigation: *F. D. I. C.* v. *Irving Trust Company et al.* (137 F. Supp. 145 (1956)).

Recommendation: Amend subsection to provide a uniform definition of the term "deposit" for the purpose of the Federal Deposit Insurance Act, section 25 (a) of the Federal Reserve Act (12 U. S. C. 615 (a)), and section 12 of the Banking Act of 1933, as amended by section 303 of the Banking Act of 1935 (12 U. S. C. 378) (recommendation No. 36 of the Comptroller of the Currency).

Amend subsection to define liability of any person acting pursuant to regulations prescribed by FDIC.

Reasons: The term "deposit" should be uniformly defined for the purpose of the 3 cited acts in order to avoid confusion as to whether or not the FDIC definition is "commonly known" whenever the other 2 acts are enforced or interpreted.

FDIC Regulation 326 has been promulgated under the authority of the present law but has not ben uniformly enforced by FDIC itself, see page 165 of the opinion in Irving Trust Company. It is both unfair and arbitrary for FDIC to acquiesce for 10 or 14 years in the manner in which assessment returns are compiled by certain banks and then to sue in order to force such banks to revise the assessment basis. If a bank compiles its assessment returns in accordance with FDIC regulations, then it should be free from liability toward FDIC upon completion of FDIC's audit of the returns, or within a specified period thereafter. For a comparable provision in the securities laws see, e. g., section 319 (c) of the Trust Indenture Act of 1939. In the Irving Trust case, FDIC brought suit to recover unpaid assessments past due for 10 and 14 years respectively, but under the 5-year statute of limitations, since the banks were not held liable for false or fraudulent assessment returns intentionally made.

The definition of "deposit" should be uniformly applied by FDIC itself without a 14-year waiting period as in Irving. At the present time, FDIC arbitrarily applies its definition of "deposit" contained in regulation 326 (c) with the result that the obligations of certain banks are deemed to be "assessable deposits" whereas the identical obligations of a nonbank are not deemed to be in this category. Example:

Traveler's checks are currently sold in huge amounts throughout the United States by both banks and nonbanks. There are three major insured issuers, the Bank of America N. T. & S. A. of San Francisco, the First National City Bank of New York, and the First National Bank of Chicago. Under regulation 326 (c), each of these issuers includes the value of its outstanding traveler's checks in its assessment base. The holders of such checks, whether they be the original purchasers or the payees, are "depositors" and have a claim to an insured deposit.

However, the major issuer of traveler's checks is American Express Co., an unincorporated aggregation of individuals (*Doud* v. *Hodge*, 127 F. Supp. 853, 855), an institution which is not insured by FDIC. Since American Express is primarily liable on traveler's checks issued by it, such liability would result in the inclusion of its outstanding traveler's checks in its assessment base, if it were FDIC insured.

In other words, if American Express were insured by FDIC, the holders of its traveler's checks would also have a claim to insured deposits in like manner as the holders of traveler's checks issued by insured banks.

Furthermore, if American Express would be on an insured status, all of its outstanding traveler's checks would constitute "deposits" under regulation 326 (c) and hence the requirement of State supervision would apply (12 U. S. C. 378).

Because of the wide divergence between the Comptroller of the Currency's concept of "deposit" and the FDIC's, American Express, an unincorporated aggregation of individuals, has not been required by the Comptroller to submit to any supervision or examination by any State supervisory authority. The result is that the holders of American Express traveler's checks have no FDIC insurance protection of their deposits and their status is reduced to that of common creditors of an unincorporated aggregation of individuals not suable in the Federal courts on the basis of diversity (*Van Sant* v. *American Express Company*, 169 F. 2d 355, 371).

2. *Definition of "transferred deposit"*

Existing law: Section 3 (n) of the Federal Deposit Insurance Act; section 3 (*l*) of the Federal Deposit Insurance Act.

Recommendation: Amend section 3 (n) to provide that whenever an insured bank receives a payment of money at any of its teller stations displaying the FDIC insured sign, such moneys, if not retained by the bank as a deposit to an account carried on its books or as trust funds, should be transferable only to an FDIC-insured institution: define the liability of both transferring and transferee banks in transactions of this type.

Reasons: Transactions involving the transfer of deposits made at insured tellers' stations occur whenever an insured bank sells at its tellers' stations the traveler's checks of another insured bank. Example:

A person who is a depositor of Riggs National Bank in Washington, D. C., desires to purchase $10,000 in traveler's checks issued by the First National City Bank of New York. Such person will ordinarily draw a check on Riggs for $10,100 and receive in exchange the traveler's checks. The proceeds of the check, less Riggs' commission, will be forwarded to First National City together with the details of the transaction. Whereupon First National City includes the $10,000 of its traveler's checks in the assessment base. While Riggs' depositor has deposited $10,100 in insured funds in exchange for obligations upon which Riggs is not primarily liable, such obligations evidence an insured deposit in First National City and the depositor is covered by FDIC. Essentially, the transaction involves the transfer of an insured deposit from Riggs to First National City.

However, if Riggs' depositor were to buy American Express traveler's checks, Riggs would be transferring the $10,000 to American Express, an uninsured institution. The evils attendant upon this type of transaction are set forth under FDIC recommendation No. 89 submitted to the committee. There is no difference between the trust funds, which FDIC suggests should be transferred only to an insured institution, and the proceeds of the sale of traveler's checks similarly transferred.

In practice, insured banks are primarily liable on the traveler's checks not issued by them, "as a matter of choice." In other words, if the holder of the

$10,000 of traveler's checks would decide to redeem them, Riggs would pay upon them "as a matter of choice" even though it is not primarily liable on them and even though it does not ordinarily charge the issuer's account with the value of redeemed traveler's checks. Redeemed traveler's checks are usually sent on for collection through FRB Regulation J facilities precisely because the issuers do not maintain sufficient balances with the redeeming banks.

3. Payment by insured banks of liabilities of noninsured institutions

Existing law: Section 18 (c) (2) of the Federal Deposit Insurance Act.

Recommendation: Add a proviso after the first sentence of section 18 to the effect that nothing in the section should be construed as limiting its applicability to bank mergers and consolidations.

Reasons: FDIC's current practice is to impose such an arbitrary limitation on the scope of section 18 (c) (2) with the result that it defeats its own purpose as set forth under its recommendation No. 89.

Example: a resident of New York presents for redemption $10,000 in traveler's checks issued by American Express at the Riggs National Bank in Washington, D. C. "As a matter of choice," Riggs National pays upon the instruments but forwards them on for collection since American Express does not have a $10,000 balance in its account with Riggs against which the instruments could be charged. Check collection between Washington, D. C., and New York usually requires 3 clear business days at the least. If American Express were to close or be thrown into bankruptcy before the $10,000 reach it, Riggs National would be a "prime obligor" on the instruments by reason of its endorsement thereof as a prerequisite to collection. Viewed on a national scale, an average of $9 million is received daily for payment by American Express through FRB Regulation J facilities. On the conservative assumption that 5 business days are required for check clearing, it follows that, at any given time, there are $45 million in the process of being collected and upon which insured banks are "prime obligors."

As FDIC argues in its recommendation No. 89, such prime obligors are covered by FDIC insurance and it would appear that, ultimately, FDIC is the prime obligor on the instruments, as their insurer.

4. Voidance of contracts made in violation of the Federal Deposit Insurance Act

Existing law: None.

Recommendation: Add a proviso to the act modeled on section 47 (a) and (b) of the Investment Company Act of 1940.

Reason: No contract made in violation of the act, or in violation of the regulations promulgated thereunder, should be valid. This would prevent insured banks from accepting deposits at their insured tellers' stations and, contrary to regulations 326 and 328, transferring such deposits to uninsured institutions.

The insured banks' present practice of accepting deposits at their tellers' stations in exchange for American Express traveler's checks is contrary to the statute and the regulations and should be countered by the suggested enactment.

5. Absorption of exchange as constituting payment of interest on demand deposits

Existing law: FRB Regulation Q based on title 12, United States code sections 371a, 371b. FDIC Regulation 329 based on title 12, United States Code, section 1828 (g). Administrative Procedure Act of 1946.

Controlling litigation: *United States* v. *Interstate Commerce Commission* (337 U. S. 430).

Recommendation: Member banks adversely affected by FRB Regulation Q should be required to exhaust the remedies at law before a fundamental change of policy occurs at the legislative level.

Reasons: The Administrative Procedure Act of 1946 (5 U. S. C. 1009) provides the remedy at law for the banks adversely affected or aggrieved by the FRB Regulation Q. By making both FRB and FDIC parties defendant, the banks would secure a judicial determination of their grievance, which should be the basis of action by Congress.

FRB recommendation No. 77 reveals the existence of a controversy between the FRB and FDIC concerning the absorption of interest charges. Since this controversy arises under the laws of the United States and it is real, it is also justifiable under the doctrine of the Interstate Commerce Commission, supra. FRB should be required to sue out a declaratory judgment of its controversy with FDIC as a prerequisite to action by the Congress. FRB's failure to avail itself of this remedy is not in the public interest and should not be condoned.

6. *Applicability of the doctrine of primary jurisdiction and administrative finality to suits based on the Federal Deposit Insurance Act and the rules and regulations promulgated thereunder*

Recommendation: Amend act to include provision similar in every respect to the provision urged in the case of the Federal Reserve Act under recommendation No. 5 thereunder. Similar reasons motivate this recommendation.

COMPTROLLER OF THE CURRENCY

1. *Voidance of contracts made in violation of the National Bank Act, and the Banking Acts of 1933 and 1935*

Existing law: None.

Recommendation: Add a proviso to the Banking Act of 1933, as amended, modeled on section 47 (a) and (b) of the Investment Company Act of 1940.

Reasons: The Comptroller's recommendation No. 36 reveals an ugly state of affairs which resulted in loss to depositors. It would appear that such persons would have no remedy at law for the enforcement of their deposit contracts, or their voidance, if contrary to title 12 United States Code, section 378. The proposed amendment would give depositors the right to enforce the Federal prohibition contained in the statute. If incorporation under the laws of Texas depends upon the filing of a surety bond proportionate to the liabilities to be incurred by the corporation, then the depositors would be able to recover from the surety whatever they cannot recover from the corporation.

2. *Enforcement of Banking Acts of 1933 and 1935 in civil proceedings*

Existing law: None.

Recommendation: Amend acts to include a provision modeled on section 42 (e) of the Investment Company Act of 1940.

Reasons: The Comptroller's recommendation No. 36 reveals the law's deficiency in providing for its enforcement in criminal, rather than both in civil and criminal proceedings. It is clear that considerable loss to depositors could have been prevented had the Comptroller sued out an injunction to prevent the corporation from violating the statute (12 U. S. C. 378). The SEC has been very successful in civil proceedings which it has brought under its own statutes to prevent violations and there is no reason why the Comptroller should be restricted to the opinion of the Justice Department, rather than to the opinion of the courts.

3. *Applicability of the doctrine of primary jurisdiction and administrative finality to suits based on statutes administered by the Comptroller of the Currency*

Recommendation: Amend Banking Acts of 1933 and 1935 to include provisions similar in every respect to the provision urged in the case of the Federal Reserve Act under recommendation No. 5 thereunder. Similar reasons motivate this recommendation.

Senator ROBERTSON. The committee will stand in recess until 10 o'clock Monday.

(Whereupon, at 11:20 a. m., the subcommittee recessed until 10 a. m., Monday, February 11, 1957.)

STUDY OF BANKING LAWS

(Financial Institutions Act of 1957)

MONDAY, FEBRUARY 11, 1957

United States Senate,
Committee on Banking and Currency,
Subcommittee on Banking,
Washington, D. C.

The subcommittee met, pursuant to recess, in room 301, Senate Office Building, at 10:05 a. m., Senator A. Willis Roberston (chairman of the subcommittee) presiding.

Present: Senators Robertson, Sparkman, Douglas, Monroney, Lausche, Clark, Bennett, Bush, and Payne.

Senator Robertson. The subcommittee will please come to order.

We are very pleased to have with us this morning the distinguished Comptroller of the Currency, the Honorable Ray M. Gidney.

The committee will be pleased to hear from you, Mr. Gidney, at this time.

STATEMENT OF RAY M. GIDNEY, COMPTROLLER OF THE CURRENCY; ACCOMPANIED BY L. A. JENNINGS, DEPUTY COMPTROLLER OF THE CURRENCY; T. V. ROBERTS, CHIEF COUNSEL; L. R. STOVER, ASSISTANT COUNSEL; AND ROY T. ENGLERT, ASSISTANT COUNSEL, OFFICE OF THE COMPTROLLER OF THE CURRENCY

Mr. Gidney. Senator, Mr. L. A. Jennings, First Deputy Comptroller, is with me, as he has a very important part in all these studies, and Mr. T. V. Roberts, Mr. L. R. Stover, and Mr. Roy T. Englert of our counsel.

I have prepared a statement, Mr. Chairman and members of the committee.

Mr. Chairman and members of the committee, I am honored to have this opportunity to testify with respect to the Financial Institutions Act of 1957. I wish to tell you how much we, in the bank supervisory field of Government, appreciate the splendid and outstanding work being done by this committee and its chairman, Senator Robertson.

First, we wish to point out that appendix A of our statement contains a list of 49 sections in title I, National Bank Act, which we endorse and support as they now appear in the committee print bill. Appendix B contains a list of 12 sections in title I which we endorse and support but recommend that minor changes of a technical nature be made in the wording. Our suggested wording appears in this appendix. In the interests of brevity, we will not comment specifically on the sections listed in appendix A, or on those sections or portions of sections listed in appendix B, unless the chairman or the committee members desire us to do so.

The first section on which we wish to make specific comment is section 8 of title I, the National Bank Act.

SECTION 8. CONFLICTS OF INTEREST PROHIBITED

Section 8 (a) would make it unlawful for the Comptroller of the Currency or any Deputy Comptroller to own stock in any national bank. It is recommended that this prohibition be extended to national bank examiners and assistant national bank examiners, and that it be made applicable to stock in bank holding companies as well as stock in banks. This would be consistent with the longstanding practice of our office.

Senator BENNETT. May I clear my mind on that?

Mr. GIDNEY. Yes.

Senator BENNETT. You are now doing that as a matter of policy?

Mr. GIDNEY. That is right.

Senator BENNETT. So the law would not make any change in the situation respecting any of these individuals?

Mr. GIDNEY. I think that makes no change whatever. Probably not even in a single instance.

Senator BENNETT. Thank you.

Mr. GIDNEY. Section 8 (b) would make it unlawful for any employee or former employee of the Comptroller of the Currency to accept employment in any national bank or district bank except pursuant to regulations prescribed by the Comptroller. We have no objection to this provision insofar as it applies to employees or former employees who have only recently left the employ of the Comptroller. However, we think it is unnecessary and is unwise to permit the Comptroller to have control over employment by a national bank of a former employee of the Comptroller who may have ceased to be such an employee 5, 10, 20, or even 30 years before. Many former employees of the Comptroller are today employed in national banks, some of them in very high positions. No reasonable purpose would be served by giving to the Comptroller control over the employment of these men by other national banks. We would suggest that this provision be amended to apply only to employees or to former employees who have ceased to be employees within a 2-year period.

At this point we should like to comment also on the provisions of section 803 of the bill which amends criminal statutes to make them applicable to employment of examiners and other employees of the Comptroller's Office by national banks. The provisions of this section give us grave concern.

Their enactment would seriously impair our ability to attract capable young men to our examining force. For practical purposes such young men joining our examining staff would do so with the knowledge that they must make bank examining a life career or leave the banking industry entirely if they should become dissatisfied with examining banks. For many years it has been our practice to obtain from each examiner an agreement reading as follows:

> You are requested to forward a statement that you will not, for a period of 2 years after you cease to hold the position of national bank examiner, accept employment of any kind in any bank which you may have examined without first receiving permission in writing from the Comptroller of the Currency.

This protective procedure has left nothing to be desired. We are strongly opposed to the enactment of statutes which would make offers of employment to, or acceptance of employment by, examiners or other employees of our office a crime. We strongly recommend to the committee that at least this portion of section 803 be eliminated.

Senator ROBERTSON. This matter has been brought to our attention by a number of witnesses. There has been no witness who thought the provisions in the tentative bill were necessary. A great many of them thought they were too drastic. I am sure it will be the sentiment of the committee to make some changes, possibly along the lines that you recommend.

Mr. GIDNEY. Yes, sir.

Senator ROBERTSON. You may proceed.

Mr. GIDNEY. There are some more paragraphs on the same order.

It is much as though you would say to a doctor that he should not take employment with a hospital, or a minister that he should not take employment with the church, or a legislator that he should not go out and practice law. These boys are in the banking field and that is where their opportunities are.

Section 803 would also make it a crime for any national bank, insured bank, savings and loan association, or Federal credit union, to make a loan to any employee of the Comptroller of the Currency without the written approval of the Comptroller. We believe that this prohibition should be confirmed to national and district banks which are examined and supervised by the Comptroller. We believe employees of the Comptroller of the Currency should be able to borrow from State-chartered banks, savings and loan associations and credit unions.

Section 803 (d) would make it a crime for any director, officer, employee, or stockholder owning 10 percent of the stock of any national or insured bank to make a political contribution in elections where supervisory officials or those having responsibility for public funds are to be elected. We believe it is an inherent right of every American citizen to make contributions to the political party of his choice. It is sufficient, in our opinion, for this prohibition to apply to the banks and we see no reason for extendng the prohibition to directors, officers, or employees, or stockholders thereof.

SECTION 12. ARTICLES OF ASSOCIATION

It is recommended that section 12 be amended to expressly require the approval of the Comptroller of the Currency for the organization of a national bank. Since 1933 the Comptroller has been required in the case of newly organized national banks to certify to the Federal Deposit Insurance Corporation that the bank is authorized to transact the business of banking and that consideration has been given to the factors enumerated in section 6 of the Federal Deposit Insurance Act. Prior to 1933, there was uncertainty about the extent of the Comptroller's authority to deny new charter applications, and for approximately the first 50 years after passage of the National Bank Act in 1863 the various Comptrollers of the Currency considered they were without authority to deny such applications unless they had reason to suppose the bank was being organized for "other than the legitimate objects contemplated by this Act."

Mr. ROGERS. I wonder if you would supply the committee with the language on that?

Mr. GIDNEY. Yes, sir.

Mr. ROGERS. It is not exactly clear in my mind.

Mr. GIDNEY. We can do so and would be glad to do it.

Senator ROBERTSON. The Chairman would like to make this point clear. You are not asking for any new authority?

Mr. GIDNEY. No.

Senator ROBERTSON. You are asking for the privilege of limiting your authority. The way a number of Comptrollers have ruled whenever anybody applies for a national bank charter, it would have to be granted. You want it especially set out in the law that you do not have to do that, but you can consider the competitive factors and other matters, and consider that if they do not need another bank in that community that you can turn the application down.

Mr. GIDNEY. We have been proceeding on that theory and basis.

Senator ROBERTSON. I think you have been proceeding correctly, but I did not know the previous Comptrollers held that they merely had to comply unless they thought they were asking for bank charters to run a race track, or something like that.

Mr. GIDNEY. I know they did feel they had to give it, and that is one of the things that contributed to the overpopulation of banks that existed in the late twenties. We have had some people tell us that they would compel us to give the charter. There was some fuss about it but they have not done so.

Now we come to a subject that aroused some little difference of opinion—preferred stock.

SECTION 20. PREFERRED STOCK

It is recommended that a two-thirds vote should be required rather than a simple majority for the issuance of preferred stock. It is recommended that the statute provide for the Comptroller's approval of the issuance of preferred stock only—

> after determination by him that the only practicable method of obtaining desired additional capital is the issuance of preferred stock.

Section 20 in its present form would, we believe, leave the Comptroller no choice but to approve all applications filed by national banks to issue preferred stock provided the plans were soundly conceived. Enactment of this section presumably will settle the policy question of whether preferred stock should be sold by national banks as a normal or usual method of raising capital or only in urgent or unusual situations or under emergency conditions, local, sectional, or national. We believe that the sale of preferred stock by national banks should be approved by the Comptroller only in urgent or unusual situations or under emergency conditions. Our reasons for this recommendation may be summarized as follows:

We have given our reasons at considerable length. It is only fair to say that our views differ from those expressed by some of your witnesses, and are supported by at least one.

Senator BUSH. I think we ought to let him proceed. This is one of the important things in this bill, is it not?

Senator ROBERTSON. Yes.

Mr. GIDNEY. (a) More than 1,600 national banks have sold in excess of $1 billion of new common capital during the past 10 years. Much of this in our opinion would have been in the form of preferred stock if the Comptroller had been willing to approve its issuance. It is clear that common stock is an adequate vehicle for raising new capital in national banks under normal conditions.

(b) The increased weight of risk of an enlarged volume of business predicated on newly acquired preferred capital would rest in the first instance on the common shareholders. The new preferred capital would justify an enlarged volume of risk assets, or more fully justify the existing volume of such assets, from the standpoint of depositor protection, but it must not be overlooked that the full weight of the increased risk would bear first on the common shareholders. Over a period of time this would result, in our opinion, in the common stock of banks losing some and perhaps much of its present high standing as a sound investment. The sale of preferred stock would tend to become the general rule in bank recapitalization programs, and the sale of common stock much more difficult.

If preferred stock were to be approved as a medium of normal bank recapitalization, it is obvious the Comptroller would have to establish sound policies relative to the proportion of preferred stock that could be issued by a bank in relation to its common capital stock or its overall capital structure. It would be undesirable for a bank to have a capital structure topheavy with nonvoting (except under certain conditions) preferred stock controlled by a thin layer of common stock. It is true the Comptroller could control this in initial instances, but if a bank issued preferred stock in reasonable proportion to its common stock and then by reason of growth or asset losses found it necessary again to raise additional capital, and this proved possible only through the issuance of more preferred stock, the Comptroller would be forced to choose between foregoing the additional capital protection needed by the bank's depositors, or permitting the bank's capital structure to become topheavy with preferred stock. Naturally, in such a situation the additional preferred stock capital would be approved, with the result that the amounts of preferred stock issued by particular banks, over a period of time, would be dictated more by exigencies than by the sound policies initially established by the Comptroller.

(c) One additional point is worthy of mention. If banks were to use the avenue of preferred stock for normal capital increases, it is easy to imagine the problems that would arise when some of those banks required emergency recapitalization. The two classes of stock already outstanding (common and preferred) could very well necessitate adding a third class of stock outranking both the existing common and preferred stocks. It is disturbing to contemplate the complications that would ensue from three classes of stock with an almost infinite number of possible variations in preferences to dividends, retirement, voting rights, voluntary and involuntary liquidation, which would give rise to conflicts of interest between the several classes of shareholders.

Senator ROBERTSON. You are the first witness to point out in this section that a liberal issue of preferred stock throws a new and heavy burden on the common stock, because they are at the bottom of the pile if there is any trouble, and the preferred stock will support more risk investment.

Mr. GIDNEY. Yes.

Senator ROBERTSON. But the owners of the common stock are left holding the bag and, therefore, in your opinion it is not fair to them to authorize the bank to get capital in this easy way.

Mr. GIDNEY. That is true. They are left holding the bag. Of course, they have leverage possibilities and it does afford attractive possibilities to speculatively inclined people. So we have that problem.

We strongly believe it is in the best interests of banking to authorize the use of preferred stock only in urgent or unusual situations or under emergency situations. That is the way the statute stands now. Consequently, we urge that the language suggested above be incorporated in the bill.

Senator BUSH. I would like to ask some questions now.

Senator ROBERTSON. We have permission to continue in session all day. It is the purpose of the chairman to permit each member to ask all the questions he wants to, because the testimony today and tomorrow is the most vital and valuable on the whole bill, and we can familiarize ourselves with the real controversial issues.

Senator BUSH. I want to say in advance that I have no preconceived ideas on this subject, but I think it ought to be considered very closely as to whether preferred stock can become rather generally used as a means for helping financing banks.

As I understand it, for some time past here, and up until recently, banks had a very hard time financing on the basis of common stock. Bank stocks drifted into relative disfavor and they were not able to offer new shares on a basis which was attractive enough to warrant their doing so. The consequence is that deposits grew, but capitalization did not keep pace with them, and we find many banks operating on a ratio of deposits to capital which 25 years ago would have been regarded as exceedingly dangerous, although now it is a rather accepted thing.

We used to think of a deposit ratio of 10 to 1 as being sort of sacrosanct, but now we do not bat an eye over 15 to 1, and the investing public does not. We frequently see ratios higher than that.

Is that not so, Mr. Gidney?

Mr. GIDNEY. That is true.

Senator BUSH. I do not know what the present market is for bank stocks, but during this period, and since World War II, I would say, there have been periods where it was very difficult for banks to finance where they needed additional capital to support this growing deposit structure. They could not sell common stock on an attractive basis so they did not do anything in a lot of cases, and conducted their affairs in a very conservative way on their investments.

We have not had any troubles, we have had good times, generally speaking. There has been no panic and the situation has rolled along pretty well. However, I do believe if during some of those periods it had not been looked upon with disfavor to sell preferred stock, that it might have been desirable in the interests of the safety of the depositors for managements to have sold some preferred stock.

You say here on page 5 in the middle of the page:

It is clear that common stock is an adequate vehicle for raising new capital in national banks under normal conditions.

I do not know just what normal conditions are any more. I wonder what you mean by normal conditions?

Mr. GIDNEY. Well, the figure we quoted as to the amount that has been raised in 10 years is an indication that conditions have been near enough to normal to hold good. I think the sale of new national bank stock in 1956 was $194 million. It is a very interesting subject and, of course, it is perfectly possible to take either side.

In a theoretical way the preferred looks all right. One of our very good New York City institutions made a study which was very persuasive up to a point, a few years ago, that it was necessary; that they could not get capital that was necessary. Just about the time that was off the press one of the banks up there sold $130 million worth of capital stock, and somewhat damaged the validity of the arguments.

One of our large banks had spoken to us several times about raising capital by preferred stock and we were somewhat negative, so they sold an amount that brought them in $56 million without difficulty. That would possibly not apply to every bank. The bank has to have prestige to sell its capital readily, of course.

I do not mean we do not have some banks whose capital is lower than we would like to have and they might get it easier by preferred stock, but I think our good standard banks have been selling stock all over the country in a large amount.

Senator BUSH. Let me ask you this question, Mr. Gidney: On the bottom of page 5 you say:

> The sale of preferred stock would tend to become the general rule in bank recapitalization progams, and the sale of common stock much more difficult.

I do not know why that should apply in the bank stock market offhand——

Mr. GIDNEY. It might or it might not. I do not know about that.

Senator BUSH. Any more than it would in the industrial forms. Why is that so obvious?

Mr. GIDNEY. I do not think it is necessarily obvious. I think that statement would arise out of the impression that our bank friends give us. It has some attractions for them, of course.

Senator BUSH. Do you find amongst the bankers any real sentiment in favor of the permissive sale of preferred stock?

Mr. GIDNEY. Oh, yes.

Senator BUSH. Quite a bit of it?

Mr. GIDNEY. The testimony of the bank representatives was to that effect.

Senator BUSH. Why would the sale of preferred stock tend to become more general than it is in any other area of our economic bloc? I do not quite see why that would be the case.

Mr. GIDNEY. I think it is the course of least resistance, for one.

Senator BUSH. I beg your pardon?

Mr. GIDNEY. I think it is the course of least resistance for many banks to sell it that way. It is true they might tap some new sources of capital.

Senator BUSH. But in order to sell preferred stock at a prime rate it has to be good and therefore has to have good coverage of earnings and assets.

Mr. GIDNEY. That is right.

Senator BUSH. They can sell a certain amount, and if they sell any more of it they will not be in that class, and if the bank values its credit, as most of them do, they will not sell preferred stock.

Mr. GIDNEY. I do not think they would run riot with it. I do not think they would run beyond the reasonable needs of the business, or anything of that kind, but they feel it is the easiest way to get the money and they can get it from sources perhaps actually not otherwise available, like insurance companies.

Senator BUSH. You say it is the easiest way. What is wrong with it, in your opinion?

Mr. GIDNEY. We have explained a few of these points.

Senator BUSH. I do not think you have. You just say it is bad and undesirable for them to have a topheavy preferred structure, and it would be dictated more by exigencies, and so forth.

I do not see anything wrong with it from a financial standpoint, so far.

Mr. GIDNEY. Not a financial standpoint alone, but from the point of equity.

Senator ROBERTSON. May I interrupt for a moment? Off the record.

(Discussion off the record.)

Senator ROBERTSON. On the record.

Mr. GIDNEY. Of course, it is all right from a financial standpoint, I think, but I will have to qualify it. We are interested in maintaining the standing of bank stock as a high-grade security; a security which is understood by everybody that buys it, which is not afflicted with varying terms, free from fancy work. The moment we depart from the present standard we get into that field.

Now, one of the motives of many people in issuing preferred stock is to retain control of their institution with a smaller ownership of stock than otherwise. That is to say, Mr. So-and-So has so many shares, and we try to get him to sell some more stock, but he will not do it because he cannot take his additional part and he does not want the control to get away from him. You can on that basis decide that preferred stock is either good or is not good. That is not open and shut. Maybe it is a good thing to let people control banks with small ownership. Maybe it is not. We think we should take the position that it is better to have one class of stock. Some of that kind of thing comes in in corporate financing with stock with voting power and stock without voting power.

Senator BUSH. That argument you use can only apply to a fairly small bank.

Mr. GIDNEY. It is particularly applicable to small banks. Yes.

Senator BUSH. Yes. It is not apt to apply it to any large banks.

Mr. GIDNEY. Not the really large banks.

Senator BUSH. They are certainly among those who have deposits which are growing to beat the band and developing ratios that, as I say, would have been regarded as very topheavy years ago. I do not, offhand, think that is an awfully good argument you have made there.

Mr. GIDNEY. It is one of the points. There is no argument in this that is absolute. I would say that.

Senator BUSH. You say it would become the danger. In the middle of page 6 you speak of permitting the bank's capital to become topheavy with preferred stock. How could that happen, Mr. Gidney? You know, I am sure, better than any of us, that it cannot become topheavy with preferred stock, because preferred stock will not have an attractive rating.

Mr. GIDNEY. I think we mean there by topheavy "disproportionate" rather than "topheavy."

Senator BUSH. I would say "topheavy" would suggest there was more of that than there was of common.

Mr. GIDNEY. Yes; and a good deal more.

Senator BUSH. It would seem to me under those circumstances the preferred itself would not be attractive, and, therefore, would not be very salable, and that would take care of itself.

Mr. GIDNEY. If that occurred, that would be quite an unhappy situation for the bank, and it did occur, of course, when there was a great deal of RFC preferred in banks.

Senator BUSH. Yes.

Mr. GIDNEY. It did occur, and there were opportunities there——

Senator BUSH. Preferred stock at that time, if I recall—and you correct me if I am wrong—was issued to save the depositors' money. It was put in to keep the banks' money solvent.

Mr. GIDNEY. For protective purposes.

Senator BUSH. That was the basic purpose of it.

Mr. GIDNEY. That is right. The bankers regarded it as having some stigma and they wished to get rid of it as quickly as they could.

Senator BUSH. Because it had never been issued before and was issued then for the first time as a lifesaving gesture or action.

Mr. GIDNEY. Yes.

Senator BUSH. Of course, any bank which did have preferred stock was suspect, so to speak, but it worked out very well, as a matter of fact; did it not?

Mr. GIDNEY. Yes.

Senator BUSH. For the purpose?

Mr. GIDNEY. It certainly did.

Senator BUSH. It supplied the capital. How about the payback? Has that been going on pretty well?

Mr. GIDNEY. The payback is entirely complete. There is not a share of RFC preferred stock outstanding. There are two banks, not national banks, that have capital notes outstanding, or debentures.

Senator BUSH. So you do not feel if a preferred stock was issued by a perfectly reputable bank as a device for raising more capital, and if that preferred stock had a sinking fund that would require the bank to be retiring it after 25 years out of earnings, that that would be a sound method of financing?

Mr. GIDNEY. I do not think it would be as good as getting capital by a common method. It would be as sound.

Senator BUSH. You do not think it would be unsound?

Mr. GIDNEY. Not unsound.

Senator BUSH. You answered that question. I am raising another.

Mr. GIDNEY. This is a matter that is not absolute either way.

Senator BUSH. The device of convertible preferred stock has become a common one in connection with many corporations. Is that right?

Mr. GIDNEY. Yes.

Senator BUSH. I would like to have your opinion on that. Do you see anything wrong with that offering of preferred stock——

Mr. GIDNEY. I do not know.

Senator BUSH. That could be convertible into the common stock of a bank?

Mr. GIDNEY. I do not see anything wrong with it except we would have to look down the road and see what price it is going to be converted at. It would have to be laid out and say it is to be on that basis.

Senator BUSH. Suppose it was convertible not far away from the market—10 percent above the market, or something like that. That is an invitation to buy and convert it, perhaps, within a few years. Is there anything wrong with that?

Mr. GIDNEY. Which market do you mean? At the time of issue or the time of conversion?

Senator BUSH. Let us say the preferred is issued at $100 at the time that the common is selling at $110, and the preferred is convertible into the common stock.

Mr. GIDNEY. Here is the thing that troubles me on that. If that conversion is exercised soon, of course it is equivalent to a sale of common. Let us suppose it is a considerable length of time ahead. Meanwhile the bank holds down its common dividends and piles up values. Are we to allow that preferred to convert at a value fixed now, whereas the intrinsic value has doubled, let us say? We must take care of that if we have convertible preferred. We must look ahead for that.

Senator BUSH. Are not stockholders able to look out for that themselves? The directors are responsible for that. Why not give them the freedom they need to supply this bank with capital?

Mr. GIDNEY. I have lots of faith in them, but I think we had better help them look down the road on that. If it is adopted I would like to have the opportunity to say the conversion shall be on an ascending basis and be related to the value of the bank at the time of conversion.

Senator BUSH. It would seem to me offhand, with no disrespect, that most of the objections you offer are designed in some way mysteriously to protect the common stockholder of the bank; whereas the purpose, I think, that is worthy, particularly in consideration of preferred stock financing, is to improve the position of the depositor. That is why I think management should have more leeway than they have and should be encouraged to get more capital even through the sale of preferred stock or convertible preferred stock, so as to give them other avenues of increasing their capital funds, except the one, namely, the sale of common stock.

Why, just because they are a bank, should they be deprived of the freedom of our markets, which are open to other corporations, particularly when in giving them that freedom you are encouraging them to afford more protection to the depositor?

Mr. GIDNEY. It is not an open and shut question. Another thing about it is, let us suppose we are talking about getting in a certain amount. In a particular case we actually got $56 million. I would rather have that $56 million come into the bank in common stock than $100 million in the form of preferred, because that common will stay and grow and become a larger protection, whereas the preferred will be retired under the schedule we mentioned, so I like the common better.

Senator BUSH. It may or may not be retired under that schedule.

Mr. GIDNEY. It may not.

Senator BUSH. That is optional with the stockholders at that time.

Mr. GIDNEY. I will admit this is a matter somewhat of bias, and my bias is on the side of holding down the preferred stock. This is the Federal Deposit Insurance Corporation's report of assets and obligations and liabilities of operating insured banks on June 30, 1956. At that time we had outstanding for national banks only $3,859,000 of preferred stock as against total capital accounts of $8 billion. We are just almost out of it in national banks.

State bank members of the Federal Reserve System had $10 million and nonmember insured banks had $14 million, of preferred stock capital notes or debentures. One could run through this and find a great number of States that have no preferred stock or debentures out for any banks. I think the concentration of the amounts is quite largely in New York, where perhaps they are smarter in these matters, and perhaps it is evidence that it is good. But we have been pursuing the policy of allowing it only in emergency, and we are down to the point where it is almost out.

That is our bias. We will have to admit to a bias.

Senator BUSH. I think you have done a very proper thing in admitting that.

Senator ROBERTSON. Mr. Gidney, for the benefit of the committee when it votes on this issue I will give a little background for the purpose of the record. I asked you and all of the other agencies dealing with the banking and credit laws to make a tabulation of the laws under your jurisdiction, and then testify before us on the 9th and 10th of November concerning any changes you wanted. I asked a distinguished group of bankers and credit men, totaling 27, to be present to hear that testimony. Then after hearing it I asked them to give us the benefit of their advice. They did so and in December they submitted recommendations to us.

No Federal agency had recommended anything concerning preferred stock. The members of the Advisory Committee, however, said for many years we did have a provision in the law about preferred stock. It had not been used since the depression years when it was used solely by the RFC to put in more working capital, and either it should be made workable or taken out of the law.

So I authorized our staff to put in a provision that would make it workable. Your testimony is we made it too workable and you would like to have it restricted by saying that the privilege shall be used only after determination by the Comptroller of the Currency that the only practicable method of obtaining desired capital is the issuance of preferred stock.

So, gentlemen, that is it.

Senator BUSH. I am sorry. There is one thing Mr. Gidney said I did not get. He said the banking witnesses here said it. I was not here. Did the American Bankers Association favor it?

Mr. GIDNEY. Yes. I made a little note that it was favored by Mr. Cravens—on this nonemergency basis—by Mr. Cravens, the Chairman of your Advisory Committee, and Mr. Lyons, representing the American Bankers Association, and Mr. Fleming, representing the Reserve City Bankers Association.

Senator BUSH. They all favored it?

Mr. GIDNEY. They all favored it. Mr. Norfleet Turner, representing the United States Chamber of Commerce, disapproves the issuance of debt obligations except in rare cases of emergency, to be determined by the Comptroller.

Senator ROBERTSON. The Chair was going to call attention to that because it applies especially to the next provision, and the history of that is largely the same.

Mr. GIDNEY. That is right.

Senator ROBERTSON. That was a recommendation of the Advisory Committee and the Chairman put it in for the purpose of study and testimony. The representatives of the United States Chamber of Commerce were bitterly opposed to capital notes and debentures. The Chair realizes that we have a bit of inconsistency in the bill itself, because we carry forward the provision of the old law that no new securities must be issued which impair the validity of existing securities. Then we come along and authorize the issuance of debentures, which undoubtedly would impair the security of existing obligations.

So if this stays in there there must be some correlation of the two apparently conflicting provisions. I understood you were going to recommend that we take it out.

You may proceed.

Mr. GIDNEY. I think we changed our mind on that, perhaps.

Senator ROBERTSON. You have changed your mind?

Mr. GIDNEY. Yes.

Senator ROBERTSON. That is all right. We want the last position.

Mr. GIDNEY. Yes, sir.

Senator SPARKMAN. Mr. Chairman, before we get away from the preferred stock section he has been talking about, I would like to inquire of Senator Bush if the provision that Mr. Gidney has recommended does not meet with your suggestion. In other words, that at times it is necessary for banks to raise capital——

Senator BUSH. You mean on page 4, at the bottom?

Senator SPARKMAN. Yes, because it says there he can grant it if he determines that it is the only practicable method of obtaining desired additional capital. As I understand it, that is your argument, that times may come when a bank has to resort to preferred stock.

Senator BUSH. Mr. Chairman, I have been asking these questions to try to develop the thing in my own mind. For the record, I am not committed to any point of view, but I would say that the suggestion you have just read would not—if one believes that it is all right for banks to use the preferred stock device for raising capital—that this restriction is not satisfactory. I would not think those who strongly favored the banks having this choice would be satisfied with that provision that Mr. Gidney proposed, because he says the only conditions on which you can issue preferred stock are that there is not any other way to do it. In other words, you have to prove first you cannot sell any common stock.

It seems to me there might be times when a bank might think it desirable to increase its capital, let us say, by 10 percent, because they gained deposits and want to improve their capital position vis-a-vis their deposits, and they will say, we will issue 10 percent more capital, but this time we will issue it in preferred stock and make it convertible into common stock, so maybe 10 years from now, after the bank has grown, we will force the conversion and we will have a capital common stock base again.

I do not see any reason why a bank should be deprived of that method of financing, and I think it would have a very desirable effect from the standpoint of depositors, to wit, it would encourage them to do financing after their deposits had grown and they felt the need of more capital, because they would have more than one way of doing it.

At times when a common stock market was not in good shape they could refer to a preferred stock and obtain the objective of increasing their capital.

I do not know why they should be deprived of that. I see no good reason in this argument of Mr. Gidney's.

Senator MONRONEY. May I ask one question, Mr. Chairman?

Senator ROBERTSON. Yes. The Senator from Oklahoma.

Senator MONRONEY. It would be possible, would it not, for a bank with capital stock of $100,000, having had a successful operation in building up a surplus, to float preferred stock in huge amounts to where the owners of the $100,000 worth of common stock would be controlling the bank, while a disproportionate amount of the capital was in nonvoting rights which were in the bank.

Mr. GIDNEY. That is the sort of thing we are apprehensive of. We do not know how large that amount would be that they could float. I would not like to think it would be very large if the buyers were all as sophisticated as we think they could be. But it could go further than we would like, certainly.

Senator MONRONEY. You could have a very small minority control of the actual stock, with nine-tenths being deprived of the right to control, or direct, or suggest, or sit on the board of directors through this preferred stock issuance provision, unless it were rather tightly scrutinized by the Comptroller.

Mr. GIDNEY. I think it should be quite tightly scrutinized by the Comptroller. The human element is human nature.

Senator MONRONEY. A lot of these old boys who run these banks like to run them as they please. Yet they might need more capital stock to maintain the increasing level of deposits. They would rather not turn loose of that bank and not want to issue common stock, therefore, but they would be very happy to take preferred or debentures, because those folks would not have one blessed thing to say about the management.

Mr. GIDNEY. I think it is a safe statement to make that we have always several cases on the stove of just that character.

Senator MONRONEY. Is it not a general rule that bankers never want to have more than the closely confined corporation, because stockholders can give them trouble in the election of directors and presidents and vice presidents?

Mr. GIDNEY. I think it could be pretty general. Human nature is pretty general.

Senator DOUGLAS. You are making an argument for the retention of cumulative voting.

Mr. GIDNEY. I was afraid you would bring that out. It does go down that street a little bit.

Senator BUSH. Mr. Chairman, I would like to suggest to the Senator from Oklahoma what he says is applicable almost to any corporate structure, including the oil business or the steel business.

Senator MONRONEY. That is true. But it is not as important in the control of an ordinary corporation as it is in a financial institution, playing with other people's money and responsible for the soundness and continued operation of a financial institution.

Senator BUSH. Of course, in this operation they are closely scrutinized by supervising Government authorities, whereas in other areas they are not, so I do not think the situation is any different in principle.

Senator ROBERTSON. The Senator from Pennsylvania.

Senator CLARK. Mr. Gidney, would your objection to the issuance of preferred stock still stand if the only preferred stock that could be issued would be entitled to full voting rights along with the common?

Mr. GIDNEY. I think our objection would be lessened. I think some of the other things are balanced and the risks would still occur, but in the particular voting stock matter which is important, our objection would be removed by that.

Senator CLARK. Such a change might meet some of the objections Senator Monroney raised.

Mr. GIDNEY. It would meet that objection. Definitely. As to the other corporations, we are just working in our own vineyard. We think there are lots of things in other corporations we would not want to see moved in here.

Senator ROBERTSON. You may proceed.

Mr. GIDNEY. Yes, sir.

SECTION 21. CAPITAL NOTES AND DEBENTURES

Section 21 would authorize national banks to issue debt obligations in the form of capital notes or debentures subordinated to deposit liabilities but having preference over liabilities owing to the shareholders in the form of capital stock or dividends on such stock. We are opposed to this proposed provision of law unless—here is where our change comes in—unless the issuance of capital notes or debentures is authorized for emergency use only, and unless repayment of such obligations is made subject to the approval of the Comptroller of the Currency. The sale of such notes or debentures, in our opinion, would cause the common capital stock of some and perhaps many national banks to lose its attractiveness as an investment because of the adverse leverage of risk brought about by enlarged asset structures based on funds realized from the sale of the notes or debentures. Repayment should be made according to the terms of the notes, but obviously the Comptroller should not permit repayment unless the capital position of the bank justifies such action.

For the above reasons, it is recommended that the first sentence of section 21 be amended by adding after the word "Comptroller" the following:

after determination by him that it is not practicable to obtain essential additional capital through the sale of common or preferred stock,.

It is also recommended that there should be added after the words "national bank" in subsection (1) of section 21 (a) "with the approval of the Comptroller of the Currency."

I believe that is the retirement feature.

A two-thirds vote rather than a simple majority should be required for the issuance of capital notes or debentures and it is recommended that an appropriate change be made in the first sentence of section 21 (a).

We would feel pretty much the same about capital notes as against preferred stock, except that preferred stock is already in the law. In the emergency situations we would be helped by having the capital-note method available.

In the troublesome periods of the early thirties, where many reorganizations took place, some of the State banking departments had something of an advantage in the matter of the ease with which the adjustments could be made. In a really desperate situation I believe these capital notes or debentures could be very useful, because in that way it might be possible to have one interested party put in a large sum in capital notes, and thus patch up the situation. But we would take the same position on them as to their being of an emergency character as we would on the preferred stock.

I think what we said about preferred stock pretty well covers the capital notes.

If there is nothing further in the form of questions on this, I will pass to the next item.

Senator BUSH. You have covered it pretty well.

SECTION 23. SHAREHOLDERS' LISTS

Mr. GIDNEY. In connection with section 23, it was the original recommendation of the Comptroller of the Currency that the right of shareholders of a national bank to inspect the shareholders' list be qualified by a requirement of a showing of a proper purpose not inimical to the interests of the bank. This recommendation was approved by the Advisory Committee for the Study of Federal Statutes Governing Financial Institutions and Credit—report, pages 5 to 6—but was not incorporated in the proposed act. We recommend that our original recommendation as approved be enacted.

In 23 (b) there has been added a sentence which would require the president or cashier to notify the Comptroller immediately of any single transaction involving the purchase or sale of 10 percent or more of the outstanding shares of a national bank. We regard this provision as unnecessary in the effective supervision of national banks. We know of no case in which the obtaining of this information at the time such a transaction was recorded on the bank's books would have enabled us to have more effectively discharged our supervisory duties.

Senator SPARKMAN. Mr. Chairman, may I ask this question, more out of curiosity than anything else.

Senator ROBERTSON. Senator Sparkman.

Senator SPARKMAN. How would a stockholder show that his purpose was not inimical to the interests of the bank? Just on a simple certificate, or what?

Mr. GIDNEY. I am not just sure how he would show it.

Senator SPARKMAN. That is what I am wondering about.

Mr. GIDNEY. I think he would state his object. If the bank thought it was unreasonable in going over it he would not be able to get the list. As it stands now, he does not have to show anything.

Senator ROBERTSON. The language in the bill is the present law. You are asking we change the present law.

Senator SPARKMAN. He is asking it be changed.

Senator ROBERTSON. Let us get that straight. Is that not the language of the present law?

Mr. JENNINGS. That is correct.

Mr. GIDNEY. Yes.

Senator ROBERTSON. And you are asking we take your recommendation, which you say we did not take before.

Mr. GIDNEY. Yes.

Senator ROBERTSON. And change the present law. But yet you tell Senator Sparkman when we take your recommendation you would not know how to implement it, because you would not know how a stockholder would be able to show he was not up to some skullduggery.

Mr. GIDNEY. It is a fault in our recommendation.

Senator SPARKMAN. The hardest thing for a person to do in attempting to prove something is to prove the negative. If you want a safeguard, the burden ought to be on the other side rather than on the stockholder.

Mr. GIDNEY. I would not feel badly if the burden were put on the other side.

Senator SPARKMAN. Unless it can be shown he has such an interest.

Mr. GIDNEY. I think that is not a bad suggestion. As the thing is now, the right is absolute. What brought it to my attention particularly was that a certain gentleman had bought 1 share, I think, of each of 3 large banks in his city, and he was demanding the stockholders' lists of each one. They asked him why he wanted it, and he said, "I want to sell the bank." Naturally, they did not like that.

Senator ROBERTSON. He said he wanted to sell the bank?

Mr. GIDNEY. Yes; in this case this individual, as I recall it, bought 1 share of stock of 1 bank, I think, of each of 2 or 3 large banks. The bank that was resisting him asked him why he wanted to see the list, and he said he wanted to sell the bank. He wanted to sell the bank. He was a self-appointed seller.

Obviously, they did not like that, but they did give him access over many days. I do not know whether he ever got the entire list. I do not know how the best way is to fix it. We thought our suggestion would be all right. I think it should be somewhat less open.

Senator DOUGLAS. Has Senator Sparkman finished?

Senator SPARKMAN. Yes; I wanted to raise the point that it seemed to me the burden is unfairly placed in that suggestion.

Senator DOUGLAS. Do I understand that the Comptroller now says he favors denying the list of stockholders if the management of the bank believes that the purpose is inimical to the interests of the bank?

Mr. GIDNEY. I do not think I had better say that I have come to that point. I see the difficulty which Senator Sparkman raises. It is a little difficult either way. One man has to prove it is a proper purpose and the other that it is improper.

Senator DOUGLAS. The question I would like to raise is this: To whose satisfaction do you have to prove or disprove these matters? Who would be the judge, or the arbitrator, in your proposal?

Mr. GIDNEY. I should think it might well be a matter of fact that might be referred to our office, conceivably.

Senator DOUGLAS. The Comptroller of the Currency?

Mr. GIDNEY. And it might go to court, conceivably.

Senator DOUGLAS. You would have an examination?

Mr. GIDNEY. I think we could have a representation of the man.

Senator DOUGLAS. And there would be a decision?

Mr. GIDNEY. And make a decision on it.

Senator DOUGLAS. And there would be an appeal to the courts?

Mr. GIDNEY. I should think there should be.

Senator DOUGLAS. By that time there might be so much time consumed that if the list is desired to circularize stockholders for the purpose of effecting a change in the control at the annual meeting the occasion would have passed; is that not true? In other words, the method of control which you propose is so lengthy that one of the purposes which it is desired to safeguard by this provision would be impossible to be carried out; is that not true?

Mr. GIDNEY. It might be. I think the purpose to circularize for control would be a proper purpose in my present opinion. I think that would be a proper purpose.

Senator DOUGLAS. The officials of the bank would have the first determination.

Mr. GIDNEY. That is true.

Senator DOUGLAS. And they would be interested parties. Then you say appeal could be taken from their decision to you.

Mr. GIDNEY. Yes.

Senator DOUGLAS. In your big office that would necessarily require further delays and appeal from your decision could be taken to the courts.

My question is this: Is not the so-called remedy so long drawn out that in effect the management could bar minority stockholders from seeing the list of shareholders and, therefore, could largely perpetuate itself in control, even though that might not be the desire of the stockholders themselves?

Mr. GIDNEY. It certainly might bar a quick action. It might bar quick action.

Senator DOUGLAS. It might bar any action.

Mr. GIDNEY. It would not bar the persistent gentleman who keeps after it.

Senator SPARKMAN. Will the Senator yield?

Senator DOUGLAS. Certainly.

Senator SPARKMAN. It seems to me that a great deal of the problem would be taken care of if the presumption is given to the stockholder. Then if the bank feels his business is not proper, the bank could easily go to court.

Mr. GIDNEY. I believe that is all right. I believe that is all right. But as the matter is now, it is completely unconditional, and the purpose can be an obviously improper one. I believe that would be all right if the burden were perhaps the other way, but I think there should be some opportunity to avoid improper ones.

Senator SPARKMAN. Require the bank to take the move if the move is to be taken, and to make the proof.

Senator DOUGLAS. Before a court or the Comptroller?

Senator SPARKMAN. If it is a matter of time, probably the court would be the one.

Mr. GIDNEY. We would accept that. I think that would be all right. We cannot expect to go very far in the direction of giving the bank the arbitrary right to refuse it, because it would be inconsistent with the general feeling on these matters.

On the other hand, we do not like it when a large, well-managed bank can have someone come in and buy one share and, I think, it is rather prima facie evidence that that is not for a good purpose. I would think I would have to support a bank that made a decision that when someone bought one share and was demanding their stockholders list—I would have to decide they had made a good case that it was not a proper purpose right on the face of that.

Senator CLARK. Why would you think that was necessarily inimical to the interests of the bank? It might be inimical to the directors or the officers at that time. I am concerned about tha phrase "inimical."

Mr. GIDNEY. I think it would be generally inimical to the public interest, because what is the man getting it for? He may be getting it to make a suckers' list, or these various purposes for which it was used.

Senator CLARK. The making of a suckers' list is something we would all quarrel with, but it would not be inimical to the interests of the bank.

I am a little concerned about that phrase as to an easy interpretation.

Mr. GIDNEY. I think the phrase is not capable of easy interpretation, but I think, as Senator Sparkman said, putting the burden on the bank would be all right.

Senator CLARK. That does not solve the underlying difficulty. The phrase itself is largely interpretative. The changing of the burden is not going to help you very much; is it?

Mr. GIDNEY. We would like a better phrase, but we have not been able to think of one.

Senator CLARK. It might lead to a conclusion.

Mr. GIDNEY. I think it is some change in the statute. You are taking out the right of creditors to demand it. If we could have it changed to a degree which would be in Senator Sparkman's suggestion, we would have helped the situation.

Senator DOUGLAS. May I ask one more question?

Senator ROBERTSON. Yes. The Senator from Illinois.

Senator DOUGLAS. That is directed to the paragraph on page 9, Mr. Gidney. You object to the provision that the cashier of a national bank will notify the Comptroller.

Mr. GIDNEY. It is not that we object to it, but we do not see a useful purpose in it.

Senator DOUGLAS. I am sorry to say in my own State some very bad irregularities in the handling of State banks insured under the Federal Deposit Insurance Corporation and subject to their examination, occurred, in which the Federal Deposit Insurance Corporation did not know who really owned the stock.

Mr. GIDNEY. Yes, sir.

Senator DOUGLAS. It turned out, as you know, that the State auditor was secretly owning stock in a bank which the State auditor was inspecting, and the Federal Deposit Insurance Corporation claimed it was not known to them. As a result, grave results developed and the large sums of money were embezzled, totaling approximately $2½ million. This was very much in the foreground of the consciousness of the committee last November when we met on this matter. I think the committee and the chairman deserve a lot of credit for putting in this clause.

If you put in the clause for State banks subject to inspection by the Federal Deposit Insurance Corporation, how can we say it should not be put in for national banks subject to inspection by the Comptroller of the Currency? How can we draw a distinction between those two types of banks?

I think the chairman and his advisers moved against the clearly demonstrated evil, which, as a matter of fact, we may find occurs in other States besides my own. I am sorry it developed in my State, but we should try to correct it.

Mr. GIDNEY. I think you would need to be consistent between the two, National as well as State. Of course, if a sale occurs it does not necessarily reflect itself immediately on the books of the bank. That is only if the stock is transferred. It may be held in other names. So it may be held without transfer.

We might have this sent in and it is difficult to do anything with it when we receive it. We learn of these important changes as we make our examinations, and even when we know of them we are not—it is not easy to do anything about it.

We had an occurrence where we knew very well that the control of the bank had been sold or purchased and a great deal of mischief resulted from it. But the knowledge did not help us to stop it. We had to move after the mischief and serve notice of removal of directors, and all those things. Fortunately there has been a resale and we hope we are getting the bank back into good standing.

In other words, what I think we mean here is that we fined this out on our own present methods with examinations, adequately. It is not that we are objecting to this, but we do not think it is necessary or helps us particularly. We are getting it now.

Senator DOUGLAS. How many examinations do you make?

Mr. GIDNEY. They are 3 times in 2 years.

Senator DOUGLAS. That is an average of once every 8 months. A lot of damage could be done in that time. Is it not desirable to have changes in the ownership called to your attention so that if unsavory characters acquire control of those banks—if people who have conflicts of interests acquire control, you could start a special examination?

Mr. GIDNEY. That might in some cases work out.

Mr. JENNINGS. I might add, we have reviewed, in connection with this recommendation, a good many reports of examination where ownership did change, to see if it would have helped us. Actually it would not in any one of the cases under normal examining procedures.

Senator DOUGLAS. How could you tell?

Mr. JENNINGS. We went in to examine the banks within a few months after the control changed hands. Obviously, as Mr. Gidney pointed out, the new owners have to do something wrong after acquiring the stock. It takes a few months to change over the policies of a bank, and we did not find in any of the cases where it would have been possible to act any sooner if we had had the information sent to us immediately.

Senator SPARKMAN. Mr. Chairman, may I ask a question at that point?

Senator ROBERTSON. Yes. Senator Sparkman.

Senator SPARKMAN. Mr. Gidney, you are not only Comptroller, but also a member of the Federal Deposit Insurance Corporation Board; are you not?

Mr. GIDNEY. That is right.

Senator SPARKMAN. In the case to which I presume Senator Douglas refers, out in Illinois, there was a complete change of stock ownership, and very soon thereafter there was an acquisition of certain so-called assets that certainly the Federal Deposit Insurance Corporation would not have been willing to insure—I believe that was the testimony which was given—had they made up the important part of the overall assets at the time the insurance was asked for. But the Federal Deposit Insurance Corporation knew nothing about the sale or the acquisition of those assets until trouble that was practically irreparable developed.

Do you not feel, regardless of the necessity of notice to the Comptroller of the Currency—do you not feel that certainly there ought to be some kind of notice to the Federal Deposit Insurance Corporation if it is carrying insurance on the deposits of that bank?

Mr. GIDNEY. Well, that is a very large field of discussion and I have not prepared myself to go into it.

Senator SPARKMAN. I wonder if you are familiar with the case I am talking about?

Mr. GIDNEY. I know quite a lot about the case.

Senator SPARKMAN. Witnesses from the Federal Deposit Insurance Corporation did testify both here and in Chicago regarding it.

Mr. GIDNEY. I think the transfer of ownership that was the question there was that which resulted in the State auditor, Hodge, becoming the owner, which was not known——

Senator SPARKMAN. No.

Mr. GIDNEY. Maybe there is some other transfer I do not know about.

Senator SPARKMAN. No. It was not that. It was tied in with the overall, but that was actually not it.

If I recall correctly, there was a change of ownership, and almost immediately after that change was made the new bank acquired several millions of dollars worth of assets that were, I will not say of dubious value, but certainly of a high-risk nature. It was not very long until the bank was in trouble.

Mr. GIDNEY. I do not recognize some of the facts as brought out, so perhaps——

Mr. ROGERS. In that case the important point was how fast it happened that this group got control of the bank and then dumped their paper with a doubtful value on the bank, all in a period of about a month's time.

Mr. GIDNEY. I do not have all of those facts clearly in mind.

Mr. ROGERS. The testimony was that the Federal Deposit Insurance Corporation did not have knowledge at all, but the State chief examiner learned of it by reading of it in the American Banker newspaper.

Mr. JENNINGS. There is one other point, if I may add a statement. We are notified of every change made in the board of directors of a national bank. It just one director leaves and resigns and a new one is appointed, we do not pay much attention to it. If there is a wholesale change in the board of directors, we learn about it immediately and we look into it to see if something is wrong. So we do have that safeguard.

I am not sure whether that was in effect in Illinois or not.

Senator BENNETT. I would like to make this observation: In effect, the president or the cashier cannot be required to give notice after the purchase or sale. The only official notice they would have would be on the transfer of the stock.

Mr. GIDNEY. That is right.

Senator BENNETT. So, in effect, all you can actually require them to do would be to notify the Comptroller or the Federal Deposit Insurance Corporation after there had been a transfer. It would seem to me people who then wanted to acquire the bank stock for an improper purpose would make sure the transfer did not occur, because they could effectively hold the stock in the name of the seller without setting this machinery in motion.

Mr. GIDNEY. I think that actually occurs in cases, and it does not show until it leaves the bank. This is not anything we strongly object to, but we do not think that it is helpful.

Senator MONRONEY. Is there anything in the law which would prevent the holding of bank stock in insured banks by dummies? It can be done now.

Mr. GIDNEY. I think there is nothing in the law that prevents holding of bank stock by anyone except bank holding companies, which companies are limited. Other than that, I know of no provision in the law which says who shall or shall not.

Senator MONRONEY. But must they disclose the real owner? For instance, a racketeer in the name of some schoolteacher buys 50 percent of the stock of a bank and still escapes any liability under the law.

Mr. GIDNEY. As far as I know, he could own it. The racketeer could own it himself or have it owned in the hands of a dummy, as far as I know.

Senator ROBERTSON. Except that one national bank cannot own the stock of another.

Senator MONRONEY. But one racketeer can control the stock of a bank without any public knowledge.

Mr. GIDNEY. I thought that was always an unpleasant possibility in our laws. Any one of the notables in that field could have bought a bank. Fortunately we have gone along without that, and maybe it is because we are lucky.

Senator MONRONEY. But had it been illegal for the ownership to be concealed by the State auditor in the Chicago case, then he would have had to disclose his financial interest in it at the time he bought it.

Senator SPARKMAN. That is right. But let me say the bank I referred to was not one, or at least at the time I referred to it it was not the one in State auditor ownership, but an entirely different group.

Senator MONRONEY. Should not something be in the law to require the true ownership of banks to be made public? It seems to me the undermining of a bank by the acquisition by racketeers, criminals, or politicians who might wish to operate it themselves, would not be in the public interest.

Mr. GIDNEY. That is a pretty difficult and extensive subject. I suppose you can go to lots of other corporations maybe more important than banks, but if there is a practical way and a simple way that it can be fixed it might be well to look for it. I do not know. I think we are getting along very well and we do not have to look ahead on that in the national bank system to that particular thing. Yet it could happen tomorrow. It might be happening this minute.

Senator DOUGLAS. I think Senator Monroney put his finger on a very important point, and I would like to request that counsel prepare a draft of an amendment on this point. I do not see any good purpose to be served in concealing the actual ownership of bank stock. I think that should be done.

Mr. GIDNEY. It might be worth seeing what could be done.

Senator ROBERTSON. The committee counsel will take note of the request of the Senator from Illinois and have it ready for us when we mark up this bill, so to speak, on the 25th.

Senator BUSH. What is the purpose of the amendment?

Senator ROBERTSON. An amendment along these lines: That we can improve on this language so the committee will have something to vote on at that time.

You may proceed.

SECTION 26. ELECTION OF DIRECTORS

Mr. GIDNEY. In Section 26 (c) mandatory cumulative voting in the election of directors of national banks has been eliminated and provision made for permissive cumulative voting in those banks which desire it. We have previously testified both before this committee and before the House Banking and Currency Committee in favor of similar legislation after being advised by the Bureau of the Budget that there was no objection. We strongly endorse this provision of the bill and recommend that it be enacted.

Senator ROBERTSON. The Chair recognizes the Senator from Illinois.

Senator DOUGLAS. I did not ask for the recognition. Why do you take the position that you do, Mr. Gidney?

Mr. GIDNEY. This question was raised by the American Bankers originally.

Senator DOUGLAS. I understand.

Mr. GIDNEY. They had the legislation introduced and supported it throughout.

Senator DOUGLAS. I understand that, but that does not require you to underwrite every position which they take.

Mr. GIDNEY. I do not agree with everything. That is true.

Senator DOUGLAS. You are a free-minded being yourself and have the right to make up your own mind, but what I am trying to get at is, why do you take this position, and not why does the American Bankers Association take it.

Mr. GIDNEY. I am getting out my authorities first. The Independent Bankers, representing the small banks, supported it.

Senator DOUGLAS. Is this the function of the Comptroller of the Currency—to find out what the bankers want and then immediately to say, "Me too"?

Mr. GIDNEY. Not necessarily, and he does not do so; but in this particular case I think the bankers are right.

Senator DOUGLAS. Why? That is what I want to get at.

Mr. GIDNEY. Because we feel the operation of this provision of cumulative voting as we observed it has not been advantageous and has not been good.

Senator DOUGLAS. In what respects?

Mr. GIDNEY. We have seen people go out and buy stock—the idea sounds good, that stockholders have a right to be represented.

Senator DOUGLAS. You say theoretically cumulative voting is correct.

Mr. GIDNEY. Theoretically it has an appeal.

Senator DOUGLAS. And is correct?

Mr. GIDNEY. I do not go that far. It has an appeal. It sounds good.

Senator DOUGLAS. It sounds good because it seems good. Is that right?

Mr. GIDNEY. If you do not look beneath the surface it seems good, but if you look beneath the surface——

Senator DOUGLAS. Go beneath the surface. What bad effects have you observed in practice?

Mr. GIDNEY. We have seen almost invariably the people who seek to force themselves on the Board in that way do so for the purpose of self-aggrandizement.

Senator DOUGLAS. Is that not a rather common motive in life?

Mr. GIDNEY. Yes.

Senator DOUGLAS. If you bar self-advancement, what becomes of business ambition?

Mr. GIDNEY. That is right.

Senator DOUGLAS. And free enterprise, and political effort?

Mr. GIDNEY. We cannot scold it, but it does not necessarily have a good effect on the institution. We have people who were not stockholders who go and buy a block of stock which they think is large enough to put them on the Board. They are volunteer members, so to speak, coming from the outside. We have seen frictions introduced in banking situations in many, many cases, and, frankly, they have been more numerous in the 2 years or so that this thing has been pending. Lots of folks did not seem to know about this before it was introduced. Now it is getting quite commonplace for the bankers to let out a cry of pain that someone is trying to do this to them. We have not seen cases where it has been helpful. It ought to be helpful sometimes. In some of these cases Senator Monroney spoke about, where some old rascal is trying to hold everything, it might be good, but we have not seen it help us out in these cases. It is most common where the management is all right that these people push in.

This is again a matter of opinion, but my opinion is we ought to get rid of that.

I do not have all of the facts about how it came into the law, but I believe it was testified before this committee or the House committee—and Mr. Wolcott will remember it—by Charlie Zimmerman. If I had a little more time I would have checked with his testimony. He said it was put in the law by or at the instance of Mr. Giannini, who wanted to have that help in pushing on to the Board of the New York City Bank in which they had strong holdings——

Senator ROBERTSON. He did, and he gave some very fine testimony. That was the gentleman from Pennsylvania. He was active in 1933, when that law went into effect.

Mr. GIDNEY. Yes, and he was an active member of the Independent Bankers Association.

Senator DOUGLAS. Everything you say is derivative. You say that the American Bankers objects to it, and the Independent Bankers objects to the provision, and so-and-so objects, and only Mr. Giannini originally asked for it. I want to know what Mr. Gidney, the Comptroller, believes, and why he believes it. Stand on your own feet.

Mr. GIDNEY. O. K. I never do anything different. I believe from my observation of its working it is not a good provision.

Senator DOUGLAS. Why?

Mr. GIDNEY. For the reasons we have mentioned.

Senator DOUGLAS. You mean people get on the boards whom the bank managements do not want on the boards? Is that not really your point?

Mr. GIDNEY. It is more than that. People come on the boards who come on for the purposes of self-glory. One man we knew about wanted to put his 21-year-old son-in-law on the board to build up the son-in-law.

Senator DOUGLAS. Has that not been done by the majority stockholders?

Mr. GIDNEY. That is done to build up the board.

Senator DOUGLAS. Is this peculiar to minority stockholders? Have not majority stockholders done this?

Mr. GIDNEY. Probably.

Senator DOUGLAS. As a matter of fact, if you have minority representation, is it not much less likely that the majority will make of a bank a means of providing outdoor relief for the younger members of their families?

Mr. GIDNEY. That is possible.

Senator DOUGLAS. You see, we have a provision for compulsory cumulative voting for industrial companies. We have had experience with it and on the whole it has worked out quite well. I might say in the famous struggle for the control of Montgomery Ward, although the group which tried to take over Montgomery Ward did not get control, they did get minority representation, and the airing of the complaints resulted in the majority deciding they had better remove the old management. They put in new management, and there is apparently much greater harmony inside the company. There has been a great distribution of the undistributed profits to stockholders, so that the stockholders are satisfied, and there has been a more aggressive policy in the opening of retail stores.

I think the general judgment would be that that dispute, which was only made possible by cumulative voting, has been a very good thing, not only for the company, but for the stockholders. Might that not occur in the matter of banks?

Mr. GIDNEY. That might be. God moves in mysterious ways his wonders to perform, and when a gentleman who might be unfavorably characterized pushes in, it might do some good.

Senator DOUGLAS. There is no objection to economic democracy, just as it is good to have two parties in politics. I think we all are for that.

Mr. GIDNEY. I am strongly for that.

Senator DOUGLAS. The opposition party would be the out party. So why is it not good to have different opinions expressed in business, provided the majority will rule?

Mr. GIDNEY. There are exceptions to anything one can say, but the general method of selecting bank directors is to try to get strong, qualified directors, who will strengthen the bank and contribute to its good management. Of course, there are exceptions under either rule and our belief is we will get better and more harmonious management by the majority rule than by the cumulative voting rule.

Senator CLARK. Will the Senator yield?

Senator DOUGLAS. Yes.

Senator CLARK. Mr. Gidney, on this question of cumulative voting, has it not been your general experience that vacancies on the boards of directors of most national banks are, as a practical matter, filled by the existing management and existing directors, and not stockholders? In other words, it is not the custom to say, "Whom will we get to fill that vacancy? Here is Charlie Jones, who is well known in the community. We like him and he gets along well with us. Let's put Charlie on the board."

When the proxies come out at the next annual meeting there is a request to put Charlie Jones on the board. Is that not the usual way?

Mr. GIDNEY. That is a prety accurate description.

Senator CLARK. And you think that is a pretty good way?

Mr. GIDNEY. It has probably an even more practical connotation than that. They usually say, "Who is an outstanding man that we can get who will improve our standing in the community and who will bring us business?"

Senator CLARK. So it comes from the top down and not from the stockholders up.

Mr. GIDNEY. It comes from a group which is highly representative of the stockholders. You have a representative government there.

Senator CLARK. But, in effect, if you make this change, you recommend there will be very few national banks chartered with compulsory cumulative voting.

Mr. GIDNEY. I think that is probably true.

Senator CLARK. So in the end what you will achieve will be to remove a check on the power of management.

Mr. GIDNEY. And I think there are very few State banks that have cumulative voting.

Senator CLARK. But the end result will be to remove the check from the power of management. That may be a good thing to do, but that will be the effect, will it not?

Mr. GIDNEY. I do not believe that is a good check on the power of management because I do not think it is exercised in a good way.

Senator CLARK. But, in effect, what you are saying—and I am not quarreling with you, but want to get your view——

Mr. GIDNEY. O.K.

Senator CLARK. In effect, what you are saying is that the management knows best and the stockholders should not have the opportunity of putting somebody on the board who may well disagree with management.

Mr. GIDNEY. You might quote it that way.

Senator CLARK. Again I am not disagreeing with you, but I want to know your view.

Mr. GIDNEY. I know Senator Douglas comes from a State where cumulative voting is in the constitution, and it has high standing in his State. The State banks in New York State do not have cumulative voting.

Senator CLARK. We have the Pennsylvania Railroad in Pennsylvania involved in a situation where cumulative voting will permit election of a minority director, and the men who run the railroad to my way of thinking are very excellent and capable and able businessmen. But they had the absolute vote, and when it was suggested that the sstockholders have the right to put him on the board, they fought it all through the courts. I have a question in my own mind as to whether that much power for management is wise, or if you should not have a little stick under the table so that perhaps a minority group of stockholders could put someone on the board.

I suggest the board of directors of a bank is not a club and should not be able to blackball somebody because they do not like him, if he has enough shares to get on the board.

Mr. GIDNEY. I think there are cases where exactly that may have happened, but they are not normal. The normal is the banks are looking for the best board they can find. If you will go into any city like Philadelphia and go down the list of the directors of banks, you will see they have reached for the best, and if it is a large and important company they have reached for the highest man they can get.

Senator CLARK. I suggest the end result is you get a very amiable and able group of individuals who run the banking community pretty much by themselves. If you believe in the trustee process, that is a fine thing. If you believe, as Senator Douglas said, in economic democracy as well as political, perhaps it is better to have a little more——

Mr. GIDNEY. I think I believe in the trustee process.

Senator CLARK. That is what I want to get at.

Mr. GIDNEY. I think it is noteworthy and might be noted in your proceedings here that on the coast the very large Transamerica Corp. did not actually exercise its cumulative voting in the election of the Citizens National Bank, but they did say they were prepared to, and thus attained their purposes. Maybe that is good, and maybe that is not. Maybe that is an illustration of how this is good. But I think it ought to be noted.

I believe, standing on my own feet, Senator, that it would be better if we were not to have this provision for the national banks.

Senator CLARK. Thank you.

Senator ROBERTSON. Thank you. You may proceed.

Mr. GIDNEY. This next is merely a technical matter, but of some importance.

SECTION 29. REMOVAL OF OFFICERS AND DIRECTORS

This section provides that hearings held by the Board of Governors of the Federal Reserve System to remove directors or officers from office shall be subject to review as provided in the Administrative Procedure Act, "and the review by the court shall be upon the weight of the evidence." There is an inconsistency. The Administrative Procedure Act provides that the reviewing court shall set aside agency action "unsupported by substantial evidence." Thus it seems that there is an inconsistency in saying the review shall be as provided by the Administrative Procedure Act, and then adding that the review shall be upon the weight of the evidence. We recommend that review should be as provided in the Administrative Procedure Act and that that portion of the fourth sentence of section 29 referring to review upon the weight of the evidencce should be deleted.

On the weight of the evidence, and means, I suppose, that the court may be come a judge and jury, and they are a jury as well as a judge.

The Administrative Procedure Act is satisfactory and we would like to stick with it.

Next we have the section on corporate powers. I think I can brief it. It is authorizing banks to contribute to nonprofit organizations. We think it would be well to confine that the nonprofit organizations and the word "nonprofit" be retained in the bill.

In the original recommendation we did not stipulate nonprofit, and we note Mr. Cravens was for the elimination of the word "nonprofit," and Mr. Lyons, representing the American Bankers Association, did not favor it. We think on the whole it would be just as well to let nonprofit stay in, although this is a matter in which your opinion is as good as or better than ours. We will take what you give us on it.

Of course, if we go into profitmaking organizations, we may be inadvertently opening up the door to a national bank buying stock, which is prohibited elsewhere. If we confined it to nonprofit probably that opening would be unobjectionable.

Then we come to stock options.

Section 31 (a) (9) would authorize any national bank to grant options to purchase its capital stock to its employees or to employees of any subsidiary corporation. We are aware that stock option plans are now in effect in 40 percent of the corporations whose stocks are listed on the New York Stock Exchange and are gaining increased use in industry generally, and that the justification given is that they are necessary in the procurement and retention of top rank officers. The only reason it is necessary to enact specific legislation to permit national banks to formulate and use stock option plans is because of the preemptive stock purchase rights of existing shareholders when additional stock is sold. We believe that banks should be on a parity with other corporations with respect to their right to use such plans when they have been soundly conceived and after approval by the Comptroller of the Currency.

We make that statement somewhat reluctantly, because I personally do not think too much of the plans generally, but if other corporations can have them, probably banks should.

However, we strongly urge that such legislation contain the following safeguards:

(*a*) We would suggest that national banks be permitted to grant only restricted stock options of the type which qualify under section 421 of the Internal Revenue Code of 1954.

I do not know the provisions of that code myself, but I take the word of the lawyers for it.

(*b*) We suggest that the statute provide that no stock option plan shall be approved by the Comptroller if the option price is less than 85 percent of the fair market value or 85 percent of book value—recognizing many times market value is not present in small banks—as determined by the Comptroller, whichever is greater. The purpose of this requirement is to prevent too great a dilution in book value which would otherwise be suffered by the bank's other shareholders in those instances where the fair market value is below book value.

I believe Mr. Cravens is for this, and Mr. Fleming and Mr. Lyons, and Mr. Turner of the chamber of commerce is silent on it. We recognize we would have quite a difficult administrative problem coming to us with this, and we would like to be encouraged to be on the conservative side in its handling if we have it.

In my visit to the coast I found there was quite a little interest in the stock options granted to an individual in a State bank—they can do it in the State banks in California—and some evidences of disapproval or disbelief in the particular kind of transaction. I have my misgivings about it, but I think it is a matter for this Congress to decide, and we will try to handle it well if it is given to us.

Senator DOUGLAS. Does not the stock option possibility give to the management the opportunity to reward itself at the expense of inarticulate stockholders?

Mr. GIDNEY. We would suggest that it be allowed only with a two-thirds vote. I think that should be required. But I think it does give possibilities for management to reward itself. That is why I am somewhat uneasy about it.

Senator DOUGLAS. Are you not making another very good indirect argument for cumulative voting, so that the inarticulate stockholders may have the incentive of duty with the board of directors?

Mr. GIDNEY. Unfortunately it has an implication of that kind.

Senator DOUGLAS. Why do you regard it as unfortunate if it helps cumulative voting? This definition should be judged on its merits.

Mr. GIDNEY. I withdraw the "unfortunately" and say it has an implication of that kind.

SECTION 32. DEALING IN SECURITIES

Section 32 (b) would provide that a national bank may, with the approval of the Comptroller, purchase and hold for not more than 90 days stock of another bank as a step in a proposed absorption of such other bank through merger, consolidation, acquisition of assets and assumption of liabilities, or otherwise. We are opposed to enactment of this proposed legislation. Two or more national banks may merge or consolidate only upon the approval of the holders of two-thirds of the stock of each bank. If the directors of the absorbing or continuing bank could use bank funds to acquire control of another bank or banks they would, in effect, be able to acquire the other bank or banks by virtually forcing the approval of two-thirds of their stockholders. Once the bank owned control of another bank, the shareholders of the acquiring bank would, as a practical matter, have very little choice but to vote for the proposed merger or consolidation. We do not believe that it is proper for the officers or directors of a national bank to use the bank's money to acquire stock in another bank as a first step to merging or consolidating with that bank. We have similar beliefs with respect to any Federal legislation affecting State banks that are members of the Federal Reserve System.

We have not needed this particular form for the mergers which have taken place by national banks, and we think it would be better if it were not enacted.

Mr. ROGERS. Have there ever been cases where national banks have ever actually done this?

Mr. GIDNEY. I do not believe so. We have had a case not too long ago where directors borrowed from their own bank and we hit them as hard as we could and made them get the loans out of there and not let it happen again, but I do not believe we have had actual cases where banks have done it that way. There are some cases where stock has come into the banks in the past for debts previously contracted, or for different things, and also through liquidation of a subsidiary company, and there are cases where there is stock in the banks. But as to going out and buying it, it not normally done.

Mr. JENNINGS. It has been a fairly common practice, on the west coast particularly for banks that are considering a merger, usually in the form of a purchase and sale, for the individuals, the directors in their individual capacities, to go out and pick up a bunch of the stock. But if we do not approve the merger or purchase, they own the stock, and that is the end of it.

Mr. ROGERS. Your position is this provision is not necessary to consummate a merger. If you do put it in it is likely to be open to abuse?

Mr. JENNINGS. Yes.

Mr. GIDNEY. Yes, it could be. I am afraid it would have some more implications of the kind Senator Douglas is interested in. I am afraid this would have another implication along this line.

Senator DOUGLAS. You seem to be making a very good case for cumulative voting.

Mr. GIDNEY. I do not mean to. Now we have a rather technical matter of the maximum loan limitations, in section 34.

In the testimony of one of the previous witnesses before this committee a question was raised as to the word "identical" in exception 6 (B) to section 34 and as to whether the use of that word might create problems. We merely wish to point out that this is the language which exists in the present statute and we have had no problems arising out of its use.

That is a loan on readily marketable staples. The note arising out of the same transaction shall not continue more than 6 months on the identical staples. You can substitute the words "same staples" for "identical staples." It is really what we mean, and it does not give us trouble.

Exception 12 to section 34 places a new limit on negotiable or nonnegotiable installment consumer paper of 25 percent of capital and surplus, but provides that upon certification by an officer of the association that the responsibility of the maker of each obligation has been evaluated and that the association is relying primarily upon the maker for the payment of each such obligation, the obligation of each maker shall be the sole applicable loan limitation. It is recommended that this proviso be amended to read as follows:

> *Provided, however*, That if the bank's files or the knowledge of its officers of the financial condition of each maker of such obligation is reasonably adequate, and there is a certification by an officer of the association, designated for that purpose by the board of directors of the association, that the responsibility of each maker of such obligations has been evaluated and the association is relying primarily upon each such maker for the payment of such obligations, the limitations of subsection (a) of this section as to the obligations of each such maker shall be the sole applicable loan limitation: *Provided further*, That such certification shall be in writing and shall be retained as part of the records of such association.

We would like to make it a little more formal, that they have the records to justify this. The only change is that their files show it. We do not want these folks to get the idea that putting their name on the certification is all that is needed. We want it to be thorough.

Mr. ROGERS. I think you weaken that provision if you say it is in the knowledge of the officers. They can say, "We have no record, but we know it."

Mr. JENNINGS. No. When the examiner is examining the bank he is going to discuss the items, and he can find out in a hurry whether the banker knows about those items or not. In some cases they carry some of the information in their heads and do not have it all in their files, so we do not want to bar that.

Mr. ROGERS. You do not think it would weaken it?

Mr. GIDNEY. The point is, I think it is all right. We do not want it to get to the point where they make that certification just on the theory this consumer paper does all right as a general thing. Our experience shows it comes out all right. We want them to do a little work on knowing the individual names. It is not going to be a tremendous lot of work, but probably results in getting a card file on a man with some credit reference there, like where he works, and a few things like that.

Senator BENNETT. In practical operation let us take an automobile dealer who sells a car on credit. He does some credit work on his applicant before he issues the original paper. Would a copy of his original credit information in the hands of the bank satisfy the file requirement?

Mr. GIDNEY. Quite likely it would, I think. Some do and some do not. Of course, it varies. In my visit to California I think I picked up the information that in a good many cases now dealers are saying to the banks, "You take all of my paper or none at all." There would be a little conflict there. They certainly would want to sort that out, so that the paper they liked all right on its own was within this exception.

Senator BENNETT. You raise another interesting question. Suppose 90 percent of the paper taken by the bank is satisfactory in terms of credit information that has been supplied, and 10 percent of it is not. If that 10 percent is still within the legal limits of the man from whom they bought the paper, then the banks can use both devices?

Mr. GIDNEY. That is right.

Senator BENNETT. And still take all of the paper?

Mr. GIDNEY. That is right. They can do so. I think we will have some problem in that. I believe there is pressure on the banks to take nonrecourse paper, which of course we would——

Senator BENNETT. And that would go within the existing limitations of the man from whom the paper is taken?

Mr. GIDNEY. That is right. It is within the exceptions now because each name provides the limitation there. We hope that our requirements for credit knowledge there will be adequately met.

Mr. JENNINGS. I think I should point out that in the event a bank has a line of credit with a particular dealer and it goes beyond 25 percent, I do not think our examiners or our office would accept just the credit work that had been done by that dealer. We would expect the bank to go into that additional paper with greater thoroughness. After all, if a bank is relying wholly on the seller, it has been found indirect paper does not pay out as well as the direct loans a bank makes itself.

Senator BENNETT. You are saying you will allow the bank the full 25 percent on one class of paper, and a full 10 percent on another class of paper, giving it in effect 35 percent?

Mr. JENNINGS. That is correct.
Mr. GIDNEY. They could go much higher than 35.
Mr. JENNINGS. They can.
Mr. GIDNEY. If they can pass this test.
Senator BENNETT. Yes.
Mr. GIDNEY. They can go to 100 percent or more.
Senator BENNETT. In relation to the individual loans on which they have adequate credit backing.
Mr. GIDNEY. Yes.
Senator MONRONEY. Is it true even though the banks secure the endorsement of the automobile dealer, that if it is on a good credit risk of the individual maker then it is exempt from the limits which would apply to the dealer?
Mr. GIDNEY. Yes.
Senator MONRONEY. It is additional security that the bank asks in its endorsement for recourse paper from the dealer?
Mr. GIDNEY. That is exactly what this does, and I think is a rather good provision, but I think its function would be good to the extent they watch or they are genuine in their treatment of that thing.
Senator MONRONEY. But each note has to stand on its own bottom?
Mr. GIDNEY. A mere laying on of hands would not be adequate.
Mr. ROGERS. My only fear is you are giving the bank an out with reference to that new phrase. If you leave it in as it is now they have to prove they have the knowledge, but this way they can say, "It is in my mind," and you cannot argue with them.
Mr. GIDNEY. "Or the knowledge of its officers" is what you mentioned there.
Mr. ROGERS. Yes.
Mr. JENNINGS. If I examined a bank and found the bank loan officer knew nothing about the makers on a line of credit that went over 25 percent, I do not think I would have very much trouble with the board of directors if I asked them to come in later. It is just a question of fact as to whether they do or do not have some data on those, however. In the larger banks their files would be all right. In the smaller banks I believe the bankers know their customers personally to a greater extent, and they would have some of the credit information in their heads. I do not think we will have trouble on that.
Mr. GIDNEY. I wonder if we changed the word "or" into "and"—might it not do that?
Senator BENNETT. Then they would require files and knowledge, and that avoids what you are trying to get at, which is a situation in which files do not exist.
Mr. GIDNEY. The last "and."
Mr. JENNINGS. No. We could not work with it.
Mr. GIDNEY. You could not work with it?
Mr. JENNINGS. No.
Senator ROBERTSON. You may proceed.

SECTION 35. MAXIMUM RATE OF INTEREST

Mr. GIDNEY. The committee has added a new sentence at the end of subsection (a) of this section which would have the effect of permitting national banks to discount paper on the same basis permitted to State banks in the States wherein they are located. The purpose of this addition is to make it clear that national banks are no longer bound by the holding in the very old case of *National Bank v. Johnson* (104 U. S. 271). That case held that the purchase of paper from a dealer by a national bank was a discount within the meaning of the present Federal statute which limits the rate of interest which national banks may charge on loans or discounts to that prescribed by the laws of the State for State banks, or if there is no limit on State banks, to 7 percent. In some States the purchase of paper from a dealer by a State bank is regarded as a purchase and sale transaction to which the interest laws do not apply. In those States there is no limitation on discount transactions. In those States where there is no limitation this raises a question as to whether national banks are not limited to 7 percent on such discount transactions even though there is no limit on the State banks with which they are in competition. Under the bill it will be clear that national banks have the same rights in this respect as do State banks.

In his testimony before this committee Mr. Cravens suggested language to be substituted for the language in the committee bill reading as follows:

> The purchase of obligations or evidences of indebtedness from the actual owner thereof shall not, for the purposes of this section, be deemed a loan or discount if such purchase would not, under the law of the State in which the purchasing bank is located, be deemed a loan or extension of credit subject to the interest or usury statutes of such State.

We favor the language suggested by Mr. Cravens and recommend that it be adopted.

SECTION 36. REAL-ESTATE LOANS

Under present law national banks may make real-estate loans in aggregate amount equal to the amount of the bank's capital stock and surplus, or 60 percent of the amount of its time and savings accounts, whichever is greater. Section 36 of the proposed act would permit national banks to make real-estate loans in an aggregate amount equal to either of these sums or 20 percent of its demand deposits, whichever of the 3 is greater. We have no objection to this proposal except that we believe that public funds and deposits owing to other banks should not be included in demand deposits for the purposes of this section.

I think Mr. Lyons, representing the American Bankers Association, wanted 20 percent of all deposits, and Mr. Fleming, representing the Reserve city bankers, agrees with our suggestion.

This section would also change present law by increasing the aggregate limit on construction loans which are not to be considered as loans secured by real estate from 50 percent of capital to 100 percent of capital and surplus. We favor this proposed change.

Mr. ROGERS. When Mr. Ely was here from Robert Morris Associates, he raised the question that there was a need for completion bonds.

Mr. GIDNEY. Yes. When this was up a year or so ago we suggested that that be included in the legislation. The banks and bankers in whom we had the highest confidence told us that was impracticable, onerous and costly, and not productive of good. We have concluded that they were right. We had put that in and the matter had come up rather hurriedly, and we made it tight enough so that we could go for it. We put that in but we decided it was not necessarily helpful, and we backed away from it.

Mr. ROGERS. I wanted the record to show that that had been in the previous bill and you had considered it.

Mr. GIDNEY. And the bank may make it when it is advantageous or necessary in a particular case. If we put it in the statute it requires they do that, no matter how good their builder is. If you have a builder who is definitely, thoroughly good, why go to the expense of a completion bond? If you have one who is very poor and they need it, they can still get it. We do not have to instruct these banks in every matter of credit judgment, because some of them are pretty smart themselves. So we thought we would back away from that.

Senator MONRONEY. Is there any difference between a Government-insured realestate mortgage under the law and the regular claimant here?

Mr. GIDNEY. Yes. There is very definitely. You are speaking of FHA?

Senator MONRONEY. Yes. This will apply only to real-estate loans on which there is just a conventional mortgage?

Mr. GIDNEY. These are construction loans. While we have it already for residential property, such as an apartment house, we need it for construction of commercial properties, there is an interim mortgage with interim financing while the thing is being built. It is larger than the 50 percent permanent mortgage they can make on that property. A responsible lender gives a commitment to make a loan when the building is completed.

Senator ROBERTSON. Is that all on this section?

Mr. GIDNEY. We have one other item here. There would be added to this section a new subsection (e) which would permit loans to be made to manufacturing and industrial businesses, where the bank looks for repayment out of the operations of the borrower's business, without such loans being regarded as real-estate loans, even though secured by a mortgage on real estate.

We favor this provision and all of these who testified were for it.

Senator ROBERTSON. The Chair wishes to make this comment: While the witness has concluded 14 and a fraction pages of his prepared statement, there is almost that much of his prepared statement left, although I doubt if the remainder will take as much time as the initial part. The witness concluded a discussion of all of his recommendations and nearly all of the other recommendations pertaining to the National Banking Act. The remainder of his discussion, and it was very kind of him to do it, comments on suggestions made to us about the Federal Reserve Act and the Federal Deposit Insurance Corporation. So since we will have to have an afternoon session, the Chair suggests that the committee stand in recess now until 2:30 p. m., and our session in the afternoon it should enable us to complete the hearing of this witness.

(Whereupon, at 12 noon the subcommittee recessed until 2:30 p. m. of the same day.)

AFTERNOON SESSION

Senator ROBERTSON. The subcommittee will please come to order.

Before our distinguished Comptroller of the Currency continues with his testimony, I feel I should announce to him that the president and five members of the Virginia Bankers Association were so much interested in what he is telling this committee that they have come to listen to him this afternoon.

Mr. GIDNEY. That is fine.

Senator ROBERTSON. We will be pleased to hear from you, Mr. Gidney. After you have finished testifying, I hope you can meet all those members.

Mr. GIDNEY. I believe I am going to go and have dinner with them, is that right?

Senator ROBERTSON. Well, that is fine. They came to show that they weren't going to sprinkle any rat poison on you.

You may proceed.

Mr. GIDNEY. We have come to section 44. Engaging in the securities business. This is a limited part of that.

A question has been raised in earlier testimony before this committee as to whether the change which was made in subsection (b) of this section is adequate to accomplish the purpose stated in our original recommendation, i.e., to provide protection against State corporations receiving deposits without State or Federal supervision. We are satisfied that this section as drawn will satisfy our purpose.

Senator BENNETT. Mr. Chairman, by "State corporations," you mean State building and loan associations?

Mr. GIDNEY. Anything.

Senator BENNETT. Any corporation chartered by the State?

Mr. GIDNEY. This is protection against State corporations of any kind receiving deposits without State or Federal supervision, unsupervised corporations.

Mr. JENNINGS. We do not include savings and loan associations?

Mr. GIDNEY. Oh, no. They are supervised. There was an outfit in Texas which calls itself United States Trust, or something, and it wasn't supervised by anybody. It went hideously broke.

Senator BENNETT. Well, the fact that in your copy of your testimony the word "State" and the word "Corporations" is capitalized made me wonder whether there is any particular special——

Mr. GIDNEY. I wouldn't know what that was capitalized. It could be small case.

Senator BENNETT. O. K.

Senator LAUSCHE. Mr. Gidney, in most cases you cannot receive deposits for safekeeping without some supervision?

Mr. GIDNEY. That is right.

Senator LAUSCHE. I don't believe we have any in Ohio.

Mr. GIDNEY. I think no.

Senator LAUSCHE. But if there are some, your statement here covers it?

Mr. GIDNEY. Yes, sir.

This is confidentially of examination reports:

Section 50 would make examination reports, related correspondence and papers, and other information obtained by the Comptroller of the Currency in the exercise of his visitatorial powers, confidential documents privileged against disclosure without the consent of the Comptroller of the Currency. This is in accordance with one of our recommendations and we favor its enactment. There has been added a proviso to the effect that such documents shall be made available to the committees of the Congress upon request. This proviso would seem ineffective to compel the Comptroller to make such documents available if it is determined by the Executive that it would not be in the public interest to do so.

That is a constitutional question. We do not know the answer.

We do not see how this proviso changes the situation as it presently exists, so we are not opposed to it, although we would prefer its deletion.

That is just a little notice that we think we could stand on constitutional grounds.

The next is reports by national banks.

Section 52 would require that each national bank shall make to the Comptroller not less than three reports of condition and of the payment of dividends during each year. We recommend that the words "and of the payment of dividends" be eliminated from the first sentence of this section. We now receive semiannual reports of earnings and dividends of national banks and this has proved to be entirely adequate. We see no reason for requiring three reports of payment of dividends.

If it were reduced to two, that would be all right.

We do not believe that it is necessary that the Comptroller be given specific statutory authority to call for reports of earnings and dividends as he does so now and may continue to do so under the power given to him to call for special reports from national banks.

This section has raised some questions as to whether under its authority the Comptroller could require national banks to publish reports of earnings and dividends, and also as to whether he could do so on a selective basis, that is, require some banks but not others to publish such reports. We do not recommend that national banks be required to publish reports of earnings and dividends. We also believe that there is some concern about differences in form and publication requirements for statements of condition. We would have no objection if there were deleted from the fourth sentence of this section everything after the second comma, reading:

and the Comptroller may prescribe different forms of such reports, and make different requirements as to their publication for different banks according to their location, size, or other reasonable classification.

Senator Robertson. Let me interrupt there to say that the witness maybe objects to that provision in the tentative bill as being too broad, and we state that it was inserted merely to make it possible for one type of report to be had from a small bank and maybe a more comprehensive one from a large bank.

We didn't want to make it possible for the Comptroller or anybody else to single out somebody for special treatment for personal reasons.

Mr. Gidney. He certainly should not. I don't think we suggested it.

Senator Robertson. You think the language you have suggested would clarify that so that there couldn't be any reports required just for personal reasons?

Mr. Gidney. I think according to location, size, and other reasonable classification would——

Senator Robertson. Would make our purpose clear?

Mr. Gidney. Would take care of that.

I don't think we asked for that or care too much for it, but we would take it.

Senator Robertson. I believe we got it from the Federal Reserve.

Mr. GIDNEY. I think you did.
Mr. JENNINGS. That is correct, sir.
Mr. GIDNEY. I don't think we have troubles in taking the same form of report from all the banks, but it is possible that we could take it a little different from the first hundred, for instance.
Senator ROBERTSON. You may proceed.
Mr. GIDNEY. The power given in the statute to call for special reports is adequate to deal with all unusual or special situations.

SECTIONS 53, 54, 55. CONSOLIDATIONS AND MERGERS

In sections 53, 54, and 55 it is recommended that there be added a provision which would require——
Senator ROBERTSON. Without objection, you are recommending the same kind of bill we passed last year, are you, in this section?
Mr. GIDNEY. No, sir. This is a technical matter of dissenting shareholder asking for the value of shares.
Senator ROBERTSON. This is not the merger legislation?
Mr. GIDNEY. This is not the big merger.
Senator ROBERTSON. All right then, you can go ahead.
Mr. GIDNEY. What this adds up to is we would like to have him required to take his action within a fixed time and not be allowed to put in a word of dissent and then let it drag for an indefinite time. This is simply to require him to——
Senator ROBERTSON. Without objection, the entire statement on that page will go in the record as is.
(The material referred to reads as follows:)

In sections 53, 54, and 55 it is recommended that there be added a provision which would require dissenting shareholders who wish to demand the value in cash of their shares to do so by a written request made to the consolidated or merged bank within 30 days after the effective date of the merger accompanied by the surrender of their stock certificates. It is also recommended that for the first sentence of subsection (d) of each of these sections there should be substituted a provision which would provide that if within 90 days one or more appraisers is not selected or the appraisers have failed to determine the value of the shares, the Comptroller shall upon written request of any interested party, cause an appraisal to be made which shall be final and binding. The purpose of these changes is to insure that the appraisal of the shares of dissenting shareholders will be handled with reasonable promptness and that such appraisals cannot be delayed unduly by either the shareholders or the bank.

We would amend section 54 to expressly require the approval of the Comptroller of the Currency in the case of consolidation of State with national banks. Such approval has always been regarded as necessary under the existing statute, but the wording is not clear and has given rise to questions from time to time.

Section 55 should be amended by adding provisions identical to those contained in subsections (e), (f), and (g) of sections 53 and 54 dealing with continuation of corporate existence, automatic transfer of trust accounts, and freedom from preemptive rights. These provisions are contained in the present statute and were omitted from the committee print bill because of an error by our office.

Senator LAUSCHE. Is there any limitation now within which he has to finally assert his rights?
Mr. GIDNEY. I think that is just the trouble. He has to initially assert his rights quite soon.
Senator LAUSCHE. That is, he declares.
Mr. GIDNEY. He declares, but then we think he can coast——
Senator LAUSCHE. Without limitation.
Mr. GIDNEY. I think, without limitation.

Mr. JENNINGS. And there is another factor, Senator: It is so open now that possibly the bank could drag its feet, and we think that both parties should be in a position within 90 days after the shareholder has declared that he dissents and wants his value, that both parties should be in a position, if they wish, to come to the Comptroller and say "Here, this matter is dragging along. We would like you to make the appraisal, and we will be bound by it."

Senator ROBERTSON. You may proceed.

Mr. GIDNEY. Now we come to a recommendation of ours which did not get support from the bankers, but which we still think is meritorious, and that is payment by Federal Deposit Insurance Corporation and the Federal Reserve Board for the use of reports of examination of national banks. That is a share of the cost of making those examinations.

In our original recommendation we recommended (No. 37) that in order to eliminate inequities and to restore a more equitable balance between the State and national banking systems, the Federal Deposit Insurance Corporation and the Federal Reserve System should be required to make certain payments to the Office of the Comptroller of the Currency. At the hearings we suggested, as an alternative proposal, that payment be made by the Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation to the Comptroller of the Currency for copies of the reports of examination of national banks, which are regularly given to the Federal Reserve System and made available to the Federal Deposit Insurance Corporation of 50 percent of the cost of making such examinations, 25 percent to be borne by the Federal Reserve System and 25 percent by the Federal Deposit Insurance Corporation. This recommendation was disapproved by the Advisory Committee with no reasons being given. However, it is apparent that there is an existing inequity which is detrimental to the national banking system. For this reason we urge that the committee give careful consideration to our proposal and that it be enacted into law.

National banks now bear the full expense of the supervision and the examinations which they receive from the Comptroller's office. The entire expenses of the Comptroller's office are paid out of assessments levied on national banks. State banks, on the contrary, which are supervised and examined by the Board of Governors of the Federal Reserve System, or the Federal Deposit Insurance Corporation, as well as by the respective State banking departments, do not bear directly any of the expense of such Federal supervision and examination. In the vast majority of cases State banks are examined jointly by the State authorities and by the examiners of the Federal Reserve banks or the Federal Deposit Insurance Corporation. In many States such examinations are conducted only once a year. By conducting joint examinations with Federal examiners State banking departments are enabled to operate with smaller staffs and at less expense to the State banks.

Senator ROBERTSON. If I may interrupt there. You are aware of the fact that our advisory committee recommended against this?

Mr. GIDNEY. Yes, sir.

Senator ROBERTSON. You are aware that all the State banks are against your recommendation?

Mr. GIDNEY. Oh, I am sure they would be; yes, sir.

Senator ROBERTSON. While we are on that subject, I might ask you this question: I have heard some State bankers express the viewpoint that when a question arises about the possible need of a new bank in a given locality and you think there ought to be one there and the State authorities think there ought not to be one there, the State authorities ought to have the power to veto your answer. What do you think about that?

Mr. GIDNEY. Well, I don't think they should. I don't think they should. I think we probably wouldn't get many national——

Senator ROBERTSON. Of course, they can't do it under existing law. Do you think they ought to have the power to do it?

Mr. GIDNEY. No; I do not. I think that would reverse the purpose of Congress in 1863 and ever since and the long line of court decisions and that we wouldn't be chartering any national banks under that basis.

Senator ROBERTSON. I imagined that you felt that way about it, but I wanted to give you an opportunity to express your views.

Mr. GIDNEY. On the other hand, we don't assume to veto their charter of a bank either.

Senator ROBERTSON. You don't want to veto any State bank?

Mr. GIDNEY. We don't want to veto theirs. We do have a pretty good degree of comity with a great many States on this and get along quite peacefully.

For instance, I have been in communication within the last few days with the Commissioner where things are pretty red hot in chartering, and we are proceeding decently and in order, I hope, along about the same line. But sometimes the boys will get irritated at us and maybe vice versa, and I think we had better not veto each other.

Senator ROBERTSON. You may proceed.

Mr. GIDNEY. The national banks receive no similar benefit. All national banks in the continental United States are members of the Federal Reserve System and are insured by the Federal Deposit Insurance Corporation. All of the funds of the Federal Deposit Insurance Corporation are derived from insurance assessments on insured banks, including national banks, and the latter have paid in approximately 50 percent of the existing Federal deposit insurance fund. Thus national banks through their payments to the Federal Deposit Insurance Corporation are paying part of the cost of examining State banks. This inequity should be eliminated.

In a majority of the States the examination fees are very much less for State banks than for national banks, particularly in the case of larger banks.

Through the payments suggested in the proposed amendment, the examination fees assessed to the national banks by the Comptroller of the Currency should be reduced, thus restoring a more equitable balance between the State and National systems.

What it amounts to is that the Federal Reserve and the FDIC are spending an estimated amount of $8 million. That is about what ours costs, not too far different, so that the Federal Government, in effect, is subsidizing the State-chartered banks to pretty nearly that amount.

Now we have a dual-banking system, and it doesn't seem right that the one side of it should be subsidized whether it is our side or the others, but our side is not. Our side is paying fully, and the other people are getting examinations for free.

Now we come to one that we put in that is controversial which the advisory committee did not accept and which will be bitterly opposed by many people. For that reason you may not wish to carry it into the bill.

In our original recommendations in connection with the banking law study we recommended (No. 45) that a national bank should be permitted to acquire by consolidation, merger, or purchase of assets and assumption of liabilities, another national bank located in the same county, which is found by the Comptroller of the Currency to be in a precarious financial condition, and to continue the office or offices of the absorbed bank as branches, regardless of the branch banking laws of the State in which the banks are located. We continue to believe that this proposal has great merit and we urge that it be given serious consideration by the committee. As we stated in testimony before the committee last November we believe that enactment of this proposal would be in the best interests of the depositors and borrowers of such banks and substantially ease the problem of the Comptroller of the Currency in the case of banks which would otherwise have to be closed and liquidated. Any legislation enacted could and should contain adequate safeguards so that there could be no abuse of its provisions. We recommend that such authority be used only when it has been found by the Comptroller of the Currency that insolvency of the acquired bank is imminent, and when the Comptroller of the Currency has been advised in writing by the Federal Deposit Insurance Corporation that the proposed acquisition and the establishment of the branch or branches by the acquiring bank is in its opinion in the public interest. Thus two agencies, the Comptroller of the Currency and the Federal Deposit Insurance Corporation, would have to agree that the takeover and the establishment of the branch or branches would be necessary and desirable in the public interest.

We conceive it is our duty to let you know if conditions are building up which could make trouble in the future.

The national banking system was built up to give the people of the United States a safer and more reliable banking system, and we are certain we have certain hazards along this line which we think need to be recognized.

Of course, 35 States have laws which probably permit this already, so it is about 13 States that would be affected.

I just noted on the personnel of the subcommittee today that there are Senators representing two States which do not have the power which this would convey.

We recognize it is highly controversial. We know many of our friends feel very strongly against it, but I think we have to speak our piece and tell you that there is a problem.

Senator ROBERTSON. The Senator from Ohio would like to ask a question.

Senator LAUSCHE. Mr. Gidney, what becomes of a situation in the event you do have an insolvent national bank and another national bank is not allowed to take it over?

Mr. GIDNEY. They could take it over and put the two offices together, but they couldn't take it over and keep the office—

Senator LAUSCHE. And keep the branch.

Now if it decides that it does not want to take it over by merging the offices, and it is not allowed to maintain a branch, what is the likelihood of the consequence?

Mr. GIDNEY. Well, I think under the assumed conditions we would have the bank closed and the Federal Deposit Insurance would pay off deposits.

Senator LAUSCHE. What you are aiming to do is make certain that that condition would not arise and that the existing bank would be permitted to take it over and maintain a branch?

Mr. GIDNEY. That is right. In maintaining banking service, of course. It doesn't arise in Ohio because the Ohio law covers the county.

Senator MONRONEY. Mr. Chairman, we happen to be a State, as you probably know, where no branch banking is allowed, period.

Mr. GIDNEY. I know that.

Senator MONRONEY. My bankers are very frightened that this would put a premium on a small national bank becoming in a precarious position where it would be worth more for it to be the only branch bank allowed in the State of Oklahoma, to have it in that condition and be able to sell it.

We are very fearful—our people are—that this is the opening wedge of branch banking in the State of Oklahoma.

Mr. GIDNEY. It would be a creeper, that is true, although we hadn't thought about those who become willfully in trouble.

Senator MONRONEY. It doesn't have to be bankrupt. It just has to be in some sort of a precarious situation.

Mr. GIDNEY. We are perfectly willing to have safeguards thrown around that so that it isn't just the Comptroller who is saying it is precarious, that the FDIC has an interest, and we would be willing to have a pretty realistic case because that is all we are asking for now.

Senator MONRONEY. But, as a matter of fact, you have had no case that I know of where a bank gets in trouble in a city, finds some other bank ready, willing, and able to take it over, assume a liability, take out the paper and get the FDIC out with practically no loss at all unless there has been an inside robbery, or something?

Mr. GIDNEY. We have not been in a very bad situation. We have been in good times with a modest number of troubles occurring and those which have occurred have been pretty much due to defalcations. There, of course, some of them have had to close; and the Chicago situation, either 1 of those 2 that have been troublesome, might well have been taken over could they have been carried as branches. I am sure they would have been reached for. I don't think they got in trouble willfully; I am not certain.

Senator MONRONEY. There is no time limit in this. I mean, in other words, the banks are merged in perpetuity. You have two banks in open violation of what the State law says.

Mr. GIDNEY. That is one of the objections.

Senator MONRONEY. I would have no objection if you would not allow it in States excepting the States that permit branch banks.

Mr. GIDNEY. There we don't have to ask for it because we have it.

Senator MONRONEY. What is the necessity in the rest of those same States? Surely if the bankers felt it was necessary they would not be protesting.

Mr. GIDNEY. I think the bankers are going ahead with sublime confidence that might not be warranted a little later, some time later.

At the other hearings, Senator Douglas said he hoped I was not a Cassandra. I agreed with him on that. I just brought down in case he should ask me the question again a little book describing events in Iowa in the middle 1920's called Grief, which was widespread over thatMidwest section. I don't believe that we can be sure that grief is banished forever.

Senator MONRONEY. I don't see why it would be necessary if a national bank took over another national bank to run two establishments. It might be if the city was of a tremendously good size.

Mr. GIDNEY. I think the willingness to take one over becomes very much greater, that is true, and you have several takers, probably, if you go to one of your larger Oklahoma cities—for instance, Tulsa or Oklahoma City—you would have several competitors for it. Whereas if they couldn't take it over, they would judge it purely on the assets, and if it was a pretty sick-looking proposition, they would say, "We are not interested."

Mr. JENNINGS. I think there is another point that should be made, and that is it is highly questionable that we would ever use this in a 2-bank town because in a 2-bank town normally it is not necessary, if one bank is taking over the other, to run a branch office.

Mr. GIDNEY. That is right.

Mr. JENNINGS. But it is in larger cities where there are many smaller banks out in suburban areas. The larger banks might have to stand by and watch many of the smaller banks close up because they could not assist by taking over some of them and continuing them as branches. Unless they could continue them as branches they would not wish to bring this business 5 or 6 miles into the downtown part of the city.

Mr. GIDNEY. You think an examiner is tough on a bank, but he isn't nearly so tough as another bank when they are asked to give help. You really see something tough then.

Senator ROBERTSON. You may proceed.

Mr. GIDNEY. Now we come to another recommendation in which our ideas were not shared by the advisory commitee, and we are very much surprised they are not. That is pension and profit-sharing accounts of national banks.

We continue to believe that it is desirable that there be basic statutory regulation of the more important aspects of retirement or pension and profit-sharing accounts established by national banks. A small number of abuses have occurred.

I have two very definitely in mind which I could cite—profit-sharing accounts.

Pension and profit-sharing accounts are continuing to grow, and it is likely that further abuses will occur. The Comptroller is without legal authority to intervene. As a basic requirement legislation should provide for the establishment of such accounts, require that the approval of shareholders be obtained—we usually are able to get that by moral suasion—set forth the manner in which they are to be managed and records maintained, and should impose limitations on their borrowing and permissible investments, particularly investments involving "own" bank stock and the stock of competing banks.

Senator LAUSCHE. Mr. Gidney, would you mind giving me a bit of background for those two cases you have in mind?

Mr. GIDNEY. Well, it is a little bank in a large State which set up a profit-sharing affair and put money into it and purchased a large amount of their own stock and some oil leases and things of that kind and then went to a large correspondent bank and borrowed a large amount of money to help carry those and also enough to go and buy a small State bank at some little distance.

We have no authority over that. We have scolded them as vigorously as we could and are continuing to try to get them to see things right.

Then right at the present moment there is in the State courts of Michigan the purchase of a bank in Port Huron, Mich., by the profit-sharing funds of the Michigan National Bank at Lansing. The attorney general of Michigan has come into the action with a very vigorous criticism of the action. We have no authority to even look over the profit-sharing plan, still less to control what is done with it; and in this particular case I think they have brought about at least very severe embarrassment by its use.

What the result of that court action will be, I don't know, and, of course, it also has some Clayton Act and antitrust implications.

Those are two that we have in mind. There are not too many. We fortunately haven't too many.

Senator MONRONEY. This is the investment of the bank of its employees' profit-sharing funds or pension funds?

Mr. GIDNEY. Yes. The bank itself could not have bought that stock, but they used the profit-sharing money and we don't think that is a very healthful development.

Senator BENNETT. Does that evade a law against branching? Does Michigan permit branching?

Mr. GIDNEY. Yes, I think you could say that it avoided it.

Senator BENNETT. It could in a State where branches were not permitted if that sort of thing were permitted to continue.

Mr. GIDNEY. This first case I cited was the great State of Texas where they bought this other bank where they are very definitely against branches. It isn't an important enough case to be very much excited about as a branch proposition because one small bank having another one up here isn't going to be very upsetting as a branch proposition, but it isn't a right transaction.

Senator BENNETT. It does point the way over a good many years to an invasion of that particular law?

Mr. GIDNEY. We think that the pension and profit-sharing plans are so good for national banks that we ought to channel them into the right lines and we would like some help to do that.

Senator LAUSCHE. Don't the profit-sharing plans contain provisos under which permission must be obtained of those who are the beneficiaries of the fund before it can be invested?

Mr. GIDNEY. I don't think so. I think it is an unconditional authority that is given. There may be variations in that. There may be variations in that.

Senator LAUSCHE. You are trying to reach those instances where there is no limit on what the bank may do with the money that has been entrusted to it?

Mr. GIDNEY. We would like to look at it. I think we should have a look at it and, too, I think there should be some ground rules laid out. I don't care about having those too restrictive. I think I have liberalized a little in the process of our thinking. I think Mr. Jennings has.

We don't know what the limitations should be, and I think they might be fairly liberal, and I think they could conduce to the welfare of the banks if they are well handled, very much so, to give proper rewards to the employees and make them a happy family, and so we still stick to this, even though we didn't get encouragement from the folks who should have welcomed it.

Senator ROBERTSON. Isn't it a fact, though, that the Treasury Department, the Bureau of Internal Revenue, has to approve all welfare funds? Unless they were set up in a bona fide way personally with management, they won't approve them as a tax deduction?

Mr. GIDNEY. That is correct.

I visited a bank the other day which is somewhat restricted in its functioning and, therefore, they do not seek the tax deduction. They are willing in their case to go ahead without the tax advantage so that they can do it the way they want. I think it is well run.

So we said here that the advisory committee thought they should wait for the Senate Labor and Public Welfare Committee to come out with its study and get legislation, and we think it would be well to be done for banks by the Banking and Currency Committee and not wait for the others.

Senator ROBERTSON. You have noticed that the advisory committee didn't accept all of your recommendation?

Mr. GIDNEY. Oh, yes.

Senator ROBERTSON. And you have noticed that I didn't accept all the advisory committee's recommendations?

Mr. GIDNEY. Frankly, Senator, I think we have all done pretty well. We are not scolding a bit.

Senator ROBERTSON. You said as much in your opening statement.

Mr. GIDNEY. Yes, and I repeat it.

Senator ROBERTSON. We appreciated that, and I assume from that that you mean you want to see action completed on this proposal.

Mr. GIDNEY. Oh, yes. I recognize your problems on it, that we have to have a bill to get through.

Senator ROBERTSON. You want to help us make it a little better.

Mr. GIDNEY. We would like to improve little places and get things if we can.

Senator ROBERTSON. Thank you, sir.

Mr. GIDNEY. With respect to this matter the advisory committee in its report pointed out that during the last Congress a subcommittee of the Senate Labor and Public Welfare Committee made a study of the need for additional Federal legislation with respect to the establishment and regulation of employee-benefit plans generally, and stated that since it seems reasonably clear that similar legislation will be pressed during this Congress, that it would seem to be premature for this recommendation of ours to be considered. We recognize that the problem of employee-benefit plans is not confined to national banks. However, we should like to point out that in the case of most such plans established by corporations a separate trustee is involved whereas in the case of banks the plan which is created by the bank may also be administered by the bank as a trustee. Under these circumstances the investment provisions may tend to be broader and to give greater freedom to the trustee than might otherwise be the case. Furthermore, since the bank itself or individuals selected and presumably controlled by the directors are in many cases trustee of an account for the benefit of the bank's own employees there is greater possibility of problems arising than if there were an entirely separate trustee. In a few cases funds of this type of trust have been used by banks to acquire their own stock beyond reasonable limits or acquire the stock of competitive banks or for other purposes more to the benefit of the bank than to the benefit of the bank's employees. We believe that legislation which would give the Comptroller some control over these matters is essential and it should not wait for consideration by the Congress of employee benefit plans generally in which other problems than those peculiar to banks would be uppermost. Furthermore, we should like to point out to this committee that the legislation proposed by the Senate Labor Committee would not have provided for the regulation of these plans but merely for the gathering of information so that it may be several years before there is any effective Federal legislation in this field.

For these reasons we strongly recommend that the committee give consideration to our original recommendation.

We shall turn now to title II, the Federal Reserve Act.

Mr. ROGERS. Mr. Gidney, before you leave the National Bank Act, are you familiar with the proposal that Mr. Cravens made concerning an institution holding itself out as a bank which is not a bank?

Mr. GIDNEY. Yes, I have a copy of his suggestion here.

Mr. ROGERS. I wonder if we could have your recommendations on it?

Mr. GIDNEY. I think his prohibition was against anyone other than an institution receiving deposits and making loans. Just on a quick look, I don't think that would be effective to meet what he is after.

I think Senator Lausche will confirm that in Ohio a savings and loan association can take deposits, according to my recollection, so that a savings and loan association in Ohio could call itself a bank, and our suggestion would be in effect that you might catch this by providing that no one should call themselves a bank except a corporation that is chartered by the Federal or State authorities as a bank, trust company, or savings bank, and then let the other people be operated as they are.

Mr. ROGERS. Thank you.

Mr. GIDNEY. I am for his proposal. I feel that I could wriggle around that if I were the fellow trying to do it.

Senator ROBERTSON. There is one other more or less lone issue that is neither National Banking Act nor Federal Reserve Act, and that is action that I took in putting in this tentative bill—the bill introduced last year on the House side by Chairman Spence to regulate saving and loan holding companies.

So far, we haven't had a single witness that endorsed that proposal. We had one witness here from California that said he is the only one to be affected, and he didn't see the necessity, as he was a small one, and if we were going to act on them we certainly ought to have some hearings, and since then I have learned that Mr. Spence has introduced a new bill—a different bill from the one we had last year.

Do you think we should under those circumstances take that provision out of the bill, or are you interested in having some other——

Mr. GIDNEY. Well, I have been pretty much trying to stick to my own field here.

Senator ROBERTSON. I know, but I asked you when you came here to be prepared to testify on what everybody said.

Mr. GIDNEY. I am sympathetic.

Senator ROBERTSON. You are one of our experts, you know, and we want to benefit by your advice.

Mr. GIDNEY. I am not so expert in that field. I am sympathetic on the idea of having restrictions on holding companies in savings and loan because about a year or two ago when they formed the first one I know of in California, and a reading of the prospectus made me think that it was the type of thing that might well have been subjected to supervision.

Senator ROBERTSON. I believe, Senator Bennett, you have in your State a bank holding company that owns savings and loan associations?

Senator BENNETT. That is right. It is an interesting twist in the old contest between the banks and the savings and loan, but apparently the bank holding company is determined to hang on to it, will try to defend itself against any attempt on the part of supervisory agencies to require divestment of that particular subsidiary.

Mr. GIDNEY. Nevertheless, I think in that case that being definitely a bank-holding company that the Reserve Board will have jurisdiction.

Senator BENNETT. That is right.

Mr. GIDNEY. And I suppose can require divestment if they conclude that is what should be done. I suppose that is the case.

Senator BENNETT. Of course, what the chairman is talking about is a different situation in which holding companies are originated primarily to hold savings and loan associations and not banks.

Mr. GIDNEY. That is right.

The CHAIRMAN. You may proceed with your discussion of the Federal Reserve Act.

Mr. GIDNEY. Now this is in the matter of section 28 (e), placing limitations on loans which may be made to executive officers of member banks.

We notice that during these hearings there have been differences of opinion as to whether the term "executive officer" should be defined in the statute or whether the power to define this term by regulation should be continued in the Board of Governors of the Federal Reserve System. We favor continuing the authority to define this term by regulation in the Board.

Senator ROBERTSON. That is the way it is in the bill; isn't it?

Mr. GIDNEY. Yes; I think some others testified they would like to have it changed.

Senator ROBERTSON. You stay with the bill on that?

Mr. GIDNEY. That is right.

Voting permits of holding company affiliates: This is the use of the reserve fund required by section 33 (b) (3) to make additions to capital of their bank affiliates as well as replacement of the capital.

The reserve fund required by this section has always been regarded as an emergency fund to be used for replacement of capital when necessary and we believe it would be undesirable to make the proposed change and to permit this fund to be depleted for the purpose of making normal additions to the capital of the banks. This might result in the reserve fund being inadequate to replace capital at a time when such replacement was essential.

I think we are with the terms of the proposed act as it is written.

Senator ROBERTSON. There was one provision of your earlier statement which I think you put in the record and I missed. The reason I am going to ask you about it is because I think some Members of Congress will be interested in it.

We had a recommendation—or is it in the present law?

Mr. ROGERS. It is a recommendation.

Senator ROBERTSON. A recommendation that officers and those who own as much as 10 percent of stock of banks should not be permitted to make a political contribution.

Mr. GIDNEY. We recommend against such limitations.

Senator ROBERTSON. You recommend against it. I just wanted to emphasize that fact.

Mr. GIDNEY. We don't like to see rights of citizenship disappear.

Senator ROBERTSON. You see, I have some Virginia friends I wanted to hear your testimony on that, sir.

Mr. GIDNEY. Yes, sir. We think that rights of citizenship should be retained by bankers and by bank examiners, even.

Senator ROBERTSON. It is just a right of a citizenship that all other officials of corporations have, and——

Mr. GIDNEY. Exactly.

Senator ROBERTSON. And at any particular point to single out a bank as being very vicious in politics and say they should not contribute or have any say-so——

Mr. GIDNEY. We strongly feel that way.

Senator ROBERTSON. You may proceed with your Federal Reserve testimony.

Mr. GIDNEY. This was on using the special reserve funds of holding companies. We think that should be held for the emergency necessitous proposition. They could use other funds if they have them for the day-to-day maintenance.

Mr. ROGERS. Is your primary objection that it would deplete the reserve fund?

Mr. GIDNEY. Well, we think the required reserve fund was set up for the day the bank is in trouble and you look for the top company to fix it up. Therefore, if that is the case, that is the right purpose. We ought to stick to that.

Mr. ROGERS. If you had the other 12 percent reserve fund and it would conceivably be wise to make use of that where they needed it for capital purposes, they still have to refill that fund?

Mr. GIDNEY. Yes, they might have to refill it.

Senator LAUSCHE. Does the bill provide that they would have to rebuild that fund?

Mr. ROGERS. Well, the law provides they have to retain the 12 percent reserve so when it goes down below that figure they have to put money in and fill it back up again.

Senator LAUSCHE. How do you reconcile your two positions?

Mr. JENNINGS. If the reserve fund, emergency fund, were used when a particular bank or banks of the holding company became somewhat undercapitalized but the banks were nevertheless in a sound condition, before they would have an oportunity to build the reserve fund back up again from earnings some of their banks might find themselves in serious trouble and the reserve fund would not be there. Under such circumstances it might be very difficult for the holding company to go out and raise additional capital by the sale of new stock. Therefore, we think during normal times the holding company should be able to recapitalize its banks through usual methods, holding the 12 percent reserve against the evil day when they might not be able to go out to the market and raise additional capital to put into bad situations.

Mr. GIDNEY. There is one large holding company in Ohio, and it might mean in order to get things up to an ideal basis we would spread that out. If we were allowed to do it freely, it might be spread out over the whole 27, or whatever it is. Then let us suppose 1 or 2 of them get into acute trouble. That has gone out. In other words, we hold it back a little bit to flow to the point of acute need.

Mr. Jennings is stronger on this matter than I am, but I have gone along with him on it, and that is the way we feel.

Mr. ROGERS. Along that line of thought then, I think we should take out the provision in the law that it is used for replacement of capital.

Mr. JENNINGS. Of course, it is replacement in an acute situation.

Mr. ROGERS. Thank you.

Mr. GIDNEY. O. K., we are not fighting mad on this one.

Now, let us see, I think that brings us to title III of the Federal Deposit Insurance Act.

SECTION 6. MANAGEMENT OF THE CORPORATION

The Federal Deposit Insurance Act would eliminate the Board of Directors of the Federal Deposit Insurance Corporation and would place the management of that Corporation in the hands of a single Administrator who would be given the power to appoint a Deputy Administrator. The act would also provide for the creation of an advisory board to consist of the Comptroller of the Currency, the Chairman of the Board of Governors of the Federal Reserve System, or his designee, and a State officer exercising functions relating to the supervision of State banks. Apparently this advisory board would have no duties except to consult with the Administrator at his request, but not less frequently than 4 times each year, and to make recommendations to the Administrator relative to the carrying out of his duties. The Administrator would be free to accept or reject the advice of the advisory board. We would doubt the wisdom of including in this legislation this change in the management of the Federal Deposit Insurance Corporations. A matter of such importance should, we think, be given more extended study before enactment into law.

In view of the fact that the Financial Institutions Act of 1957 deals primarily with operating matters, we suggest that it should not include a change in the management of the Corporation but that consideration of this matter should be left for the proposed National Monetary Commission to examine more fully.

If serious consideration is to be given by the committee to establishing a single Administrator for the Corporation, we deem it imperative that he be placed under the general supervision of a Cabinet office, which it is presumed would be the Secretary of the Treasury. The insurance fund of the Federal Deposit Insurance Corporation is presently in excess of $1½ billion, and the Corporation has a call upon the Treasury for loans in an amount up to $3 billion. We do not believe any single Administrator should be given unsupervised power or control over and responsibility for such a large sum.

Senator ROBERTSON. You realize the proposal in the tentative bill grew out of the scandals in the summer by a one-man board, and you think it would be better since we are not going generally into policy matters to defer that and let the new Monetary Commission consider that and submit a recommendation?

Mr. GIDNEY. That is exactly the recommendation I have, sir.

Senator ROBERTSON. Well now, what would you think about a three-man board without having you on it?

Mr. GIDNEY. I don't think that would be best. I don't covet being on it, but I don't think you want to take anything away from that board that is good, and I think the Comptroller, whether it is the previous one or the next one, will be good.

Senator ROBERTSON. My question wasn't very fairly phrased.

You think it is best for the Comptroller to be an ex officio member of this board?

Mr. GIDNEY. I think great advantages come from that, and if I had just the—what do we say? my druthers—if I just do it by edict, which I can't, you would add 2 men to the board, 1 from the Federal Reserve and 1 perhaps from the State people.

Senator LAUSCHE. Making it five?

Mr. GIDNEY. Make it five.

Senator LAUSCHE. Instead of reducing it to one?

Mr. GIDNEY. Instead of reducing it to one—if I were fixing it up.

Senator ROBERTSON. I think the witness of the Federal Reserve Board last November said if you want the largest area of considered judgment you would have a five-man board.

Mr. GIDNEY. Yes.

Senator ROBERTSON. I think Governor Robertson recommended that, and perhaps he did include a member of the Federal Reserve Board, the Comptroller, and one State official engaged in banking and the other 2 the full-time members.

Mr. GIDNEY. I think if we had the three-man board not tied in to either the Federal Reserve or ourselves, you have the inevitable tendency to build up a separate empire and to fight off the outside.

Now in the almost 4 years I have been here, we have had very good relationships back and forth between the FDIC and our office and the Federal Reserve and the interrelationships in all directions there have been good, and they ought to be kept that way.

A three-man board completely separated becomes a separate principality with all the tendencies to build its field, enlarge it, and so forth.

I think you would get a very good result if you added a representative of the board and a representative supervisor appointed by the President.

Senator ROBERTSON. And you think that putting a reserve of a billion dollars and a joint account of the Treasury of 3 billion more is just a little too much for 1 man to have under his supervision?

Mr. GIDNEY. That is just what I think. The last figure I saw was just too much. I think a straightforward and proper person wouldn't want to be loaded with that much and an improper person shouldn't have it.

The Treasury is interested because they have a call on them for 3 billion there, so if there is ever to be a single administrator he should be placed over in the Treasury Department.

Senator ROBERTSON. Let them watch him?

Mr. GIDNEY. Yes. They let me have a great deal of leeway, but they are all there.

Senator ROBERTSON. You may proceed.

Mr. GIDNEY. We come to the assessment rate and assessment credits.

We have noticed that repeatedly throughout these hearings the question of assessments by the Federal Deposit Insurance Corporation has been raised with some suggestions that a study should be made. We concur in the desirability of a study to determine—that is a great American custom—whether a more scientific basis for levy of assessments is possible.

We believe, however, that no change should be made in current assessment rates until such a study has been completed. Furthermore, we believe that a study should not be forced to completion by a statute limiting the study period to 1 year as has been suggested in these hearings. It should be sufficient for the committee to request that the results of the study be presented to the Senate Banking and Currency Committee within 1 year.

Now I notice in some of the testimony some things that disquieted me quite a lot, and that was the suggestion that the FDIC could take care of losses of a normal nature just coming along in a normal situation, but if it is a really big trouble, why, somebody thought they could not take care of it. That hasn't been my conception of it. That is not the conception of the board of members of that FDIC. That isn't the public's conception. I think the public believes we have an insurance plan to take care of whatever comes.

Senator ROBERTSON. I am sure the public believes when you say an account is guaranteed to $10,000, as long as there is any Government left, they are going to get the $10,000. That is what they think.

Mr. GIDNEY. I am sure of it. I believe that is what Congress intended, but some of our folks, two of them, at least, threw in that idea, and I just didn't want to——

Senator ROBERTSON. They were assuming suppose we get bombed and a lot of these billion-dollar banks get blown up; then we won't pay. That is the idea.

Mr. GIDNEY. Well, I don't know just how large the difficulty might be, but I think our job is to head off troubles like those of the early thirties, and we need a large fund and we need to handle it well to do that. I don't think we should——

Senator ROBERTSON. So your idea is that we should proceed on the assumption, first, that we are not going to have everybody get into smithers in an atomic war but there could be a depression which should make it tough for a lot of banks and if that should come the Government has a legal and moral obligation to pay off all depositors up to $10,000 and you ought to figure on a reserve enough to do it.

Mr. GIDNEY. Certainly the Corporation has that obligation. The Corporation has that obligation, and the Corporation to meet that day has $1,742 million in its fund and a call on the Treasury for $3 billion or $4,742 million.

Senator ROBERTSON. In framing this tentative bill, I took the position that I didn't know what the demands would be, but I was willing to have it studied for a year.

Mr. GIDNEY. Oh, yes.

Senator ROBERTSON. And that is what we plan to do.

Mr. GIDNEY. But I did want to put in a disclaimer on that.

Senator ROBERTSON. A lot said, "Oh, no, you have more funds than you will ever need. Let's cut the assessment right now." You don't agree with that?

Mr. GIDNEY. As a director, I am not ready to cut it further. It has been cut once, so they are now paying about 40 percent of what they originally paid.

Senator LAUSCHE. Senator Robertson, I think there has been developed a tendency throughout the whole economy to ask for reduction in rates which are contributed for the purpose of maintaining a fund to take care of disasters. Manufacturers are wanting to reduce rates in the workmen's compensation law, in the unemployment compensation law, and in every instance they argue that the prosperity is the basis under which the cuts should be made. They are unwilling, however, to recognize the plight in which we find ourselves when the disaster comes.

Mr. GIDNEY. That is right.

Senator LAUSCHE. Regretfully in Ohio, contrary to my fight—rebates were made in the unemployment compensation fund on the basis that the fund is adequate, never shall we encounter disaster of such gravity that the fund would not meet it; and if we are to err, the error ought to be in the direction of the fund being too large, rather than too small.

Mr. GIDNEY. That is what I believe.

Senator LAUSCHE. With respect to your statement that the Corporation will have to pay, from my understanding the public thinks that the Federal Government is guaranteeing their deposit.

Mr. GIDNEY. I think that is true too. I think some of the idea might be a little like the gentleman down in a certain State who couldn't repair his roof when it was raining because it was inconvenient and when it wasn't raining he didn't need to.

Now we come to the big merger act, section 23.

Senator ROBERTSON. Off the record.

(Discussion off the record.)

SECTION 23. MERGERS AND CONSOLIDATIONS

Mr. GIDNEY. Section 23 of the Federal Deposit Insurance Act is identical with S. 3911 of the 84th Congress which was fully considered by the Senate Banking and Currency Committee, and approved by the Senate in July 1956. This section would require the approval of 1 of the 3 Federal bank supervisory agencies for all bank mergers in which either of the banks involved is an insured bank and would require that consideration be given to the competitive aspects of such mergers as well as highly important banking factors.

Other legislation has been introduced in the Congress which would amend section 7 of the Clayton Act to prohibit bank mergers by means of acquisition of assets when the effect of such acquisition of assets may be substantially to lessen competition or to tend to create a monopoly.

We strongly favor the provisions of section 23 of the committee print bill and urge that it be enacted in lieu of legislation which would make bank asset acquisitions subject to the provisions of the Clayton Act.

This Department considers it essential to weight and adequately consider the always important and frequently vital banking factors in conjunction with purely competitive factors so as to arrive at fair and well-balanced decisions in approving or denying bank mergers. Legislation which would make the Clayton Act applicable to bank asset acquisitions would place jurisdiction in the Department of Justice rather than the Federal bank supervisory agencies and would legally require the denial of bank mergers solely on competitive grounds.

Banking has unique safeguards against monopoly or inadequate competition which are not present in industry or trade. Banks may not establish offices across State lines. Their operations within individual States are either limited to one head office (in nonbranch bank States, such as Illinois, Texas, Florida, etc.) or to the establishment of branch offices within the State where the bank's head office is located as may be approved by the bank supervisory authorities within areas defined in State statutes authorizing branch banking. A majority of the branch bank States restrict such activities to county limits, but some States permit it on a trade area basis, a contiguous county basis, or on a statewide basis. Obviously, the concentration of commercial bank assets within such geographical limitations can never pose problems of an antitrust nature that even approach in seriousness those with which the Justice Department has long been confronted in industry or trade.

We consider it essential to place jurisdiction over bank mergers in the Federal bank supervisory agencies because they are best suited to consider the broad monetary and banking questions and economic and financial development problems which surround a decision on the relative competitive factors involved in a decision as to whether a bank should or should not be merged.

Banking is a closely regulated industry and we believe its regulation should be continued in the hands of the Federal bank supervisory agencies rather than to place one phase of its regulation under the jurisdiction of another Government department.

We sincerely believe the status of competition in banking today is at a very high level and that the public interest in this respect is being well served. We believe that the enactment of section 23 will insure, beyond all doubt, a continuance of this status.

SECTION 26. PAYMENT OF INTEREST

Under present statutes prohibiting the payment of interest on demand deposits, the Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation have taken differing positions with respect to absorption of exchange charges. In its recommendation No. 77 the Board pointed out that this has resulted in placing member banks at a serious competitive disadvantages in some sections of the country, and recommended that Congress should by legislation either explicity state that absorption of exchange charges constitutes the payment of interest or give to the Board or the Federal Deposit Insurance Corporation the power to define "interest" for both classes of banks—put it in one place. National banks in the continental United States are member banks in the Federal Reserve System and find themselves at the same competitive disadvantage with respect to insured nonmember banks as do other member banks, of the Federal Reserve System. We think that under the proposed act the question of whether absorption of exchange charges shall be deemed to be interest is left undecided.

For this reason, we recommend that section 41 of the Federal Reserve Act, and section 26 of the Federal Deposit Insuranse Act, both prohibiting the payment of interest on demand deposits, should contain express prohibitions against the absorption of exchange charges by members and by insured banks respectively.

Senator ROBERTSON. That was the final recommendation of our advisory committee. They said that in planning the bill to write the same definition of interest in the FDIC statute as we previously had in the Federal Reserve Act still left them in doubt, and they thought if we really wanted to come to grips on it, it would be far better just to put it in better language.

Mr. GIDNEY. Call a spade a spade.

Senator ROBERTSON. No insured bank can absorb exchange—period. Incidentally, do you know how many banks in Virginia are nonpar?

Mr. GIDNEY. Only 2 or 3—maybe none at all.

Senator ROBERTSON. I think it is only one. I am rather proud of that.

Mr. GIDNEY. I am, too, sir. When I was in charge of the Federal Reserve Bank of Cleveland, there wasn't one in the entire district.

Senator ROBERTSON. Mr. Jennings has a list. We have got a good many letters from Minnesota, we are getting some from North Carolina, some from South Carolina and Louisiana. Would you supplement your statement by putting Mr. Jennings' list in.

Mr. JENNINGS. My list, Senator, is by States, and has the number of nonpar banks in the States and the number of branches operated by those banks. There are 1,748 nonpar banks in the country, and they operate 318 branches, so there is a total of 2,066 offices that are nonpar at the present time.

Mr. GIDNEY. That represents about 2 percent of the deposits of the banks of the country. And a good part of the deposit volume is grouped in a small number of banks in this list.

Senator ROBERTSON. Without objection, that statement will be filed with your testimony.

(The list referred to follows:)

Number of commercial banks (nonmember) and branches, by States, on Federal Reserve nonpar list, June 30, 1956

State	Banks	Branches and offices
Alabama	94	1
Arkansas	113	19
Florida	47	1
Georgia	281	2
Illinois	2	
Kansas	2	
Louisiana	106	25
Minnesota	405	
Mississippi	148	63
Missouri	58	
North Carolina	91	142
North Dakota	97	18
Oklahoma	6	
South Carolina	75	7
South Dakota	99	25
Tennessee	81	15
Texas	41	
Virginia	1	
West Virginia	1	
Total	1,748	318
Grand total	2.066	

Mr. GIDNEY. We have covered the ones I had written up. Then we had appendix A. These are matters we are agreeing with the bill as it is drawn. And appendix B is slight technical changes.

Senator ROBERTSON. I don't think it will be necessary to explain in detail the things with which you agree. And of course there is no use mentioning the obsolete sections that everyone says should be repealed.

(Appendix A follows:)

APPENDIX A

Sections of title I, the National Bank Act, upon which we have not commented otherwise, but which we favor.

Section

1. Short title
2. Office of Comptroller of the Currency
4. Appointment of Comptroller
5. Deputy Comptrollers
6. Chief national bank examiner
7. Employees and salaries
9. Seal
10. Office facilities
11. Annual report
13. Organization certificate
14. Commencement of business
15. Capital
17. Payment of bank of deficiency in capital stock
18. Increase in capital stock
24. Shareholders' liability
25. Number of directors
28. Oath of directors
30. Liability of directors
33. Trust powers
37. Limit on bank's indebtedness
38. Holding of real estate
40. Change of name or location
41. Dealing with own stock
42. Depositaries and financial agents
43. Investment in bank premises
45. Acting as insurance agent or broker

46. Acts in contemplation of insolvency
47. General provision for amending articles
48. Examinations of banks
51. State examination or license prohibited
56. Conversion of State banks
58. Voluntary dissolution
60. Distribution of assets
61. Winding up business of bank
62. Resumption of business
63. Purchase of bank property
66. Ratification of certain acts
67. Taxation of national bank shares
68. Lawful reserves in Territories and possessions
69. Venue of actions
70. Territorial applicability of act

(Appendix B follows:)

Appendix B

Sections in which it is recommended that changes of a minor or technical nature be made.

Title I. National Bank Act

Section 2. Definitions

Subsection (b) should be amended by inserting the words "or doing a fiduciary business" immediately after the word "deposits." This will eliminate any question as to whether a trust company which does not receive deposits may merge or consolidate with a national bank.

Section 16. Capital stock

We recommend that the reference contained in section 16 (c) to June 16, 1934, be eliminated. Formerly national banks were permitted to invest up to 100 percent of their capital in corporations engaged on June 16, 1934, in holding the bank premises. However, by Public Law 460 of the 83d Congress the law was amended to permit national banks to invest up to 100 percent of their capital in the stock of corporations engaged in holding the bank premises without regard to whether such corporations had been so engaged on June 16, 1934. At the time of that amendment references to June 16, 1934, in this statute should have been eliminated.

Section 19. Decrease in capital stock

In section 19 the words "the holders of" should be inserted just before the words "at least" in the latter part of the section.

Section 22. Dividends

In the second sentence of subsection (d) of this section there should be inserted a comma after the word "capital" in order to make the meaning clear.

Section 26. Election of directors

In section 26 (c) (4) reference is made to holding company affiliates of national banks. In this connection reference should be made to the definition of holding company affiliate contained in section 31 of the Federal Reserve Act. In this same section the acting as proxy of any officer, clerk, teller or bookkeeper is prohibited. It is suggested that in lieu of the words "officer, clerk, teller, or bookkeeper" there should be inserted the words "director, officer, employee or attorney." This would conform the statutory language to the language contained in the standard form of bylaws recommended by the Comptroller to national banks.

Section 27. Qualifications of directors.

In section 27 the word "par" should be substituted for the word "part" in the second sentence, and the word "office" should be substituted for the word "place" at the end of the section.

Section 29. Removal of officers and directors

In the first sentence of section 29 commas should be inserted after the words "national bank" and "District of Columbia" in orders to make the meaning clear.

Section 31. Corporate powers

In view of the fact that some national banks have foreign branches established in accordance with provisions contained in the Federal Reserve Act, section 31 (b) should be amended by adding the words "or the Federal Reserve Act" at the end thereof.

Section 39. Branch offices

With reference to section 39, that portion of subsection (a) which relates to branches continuously maintained and operated for a period of more than 25 years preceding the approval of the act should be eliminated. This provision was originally enacted in 1927 and was designed to permit national banks to retain in operation branches which they had operated for 25 years prior to 1927. Any such existing branches which were made lawful by this provision of the 1927 act are in lawful operation and may be legally retained under the first part of subsection (a). Therefore, there is no longer any need for the second portion of this section, and it is recommended that all after the comma be deleted.

Section 44. Engaging in the securities business

In section 44 the comma after the word "obligations" in the last line of subsection (a) (1) should be deleted, and the word "on" should be substituted for the word "or."

Section 49. Expenses of examinations

The reference in section 49 (c) to section 50 (b) should actually be a reference to section 59 (b).

Sections 53 to 55. Consolidation and merger of national banks

In the last sentence of subsection (d) of section 53 there should be inserted the words "at public auction" immediately following the word "sold." This same change should be made in sections 54 and 55.

Section 57. Conversion, merger, or consolidation of national banks with State banks

It is recommended that the words "certified or" be inserted just before the word "registered" in section 57 (a) (1), as certified mail rather than registered mail is ordinarily now used and it serves the purpose that was formerly served by registered mail.

It is recommended that the second sentence of subsection (a) (2) of section 57 be amended by deleting therefrom the words "the date on which the shareholders' meeting was held authorizing" and substituting therefor the words "the effective date of"; and by deleting the words "unanimous vote of the dissenting shareholders" and substituting therefor the words "the vote of the holders of the majority of the stock, the owners of which are."

There should be added at the end of subsection (a) (2) of section 57 the following sentence:

"If the shares are sold at a price greater than the amount paid to the dissenting shareholders the excess of such sale price shall be paid to said shareholders."

Section 59. Appointment of receiver

The last sentence of section 59 (b) should be eliminated. This provision for the payment of interest on demand deposits was superseded by paragraph 12 of section 19 of the Federal Reserve Act, enacted in 1933. If reenacted at this time it will conflict with section 41 (b) of the proposed Federal Reserve Act.

Section 64. Conservation

Section 64 (d) provides that while a national bank is in the hands of a conservator the Comptroller may require the conservator to set aside and make available for payment to creditors such amounts as in the opinion of the Comptroller may safely be used for this purpose. The word "for" should be inserted just before the word "payment." It is assumed that the word "creditors" as used in this statute should be interpreted to include depositors.

In section 64 (f) the reference to section 206 should be a reference to subsection (d) of section 64.

Section 65. Emergency powers of the President

The words "the National Banking System and" should be deleted from the fourth line of this section since provisions for circulating notes of national banks are not included in the committee print.

Title II. Federal Reserve Act

Section 43. Federal Reserve notes

In section 43 (g) of the Federal Reserve Act there should be deleted the words "Comptroller of the Currency shall, under the direction of the Secretary of the Treasury," and inserted in lieu thereof the following: "Secretary of the Treasury shall"; and the words "and" and "shall." In Section 43 (i) the words "Secretary of the Treasury" should be substituted for the words "Comptroller of the Currency." Under existing practice plates and dies for the printing of Federal Reserve notes are procured by the Bureau of Engraving and Printing, a Bureau of the Treasury Department, and not by the Comptroller of the Currency.

Senator Robertson. Without objection, the complete prepared statement of Mr. Gidney will be made a part of the record at this point.

(The prepared statement of Mr. Gidney follows:)

Statement of Ray M. Gidney, Comptroller of the Currency

Mr. Chairman and members of the committee, I am honored to have this opportunity to testify with respect to the Financial Institutions Act of 1957. I wish to tell you how much we, in the bank-supervisory field of government, appreciate the splendid and outstanding work being done by this committee and its chairman, Senator Robertson.

First, we wish to point out that appendix A of our statement contains a list of sections in title I, National Bank Act, which we endorse and support as they now appear in the committee print bill. Appendix B contains a list of sections in title I which we endorse and support but recommend that minor changes of a technical nature be made in the wording. Our suggested wording appears in this appendix. In the interests of brevity, we will not comment specifically on the sections listed in appendix A, or on those sections or portions of sections listed in appendix B, unless the chairman or committee members desire us to do so.

The first section on which we wish to make specific comment is section 8 of title I, the National Bank Act.

Section 8. Conflicts of interest prohibited

Section 8 (a) would make it unlawful for the Comptroller of the Currency or any Deputy Comptroller to own stock in any national bank. It is recommended that this prohibition be extended to national bank examiners and assistant national bank examiners, and that it be made applicable to stock in bank holding companies as well as stock in banks. This would be consistent with the longstanding practice of our Office.

Section 8 (b) would make it unlawful for any employee or former employee of the Comptroller of the Currency to accept employment in any national bank or district bank except pursuant to regulations prescribed by the Comptroller. We have no objection to this provision insofar as it applies to employees or former employees who have only recently left the employ of the Comptroller. However, we think it is unnecessary and is unwise to permit the Comptroller to have control over employment by a national bank of a former employee of the Comptroller who may have ceased to be such an employee, 5, 10, 20, or even 30 years before. Many former employees of the Comptroller are today employed in national banks, some of them in very high positions. No reasonable purpose would be served by giving to the Comptroller control over the employment of these men by other national banks. We would suggest that this provision be amended to apply only to employees or to former employees who have ceased to be employees within a 2-year period.

At this point we should like to comment also on the provisions of section 803 of the bill which amends criminal statutes to make them applicable to employment of examiners and other employees of the Comptroller's Office by national banks. The provisions of this section give us grave concern.

Their enactment would seriously impair our ability to attract capable young men to our examining force. For practical purposes such young men joining our examining staff would do so with the knowledge that they must make bank examining a life career or leave the banking industry entirely if they should become dissatisfied with examining banks. For many years it has been our practice to obtain from each examiner an agreement reading as follows:

"You are requested to forward a statement that you will not, for a period of 2 years after you cease to hold the position of national bank examiner, accept employment of any kind in any bank which you may have examined without first receiving permission in writing from the Comptroller of the Currency."

This protective procedure has left nothing to be desired. We are strongly opposed to the enactment of statutes which would make offers of employment to, or acceptance of employment by, examiners or other employees of our office a crime. We strongly recommend to the committee that at least this portion of section 803 be eliminated.

Section 803 would also make it a crime for any national bank, insured bank, savings and loan association, or Federal credit union to make a loan to any employee of the Comptroller of the Currency without the written approval of the Comptroller. We believe that this prohibition should be confined to national and district banks which are examined and supervised by the Comptroller. We believe employees of the Comptroller of the Currency should be able to borrow from State-chartered banks, savings and loan association, and credit unions.

Section 803 (d) would make it a crime for any director, officer, employee, or stockholder owning 10 percent of the stock of any national or insured bank to make a political contribution in elections where supervisory officials or those having responsibility for public funds are to be elected. We believe it is an inherent right of every American citizen to make contributions to the political party of his choice. It is sufficient, in our opinion, for this prohibition to apply to the banks and we see no reason for extending the prohibition to directors, officers, or employees or stockholders thereof.

Section 12. Articles of association

It is recommended that section 12 be amended to expressly require the approval of the Comptroller of the Currency for the organization of a national bank. Since 1933 the Comptroller has been required in the case of newly organized national banks to certify to the Federal Deposit Insurance Corporation that the bank is authorized to transact the business of banking and that consideration has been given to the factors enumerated in section 6 of the Federal Deposit Insurance Act. Prior to 1933 there was uncertainty about the extent of the Comptroller's authority to deny new charter applications, and for approximately the first 50 years after passage of the National Bank Act in 1863 the various Comptrollers of the Currency considered they were without authority to deny such applications unless they had reason to suppose the bank was being organized for "other than the legitimate objects contemplated by this act."

Section 20. Preferred stock

It is recommended that a two-thirds vote should be required rather than a simple majority for the issuance of preferred stock. It is recommended that the statute provide for the Comptroller's approval of the issuance of preferred stock only "after determination by him that the only practicable method of obtaining desired additional capital is the issuance of preferred stock."

Section 20 in its present form would, we believe, leave the Comptroller no choice but to approve all applications filed by national banks to issue preferred stock provided the plans were soundly conceived. Enactment of this section presumably will settle the policy question of whether preferred stock should be sold by national banks as a normal or usual method of raising capital or only in urgent or unusual situations or under emergency conditions, local, sectional, or national. We believe that the sale of preferred stock by national banks should be approved by the Comptroller only in urgent or unusual situations or under emergency conditions. Our reasons for this recommendation may be summarized as follows:

(*a*) More than 1,600 national banks have sold in excess of $1 billion of new common capital during the past 10 years. Much of this in our opinion would have been in the form of preferred stock if the Comptroller had been willing to approve its issuance. It is clear that common stock is an adequate vehicle for raising new capital in national banks under normal conditions.

(*b*) The increased weight of risk of an enlarged volume of business predicated on newly acquired preferred capital would rest in the first instance on the common shareholders. The new preferred capital would justify an enlarged volume of risk assets, or more fully justify the existing volume of such assets, from the standpoint of depositor protection, but it must not be overlooked that the full weight of the increased risk would bear first on the common shareholders. Over a period of time this would result, in our opinion, in the common stock of banks losing some and perhaps much of its present high standing as a sound investment. The sale of preferred stock would tend to become the general rule in bank recapitalization programs, and the sale of common stock much more difficult.

If preferred stock were to be approved as a medium of normal bank recapitalization, it is obvious the Comptroller would have to establish sound policies relative to the proportion of preferred stock that could be issued by a bank in relation to its common capital stock or its overall capital structure. It would be undesirable for a bank to have a capital structure topheavy with nonvoting (except under certain conditions) preferred stock controlled by a thin layer of common stock. It is true the Comptroller could control this in initial instances, but if a bank issued preferred stock in reasonable proportion to its common stock and then by reason of growth or asset losses found it necessary again to raise additional capital, and this proved possible only through the issuance of more preferred stock, the Comptroller would be forced to choose between foregoing the additional capital protection needed by the bank's depositors, or permitting the bank's capital structure to become topheavy with preferred stock. Naturally, in such a situation the additional preferred capital would be approved, with the result that the amounts of preferred stock issued by particular banks, over a period of time, would be dictated more by exigencies than by the sound policies initially established by the Comptroller.

(*c*) One additional point is worthy of mention. If banks were to use the avernue of preferred stock for normal capital increases, it is easy to imagine the problems that would arise when some of those banks required emergency recapitalization. The two classes of stock already outstanding (common and preferred) could very well necessitate adding a third class of stock outranking both the existing common and preferred stocks. It is disturbing to contemplate the complications that would ensue from three classes of stock with an almost infinite number of possible variations in preferences as to dividends, retirement, voting rights, voluntary and involuntary liquidation, which would give rise to conflicts of interest between the several classes of shareholders.

We strongly believe it is in the best interests of banking to authorize the use of preferred stock only in urgent or unusual situations or under emergency situations. Consequently, we urge that the language suggested above be incorporated in the bill.

Section 21. Capital notes and debentures

Section 21 would authorize national banks to issue debt obligations in the form of capital notes or debentures subordinated to deposit liabilities but having preference over liabilities owing to the shareholders in the form of capital stock or dividends on such stock. We are opposed to this proposed provision of law unless the issuance of capital notes or debentures is authorized for emergency use only, and unless repayment of such obligations is made subject to the approval of the Comptroller of the Currency. The sale of such notes or debentures, in our opinion, would cause the common capital stock of some and perhaps many national banks to lose its attractiveness as an investment because of the adverse leverage of risk brought about by enlarged asset structures based on funds realized from the sale of the notes or debentures. Repayment should be made according to the terms of the notes, but obviously the Comptroller should not permit repayment unless the capital position of the bank justifies such action.

For the above reasons, it is recommended that the first sentence of section 21 be amended by adding after the word "Comptroller" the following "after determination by him that it is not practicable to obtain essential additional capital through the sale of common or preferred stock."

It is also recommended that there should be added after the words "national bank" in subsection (1) of section 21 (a) "with the approval of the Comptroller of the Currency."

A two-thirds vote rather than a simple majority should be required for the issuance of capital notes or debentures and it is recommended that an appropriate change be made in the first sentence of section 21 (a).

Sec. 23. Shareholders' lists

In connection with section 23, it was the original recommendation of the Comptroller of the Currency that the right of shareholders of a national bank to inspect the shareholders' list be qualified by a requirement of a showing of a proper purpose not inimical to the interests of the bank. This recommendation was approved by the Advisory Committee for the Study of Federal Statutes Governing Financial Institutions and Credit (report, pp. 5–6), but was not incorporated in the proposed act. We recommend that our original recommendation as approved be enacted.

In 23 (b) there has been added a sentence which would require the president or cashier to notify the Comptroller immediately of any single transaction involving the purchase or sale of 10 percent or more of the outstanding shares of a national bank. We regard this provision as unnecessary in the effective supervision of national banks. We know of no case in which the obtaining of this information at the time such a transaction was recorded on the bank's books would have enabled us to have more effectively discharged our supervisory duties.

Sec. 26. Election of directors

In section 26 (c) mandatory cumulative voting in the election of directors of national banks has been eliminated and provision made for permissive cumulative voting in those banks which desire it. We have previously testified both before this committee and before the House Banking and Currency Committee in favor of similar legislation after being advised by the Bureau of the Budget that there was no objection. We strongly endorse this provision of the bill and recommend that it be enacted.

Sec. 29. Removal of officers and directors

This section provides that hearings held by the Board of Governors of the Federal Reserve System to remove directors or officers from office shall be subject to review as provided in the Administrative Procedure Act "and the review by the court shall be upon the weight of the evidence." The Administrative Procedure Act provides that the reviewing court shall set aside agency action "unsupported by substantial evidence." Thus it seems that there is an inconsistency in saying the review shall be as provided by the Administrative Procedure Act, and then adding that the review shall be upon the weight of the evidence. We recommend that review should be as provided in the Administrative Procedure Act and that that portion of the fourth sentence of section 29 referring to review upon the weight of the evidence should be deleted.

Section 31. Corporate powers

In the earlier testimony before this committee a question was raised by one of the witnesses as to whether the contributions authorized by section 31 (a) (8) to organizations established for the purpose of civic improvement or betterment should be limited to contributions to nonprofit organizations as would be done by the bill. We believe it is essential to confine to nonprofit organizations the institutions to which such contributions should be authorized for national banks. We recognize that in some cases national banks may find it desirable to make contributions to profitmaking organizations, for example, a parking-lot corporation just getting started as a community project. However, such contributions normally may be regarded as legitimate business expenses rather than as charitable contributions. We recommend that the word "nonprofit" be retained in the section.

Section 31 (a) (9) would authorize any national bank to grant options to purchase its capital stock to its employees or to employees of any subsidiary corporation. We are aware that stock option plans are now in effect in 40 percent of the corporations whose stocks are listed on the New York Stock Exchange and are gaining increased use in industry generally, and that the justification given is that they are necessary in the procurement and retention of top rank officers. The only reason it is necessary to enact specific legislation to permit national banks to formulate and use stock-option plans is because of the preemptive stock-purchase rights of existing shareholders when additional stock is sold. We believe that banks should be on a parity with other corporations with respect to their right to use such plans when they have been soundly conceived and after approval by the Comptroller of the Currency.

We strongly urge that such legislation contain the following safeguards:

(*a*) We would suggest that national banks be permitted to grant only restricted stock options of the type which qualify under section 421 of the Internal Revenue Code of 1954.

(*b*) We suggest that the statute provide that no stock option plan shall be approved by the Comptroller if the option price is less than 85 percent of the fair market value or 85 percent of book value, as determined by the Comptroller, whichever is greater. The purpose of this requirement is to prevent too great a dilution in book value which would otherwise be suffered by the bank's other shareholders in those instances where the fair market value is below book value.

Section 32. Dealing in securities

Section 32 (b) would provide that a national bank may, with the approval of the Comptroller, purchase and hold for not more than 90 days stock of another bank as a step in a proposed absorption of such other bank through merger, consolidation, acquisition of assets and assumption of liabilities, or otherwise. We are opposed to enactment of this proposed legislation. Two or more national banks may merge or consolidate only upon the approval of the holders of two-thirds of the stock of each bank. If the directors of the absorbing or continuing bank could use bank funds to acquire control of another bank or banks they would, in effect, be able to acquire the other bank or banks by virtually forcing the approval of two-thirds of their stockholders. Once the bank owned control of another bank, the shareholders of the acquiring bank would, as a practical matter, have very little choice but to vote for the proposed merger or consolidation. We do not believe that it is proper for the officers or directors of a national bank to use the bank's money to acquire stock in another bank as a first step to merging or consolidating with that bank. We have similar beliefs with respect to any Federal legislation affecting State banks that are members of the Federal Reserve System.

Section 34. Maximum loan limitations

In the testimony of one of the previous witnesses before this committee a question was raised as to the word "identical" in exception 6 (B) to section 34 and as to whether the use of that word might create problems. We merely wish to point out that this is the language which exists in the present statute and we have had no problems arising out of its use.

Exception 12 to section 34 places a new limit on negotiable or nonnegotiable installment consumer paper of 25 percent of capital and surplus, but provides that upon certification by an officer of the association that the responsibility of the maker of each obligation has been evaluated and that the association is relying primarily upon the maker for the payment of each such obligation, the obligation of each maker shall be the sole applicable loan limitation. It is recommended that this proviso be amended to read as follows:

"*Provided, however*, That if the bank's files or the knowledge of its officers of the financial condition of each maker of such obligations is reasonably adequate, and there is a certification by an officer of the association, designated for that purpose by the board of directors of the association, that the responsibility of each maker of such obligations has been evaluated and the association is relying primarily upon each such maker for the payment of such obligations, the limitations of subsection (a) of this section as to the obligations of each such maker shall be the sole applicable loan limitation: *Provided further*, That such certification shall be in writing and shall be retained as part of the records of such association."

Section 35. Maximum rate of interest

The committee has added a new sentence at the end of subsection (a) of this section which would have the effect of permitting national banks to discount paper on the same basis permitted to State banks in the States wherein they are located. The purpose of this addition is to make it clear that national banks are no longer bound by the holding in the very old case of *National Bank* v. *Johnson* (104 U. S. 271). That case held that the purchase of paper from a dealer by a national bank was a discount within the meaning of the present Federal statute which limits the rate of interest which national banks may charge on loans or discounts to that prescribed by the laws of the State for State banks, or if there is no limit on State banks, to 7 percent. In some States the purchase of paper from a dealer by a State bank is regarded as a purchase and sale transaction to which the interest laws do not apply. In those States there is no limitation on discount transactions. This raises a question as to whether national banks are not limited to 7 percent on such discount transactions even though there is no limit on the State banks with which they are in competition. Under the bill it will be clear that national banks have the same rights in this respect as do State banks.

In his testimony before this committee Mr. Cravens suggested language to be substituted for the language in the committee bill reading as follows:

"The purchase of obligations or evidences of indebtedness from the actual owner thereof shall not, for the purposes of this section, be deemed a loan or discount if such purchase would not, under the law of the State in which the purchasing bank is located, be deemed a loan or extension of credit subject to the interest or usury statutes of such State."

We favor the language suggested by Mr. Cravens and recommend that it be adopted.

Section 36. Real-estate loans

Under present law national banks may make real-estate loans in an aggregate amount equal to the amount of the bank's capital stock and surplus, or 60 percent of the amount of its time and savings accounts, whichever is greater. Section 36 of the proposed act would permit national banks to make real-estate loans in an agregate amount equal to either of the sums or 20 percent of its demand deposits, whichever of the 3 is greater. We have no objection to this proposal except that we believe that public funds and deposits owing to other banks should not be included in demand deposits for the purposes of this section.

This section would also change present law by increasing the aggregate limit on construction loans which are not to be considered as loans secured by real estate from 50 percent of capital to 100 percent of capital and surplus. We favor this proposed change.

There would be added to this section a new subsection (e) which would permit loans to be made to manufacturing and industrial businesses where the bank looks for repayment out of the operations of the borrower's business, without such loans being regarded as real-estate loans even though secured by a mortgage on real estate. We favor this provision.

Section 44. Engaging in the securities business

A question has been raised in earlier testimony before this committee as to whether the change which was made in subsection (b) of this section is adequate to accomplish the purpose stated in our original recommendation, that is, to provide protection against State corporations receiving deposits without State or Federal supervision. We are satisfied that this section as drawn will satisfy our purpose.

Section 50. Confidentiality of examination reports

Section 50 would make examination reports, related correspondence and papers, and other information obtained by the Comptroller of the Currency in the exercise of his visitatorial powers, confidential documents privileged against disclosure without the consent of the Comptroller of the Currency. This is in accordance with one of our recommendations and we favor its enactment. There has been added a proviso to the effect that such documents shall be made available to the committees of the Congress upon request. This proviso would seem ineffective to compel the Comptroller to make such documents available if it is determined by the Executive that it would not be in the public interest to do so. We do not see how the proviso changes the situation as it presently exists, so as we are not opposed to it, although we would prefer its deletion.

Section 52. Reports by national banks

Section 52 would require that each national bank shall make to the Comptroller not less than three reports of condition and of the payment of dividends during each year. We recommend that the words "and of the payment of dividends" be eliminated from the first sentence of this section. We now receive semiannual reports of earnings and dividends of national banks and this has proved to be entirely adequate. We see no reason for requiring three reports of payment of dividends. We do not believe that it is necessary that the Comptroller be given specific statutory authority to call for reports of earnings and dividends as he does so now and may continue to do so under the power given to him to call for special reports from national banks.

This section has raised some questions as to whether under its authority the Comptroller could require national banks to publish reports of earnings and dividends, and also as to whether he could do so on a selective basis, that is, require some banks but not others to publish such reports. We do not recommend that national banks be required to publish reports of earnings and dividends. We also believe that there is some concern about differences in form and publication requirements for statements of conditon. We would have no objection if there were deleted from the fourth sentence of this section everything after the second comma, reading "and the Comptroller may prescribe different forms of such reports, and make different requirements as to their publication for different banks according to their location, size, or other reasonable classification." The power given in the statute to call for special reports is adequate to deal with all unusual or special situations.

Sections 53, 54, 55. Consolidations and mergers

In sections 53, 54, and 55 it is recommended that there be added a provision which would require dissenting shareholders who wish to demand the value in cash of their shares to do so by a written request made to the consolidated or merged bank within 30 days after the effective date of the merger accompanied by the surrender of their stock certificates. It is also recommended that for the first sentence of subsection (d) of each of these sections there should be substituted a provision which would provide that if within 90 days one or more appraisers is not selected or the appraisers have failed to determine the value of the shares, the Comptroller shall upon written request of any interested party, cause an appraisal to be made which shall be final and binding. The purpose of these changes is to insure that the appraisal of the shares of dissenting shareholders will be handled with reasonable promptness and that such appraisals cannot be delayed unduly by either the shareholders or the bank.

We went amend section 54 to expressly require the approval of the Comptroller of the Currency in the case of consolidation of State with national banks. Such approval has always been regarded as necessary under the existing statute but the wording is not clear and has given rise to questions from time to time.

Section 55 should be amended by adding provisions identical to those contained in subsections (e), (f), and (g) of sections 53 and 54 dealing with continuation of corporate existence, automatic transfer of trust accounts, and freedom from preemptive rights. These provisions are contained in the present statute and were omitted from the committee print bill because of an error by our office.

Payment by the Federal Deposit Insurance Corporation and the Federal Reserve Board for the use of reports of examination of national banks

In our original recommendation we recommended (No. 37) that in order to eliminate inequities and to restore a more equitable balance between the State and National banking systems, the Federal Deposit Insurance Corporation and the Federal Reserve System should be required to make certain payments to the office of the Comptroller of the Currency. At the hearings we suggested, as an alternative proposal, that payment be made by the Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation to the Comptroller of the Currency for copies of the reports of examination of national banks, which are regularly given to the Federal Reserve System and made available to the Federal Deposit Insurance Corporation, of 50 percent of the cost of making such examinations, 25 percent to be borne by the Federal Reserve System and 25 percent by the Federal Deposit Insurance Corporation. This recommendation was disapproved by the Advisory Committee with no reasons being given. However, it is apparent that there is an existing inequity which is detrimental to the national banking system. For this reason we urge that the committee give careful consideration to our proposal and that it be enacted into law.

National banks now bear the full expense of the supervision and the examinations which they receive from the Comptroller's Office. The entire expenses of the Comptroller's Office are paid out of assessments levied on national banks. State banks, on the contrary, which are supervised and examined by the Board of Governors of the Federal Reserve System, or the Federal Deposit Insurance Corporation, as well as by the respective State banking departments, do not bear directly any of the expense of such Federal supervision and examination. In the vast majority of cases State banks are examined jointly by the State authorities and by the examiners of the Federal Reserve banks or the Federal Deposit Insurance Corporation. In many States such examinations are conducted only once a year. By conducting joint examinations with Federal examiners State banking departments are enabled to operate with smaller staffs and at less expense to the State banks.

Thus State banks are, in varying degrees depending on the particular State, subsidized by the Federal Government through the Federal Reserve System, and by national banks through the Federal Deposit Insurance Corporation. The national banks receive no similar benefit. All national banks in the continental United States are members of the Federal Reserve System and are insured by the Federal Deposit Insurance Corporation. All of the funds of the Federal Deposit Insurance Corporation are derived from insurance assessments on insured banks, including national banks, and the latter have paid in approximately 50 percent of the existing Federal deposit insurance fund. Thus national banks through their payments to the Federal Deposit Insurance Corporation are paying part of the cost of examining State banks. This inequity should be eliminated.

In a majority of the States the examination fees are very much less for State banks than for national banks, particularly in the case of larger banks.

Through the payments suggested in the proposed amendment the examination fees assessed to the national banks by the Comptroller of the Currency could be reduced, thus restoring a more equitable balance between the State and National systems.

Merger or consolidated bank as branch office

In our original recommendations in connection with the banking law study we recommend (No. 45) that a national bank should be permitted to acquire by consolidation, merger, or purchase of assets and assumption of liabilities, another national bank located in the same county, which is found by the Comptroller of the Currency to be in a precarious financial condition, and to continue the office or offices of the absorbed banks as branches, regardless of the branch banking laws of the State, in which the banks are located. We continue to believe that this proposal has great merit and we urge that it be given serious consideration by the committee. As we stated in testimony before the committee last November we believe thatt enactment of this proposal would be in the best interests of the depositors and borrowers of such banks and substantially ease the problem of the Comptroller of the Currency in the case of banks which would otherwise have to be closed and liquidated. Any legislation enacted could contain adequate safeguards so that there could be no abuse of its provisions. We recommend that such authority be used only when it has been found by the Comptroller of the Currency that insolvency of the acquired bank is imminent, and when the Comptroller of the Currency has been advised in writing by the Federal Deposit Insurance Corporation that the proposed acquisition and the establishment of the branch or branches by the acquiring bank is in its opinion in the public interest. Thus two agencies, the Comptroller of the Currency and the Federal Deposit Insurance Corporation, would have to agree that the takeover and the establishment of the branch or branches would be necessary and desirable in the public interest.

Administration of pension and profit-sharing accounts of national banks

We continue to believe that it is desirable that there be basic statutory regulation of the more important aspects of retirement or pension, and profit-sharing accounts established by national banks. A small number of abuses have occurred. Pension and profit-sharing accounts are continuing to grow and it is likely that further abuses will occur. The Comptroller is without legal authority to intervene. As a basic requirement legislation should provide for the establishment of such accounts, require that the approval of shareholders be obtained, set forth the manner in which they are to be managed and records maintained, and should impose limitations on their borrowing and permissible investments, particularly investments involving "own" bank stock and the stock of competing banks.

With respect to this matter the Advisory Committee in its report pointed out that during the last Congress a subcommittee of the Senate Labor and Public Welfare Committee made a study of the need for additional Federal legislation with respect to the establishment and regulation of employee benefit plans generally, and stated that since it seems reasonably clear that similar legislation will be pressed during this Congress, that it would seem to be premature for this recommendation of ours to be considered. We recognize that the problem of employee benefit plans is not confined to national banks. However, we should like to point out that in the case of most such plans established by corporations a separate trustee is involved whereas in the case of banks the plan which is created by the bank may also be administered by the bank as trustee. Under these circumstances the investment provisions may tend to be broader and to give greater freedom to the trustee than might otherwise be the case. Furthermore, since the bank itself or individuals selected and presumably controlled by the directors are in many cases trustee of an account for the benefit of the bank's own employees there is greater possibility of problems arising than if there were an entirely separate trustee. In a few cases funds of this type of trust have been used by banks to acquire their own stock beyond reasonable limits or acquire the stock of competitive banks or for other purposes more to the benefit of the bank than to the benefit of the bank's employees. We believe that legislation which would give the Comptroller some control over these matters is essential and it should not wait for consideration by the Congress of employee benefit plans generally in which other problems than those peculiar to banks would be uppermost. Furthermore, we should like to point out to this committee that the legislation proposed by the Senate Labor Committee would not have provided for the regulation of these plans but merely for the gathering of information so that it may be several years before there is any effective Federal legislation in this field.

For these reasons we strongly recommend that the Committee give consideration to our original recommendation.

We shall turn now to title II, the Federal Reserve Act.

Section 28. Restrictions on officers and directors of member banks

Section 28 (e) places limitations on loans which may be made to executive officers of member banks. We notice that during these hearings there have been differences of opinion as to whether the term "executive officer" should be defined in the statute or whether the power to define this term by regulation should be continued in the Board of Governors of the Federal Reserve System. We favor continuing the authority to define this term by regulation in the Board.

Section 33. Voting permits of holding company affiliates

Section 33 (b) (3) of the Federal Reserve Act would change present law to permit holding company affiliates of member banks to use the reserve fund required by that section for the purpose of making additions to capital of their bank affiliates as well as for replacement of capital. The reserve fund required by this section has always been regarded as an emergency fund to be used for replacement of capital when necessary and we believe it would be undesirable to make the proposed change and to permit this fund to be depleted for the purpose of making normal additions to the capital of the banks. This might result in the reserve fund being inadequate to replace capital at a time when such replacement was essential.

We wish to make some comments with respect to title III, the Federal Deposit Insurance Act.

Section 6. Management of the Corporation

The Federal Deposit Insurance Act would eliminate the Board of Directors of the Federal Deposit Insurance Corporation and would place the management of that corporation in the hands of a single Administrator who would be given the power to appoint a Deputy Administrator. The act would also provide for the creation of an Advisory Board to consist of the Comptroller of the Currency, the Chairman of the Board of Governors of the Federal Reserve System, or his designee, and a State officer exercising functions relating to the supervision of State banks. Apparently this Advisory Board would have no duties except to consult with the Administrator at his request, but not less frequently than 4 times each year, and to make recommendations to the Administrator relative to the carrying out of his duties. The Administrator would be free to accept or reject the advice of the Advisory Board. We would doubt the wisdom of including in this legislation this change in the management of the Federal Deposit Insurance Corporation. A matter of such importance should we think be given more extended study before enactment into law.

In view of the fact that the Financial Institutions Act of 1957 deals primarily with operating matters, we suggest that it should not include a change in the management of the Corporation but that consideration of this matter should be left for the proposed National Monetary Commission to examine more fully.

If serious consideration is to be given by the committee to establishing a single Administrator for the Corporation, we deem it imperative that he be placed under the general supervision of a Cabinet officer, which it is presumed would be the Secretary of the Treasury. The insurance fund of the Federal Deposit Insurance Corporation is presently in excess of $1½ billion, and the Corporation has a call upon the Treasury for loans in an amount up to $3 billion. We do not believe any single Administrator should be given unsupervised power or control over and responsibility for such a large sum.

Section 16. Assessment rate

Section 18. Assessment credits

We have noticed that repeatedly throughout these hearings the question of assessments by the Federal Deposit Insurance Corporation has been raised with some suggestions that a study should be made. We concur in the desirability of a study to determine whether a more scientific basis for levy of assessments is possible.

We believe, however, that no change should be made in current assessment rates until such a study has been completed. Furthermore, we believe that a study should not be forced to completion by a statute limiting the study period to 1 year as has been suggested in these hearings. It should be sufficient for the committee to request that the results of the study be presented to the Senate Banking and Currency Committee within 1 year.

Section 23. Mergers and consolidations

Section 23 of the Federal Deposit Insurance Act is identical with S. 3911 of the 84th Congress which was fully considered by the Senate Banking and Currency Committee, and approved by the Senate in July 1956. This section would require the approval of 1 of the 3 Federal bank supervisory agencies for all bank mergers in which either of the banks involved is an insured bank and would require that consideration be given to the competitive aspects of such mergers as well as highly important banking factors.

Other legislation has been introduced in the Congress which would amend section 7 of the Clayton Act to prohibit bank mergers by means of acquisition of assets when the effect of such acquisition of assets may be substantially to lessen competition or to tend to create a monopoly.

We strongly favor the provisions of section 23 of the committee print bill and urge that it be enacted in lieu of legislation which would make bank asset acquisitions subject to the provisions of the Clayton Act.

This Department considers it essential to weigh and adequately consider the always important and frequently vital banking factors in conjunction with purely competitive factors so as to arrive at fair and well-balanced decisions in approving or denying bank mergers. Legislation which would make the Clayton Act applicable to bank-asset acquisitions would place jurisdiction in the Department of Justice rather than the Federal bank supervisory agencies and would legally require the denial of bank mergers solely on competitive grounds.

Banking has unique safeguards against monopoly or inadequate competition which are not present in industry or trade. Banks may not establish offices across State lines. Their operations within individual States are either limited to one head office (in nonbranch bank States, such as Illinois, Texas, Florida, etc.) or to the establishment of branch offices within the State where the bank's head office is located as may be approved by the bank supervisory authorities within areas defined in State statutes authorizing branch banking. A majority of the branch bank States restrict such activities to county limits, but some States permit it on a trade area basis, a contiguous county basis, or on a statewide basis. Obviously, the concentration of commercial bank assets within such geographical limitations can never pose problems of an antitrust nature that even approach in seriousness those with which the Justice Department has long been confronted in industry or trade.

We consider it essential to place jurisdiction over bank mergers in the Federal bank supervisory agencies because they are best suited to consider the broad monetary and banking questions and economic and financial development problems which surround a decision on the relative competitive factors involved in a decision as to whether a bank should or should not be merged. Banking is a closely regulated industry and we believe its regulation should be continued in the hands of the Federal bank supervisory agencies rather than to place one phase of its regulation under the jurisdiction of another Government department.

We sincerely believe the status of competition in banking today is at a very high level and that the public interest in this respect is being well served. We believe that the enactment of section 23 will insure, beyond all doubt, a continuance of this status.

Section 26. Payment of interest

Under present statutes prohibiting the payment of interest on demand deposits, the Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation have taken differing positions with respect to absorption of exchange charges. In its recommendation No. 77 the Board pointed out that this has resulted in placing member banks at a serious competitive disadvantage in some sections of the country, and recommended that Congress should by legislation either explicitly state that absorption of exchange charges constitutes the payment of interest or give to the Board or the Federal Deposit Insurance Corporation the power to define "interest" for both classes of banks. National banks in the continental United States are member banks in the Federal Reserve System and find themselves at the same competitive disadvantage with respect to insured nonmember banks as do other member banks of the Federal Reserve System. We think that under the proposed act the question of whether absorption of exchange charges shall be deemed to be interest is left undecided. For this reason we reclegislation proposed by the Senate Labor Committee would not have provided for the regulation of these plans but merely for the gathering of information so that it may be several years before there is any effective Federal legislation in this field.

For these reasons we strongly recommend that the Committee give consideration to our original recommendation.

We shall turn now to title II, the Federal Reserve Act.

Section 28. Restrictions on officers and directors of member banks

Section 28 (e) places limitations on loans which may be made to executive officers of member banks. We notice that during these hearings there have been differences of opinion as to whether the term "executive officer" should be defined in the statute or whether the power to define this term by regulation should be continued in the Board of Governors of the Federal Reserve System. We favor continuing the authority to define this term by regulation in the Board.

Section 33. Voting permits of holding company affiliates

Section 33 (b) (3) of the Federal Reserve Act would change present law to permit holding company affiliates of member banks to use the reserve fund required by that section for the purpose of making additions to capital of their bank affiliates as well as for replacement of capital. The reserve fund required by this section has always been regarded as an emergency fund to be used for replacement of capital when necessary and we believe it would be undesirable to make the proposed change and to permit this fund to be depleted for the purpose of making normal additions to the capital of the banks. This might result in the reserve fund being inadequate to replace capital at a time when such replacement was essential.

We wish to make some comments with respect to title III, the Federal Deposit Insurance Act.

Section 6. Management of the Corporation

The Federal Deposit Insurance Act would eliminate the Board of Directors of the Federal Deposit Insurance Corporation and would place the management of that corporation in the hands of a single Administrator who would be given the power to appoint a Deputy Administrator. The act would also provide for the creation of an Advisory Board to consist of the Comptroller of the Currency, the Chairman of the Board of Governors of the Federal Reserve System, or his designee, and a State officer exercising functions relating to the supervision of State banks. Apparently this Advisory Board would have no duties except to consult with the Administrator at his request, but not less frequently than 4 times each year, and to make recommendations to the Administrator relative to the carrying out of his duties. The Administrator would be free to accept or reject the advice of the Advisory Board. We would doubt the wisdom of including in this legislation this change in the management of the Federal Deposit Insurance Corporation. A matter of such importance should we think be given more extended study before enactment into law.

In view of the fact that the Financial Institutions Act of 1957 deals primarily with operating matters, we suggest that it should not include a change in the management of the Corporation but that consideration of this matter should be left for the proposed National Monetary Commission to examine more fully.

If serious consideration is to be given by the committee to establishing a single Administrator for the Corporation, we deem it imperative that he be placed under the general supervision of a Cabinet officer, which it is presumed would be the Secretary of the Treasury. The insurance fund of the Federal Deposit Insurance Corporation is presently in excess of $1½ billion, and the Corporation has a call upon the Treasury for loans in an amount up to $3 billion. We do not believe any single Administrator should be given unsupervised power or control over and responsibility for such a large sum.

Section 16. Assessment rate

Section 18. Assessment credits

We have noticed that repeatedly throughout these hearings the question of assessments by the Federal Deposit Insurance Corporation has been raised with some suggestions that a study should be made. We concur in the desirability of a study to determine whether a more scientific basis for levy of assessments is possible.

We believe, however, that no change should be made in current assessment rates until such a study has been completed. Furthermore, we believe that a study should not be forced to completion by a statute limiting the study period to 1 year as has been suggested in these hearings. It should be sufficient for the committee to request that the results of the study be presented to the Senate Banking and Currency Committee within 1 year.

Section 23. Mergers and consolidations

Section 23 of the Federal Deposit Insurance Act is identical with S. 3911 of the 84th Congress which was fully considered by the Senate Banking and Currency Committee, and approved by the Senate in July 1956. This section would require the approval of 1 of the 3 Federal bank supervisory agencies for all bank mergers in which either of the banks involved is an insured bank and would require that consideration be given to the competitive aspects of such mergers as well as highly important banking factors.

Other legislation has been introduced in the Congress which would amend section 7 of the Clayton Act to prohibit bank mergers by means of acquisition of assets when the effect of such acquisition of assets may be substantially to lessen competition or to tend to create a monopoly.

We strongly favor the provisions of section 23 of the committee print bill and urge that it be enacted in lieu of legislation which would make bank asset acquisitions subject to the provisions of the Clayton Act.

This Department considers it essential to weigh and adequately consider the always important and frequently vital banking factors in conjunction with purely competitive factors so as to arrive at fair and well-balanced decisions in approving or denying bank mergers. Legislation which would make the Clayton Act applicable to bank-asset acquisitions would place jurisdiction in the Department of Justice rather than the Federal bank supervisory agencies and would legally require the denial of bank mergers solely on competitive grounds.

Banking has unique safeguards against monopoly or inadequate competition which are not present in industry or trade. Banks may not establish offices across State lines. Their operations within individual States are either limited to one head office (in nonbranch bank States, such as Illinois, Texas, Florida, etc.) or to the establishment of branch offices within the State where the bank's head office is located as may be approved by the bank supervisory authorities within areas defined in State statutes authorizing branch banking. A majority of the branch bank States restrict such activities to county limits, but some States permit it on a trade area basis, a contiguous county basis, or on a statewide basis. Obviously, the concentration of commercial bank assets within such geographical limitations can never pose problems of an antitrust nature that even approach in seriousness those with which the Justice Department has long been confronted in industry or trade.

We consider it essential to place jurisdiction over bank mergers in the Federal bank supervisory agencies because they are best suited to consider the broad monetary and banking questions and economic and financial development problems which surround a decision on the relative competitive factors involved in a decision as to whether a bank should or should not be merged. Banking is a closely regulated industry and we believe its regulation should be continued in the hands of the Federal bank supervisory agencies rather than to place one phase of its regulation under the jurisdiction of another Government department.

We sincerely believe the status of competition in banking today is at a very high level and that the public interest in this respect is being well served. We believe that the enactment of section 23 will insure, beyond all doubt, a continuance of this status.

Section 26. Payment of interest

Under present statutes prohibiting the payment of interest on demand deposits, the Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation have taken differing positions with respect to absorption of exchange charges. In its recommendation No. 77 the Board pointed out that this has resulted in placing member banks at a serious competitive disadvantage in some sections of the country, and recommended that Congress should by legislation either explicitly state that absorption of exchange charges constitutes the payment of interest or give to the Board or the Federal Deposit Insurance Corporation the power to define "interest" for both classes of banks. National banks in the continental United States are member banks in the Federal Reserve System and find themselves at the same competitive disadvantage with respect to insured nonmember banks as do other member banks of the Federal Reserve System. We think that under the proposed act the question of whether absorption of exchange charges shall be deemed to be interest is left undecided. For this reason we recommend that section 41 of the Federal Reserve Act, and section 26 of the Federal Deposit Insurance Act, both prohibiting the payment of interest on demand deposits, should contain express prohibitions against the absorption of exchange charges by member and by insured banks respectively.

Senator ROBERTSON. Are there further questions?

Senator BENNETT. No questions.

Senator ROBERTSON. The chief counsel has a question.

Mr. ROGERS. Mr. Gidney, in the conservation section, we took out in one sentence, a provision for your payment to depositors. I see in your technical amendments you think that depositors are covered by the provisions for payment to creditors. Would it be just as well to restore that language to the bill?

Mr. GIDNEY. I think I shall fall back on Mr. Jennings on that.

Mr. JENNINGS. I think it would be just as well to restore that to include the word "deposits" or "depositors," whichever one is appropriate to that section.

Senator ROBERTSON. Thank you. If there are no further questions, we want to thank you. Your testimony has been very clear and very helpful.

Mr. GIDNEY. I should like to just say this is a fine piece of work going forward, and if it can come through, it will be a valuable accomplishment.

Senator ROBERTSON. We appreciate that. Thank you very much.

We have a report on our committee print bill from the Comptroller General of the United States.

It will be inserted in the record at this point.

(The report referred to follows:)

COMPTROLLER GENERAL OF THE UNITED STATES,
Washington, D. C., February 7, 1957.

B-130239

Hon. J. W. FULBRIGHT,
Chairman, Commitee on Banking and Currency,
United States Senate.

DEAR MR. CHAIRMAN: Reference is made to your letter of January 5, 1957, acknowledged January 9, 1957, requesting a report from us on a proposed bill to amend and revise the statutes governing financial institutions and credit.

The proposed bill was drafted after consultation with the Federal agencies involved, a study report by committee staff, hearings by the committee, and review of agency legislative recommendations by an advisory committee of private citizens expert in the field. The first seven titles of the bill deal consecutively with national banks, the Federal Reserve bank system, the Federal Deposit Insurance Corporation, Federal Home Loan Banks, Federal savings and loan associations, the Federal Savings and Loan Insurance Corporation, and Federal credit unions. The eighth and last title of the bill contains repealing provisions, separability and savings clauses, and miscellaneous amendments to statutory law related to other titles of the bill.

With respect to national banks and the Federal Reserve System, covered by titles I and II of the bill, your committee realizes, we are sure, that the General Accounting Office presently has no audit responsibilities and for that reason we have no comments on those titles of the bill which we feel would be helpful to the committee. However, in connection with title II of the bill mention should perhaps be made of the question which has arisen in the past and which was discussed with counsel for the committee regarding an audit by the General Accounting Office of the Federal Reserve System.

For a number of years, the accounts of the Board of Governors of the Federal Reserve System, but not those of the Reserve banks, were audited by the General Accounting Office. The Banking Act of 1933 amended section 10 of the Federal Reserve Act to provide explicitly that funds of the Board, which are derived from assessments on the Federal Reserve banks, "shall not be construed to be Government funds or appropriated moneys." The 1933 act further provided that the Board should determine and prescribe the manner in which its obligations should be incurred and its disbursements and expenses allowed and paid. By reason of this language, our audits of the Board ceased, and it is our opinion that specific authorization by the Congress would be needed to permit us to undertake an audit of the activities of the Board or of the Reserve banks.

This question was discussed at the time of enactment of the Government Corporation Control Act of 1945 (31 U. S. C. 841), and the Congress determined to exclude the Federal Reserve System from audit under that act, principally because of the fact that all of the stock of the banks was owned by members banks and the strong control exercised over the Reserve banks by the Board. During the 84th Congress a bill (H. R. 2643) was introduced which would have required us to make an audit of the Board, the Open Market Committee, and the Reserve banks. A similar bill (H. R. 7602) was introduced in the preceding Congress. Neither bill was enacted. Our position as to both bills was that we believed it to be a matter of policy for the Congress to determine whether such an audit was necessary or desirable. It has been reported to us that the Board, the Open Market Committee, and the Reserve banks are presently audited by private firms and the reports of these audits are made available to appropriate congressional committees. In view of the prior history of the matter, we have no recommendation to make concerning a change in the existing law.

With respect to title III of the bill, the Federal Deposit Insurance Act, we have the following comments:

In section 4, page 150, it is suggested that the word "assets" be changed to "surplus."

Section 6, page 151, provides that the management of the Corporation shall be vested in an Administrator. Whether the management should be vested in an Administrator or in a Board of Directors as it is under existing law is, in our opinion, a matter of policy for determination by the Congress. Our audits of the Corporation have not disclosed any deficiencies attributable to the present form of management.

Section 10, pages 153–154, makes certain records confidential and privileged. The language used is so broad that it would preclude access to such records by the General Account Office without the consent of the Corporation. The General Accounting Office is directed by section 38 of the bill to make an audit of the financial transactions of the Corporation, and while we certainly believe that the records in question should be treated as confidential so far as concerns disclosure of any information which might adversely affect a bank, we feel that our audit cannot be as complete and effective as it should be without access to such records. We therefore recommend the insertion of the following language immediately after the word "prohibited" in line 6 on page 154: "except that such records shall be made available to the General Accounting Office in connection with the audit authorized by section 38 hereof."

Section 16, pages 156–158, deals with the assessment rate for insured banks. As the committee knows, the deductions and exclusions from the assessment base permitted under existing law, and continued in subsection 16 (a) of the proposed bill, have been the cause of considerable difficulty in administration. We believe the committee might well give consideration to the desirability of including in this section a provision permitting banks, at their option, to take a standard percentage deduction in lieu of the present itemization of deductions. We believe that such a provision could be worked out which would result in not too great a reduction in income to the Corporation, and which would at the same time result in savings both to the banks and the Corporation in computation and audit procedures. We understand that the Corporation is presently making studies looking toward simplification of assessment computations.

In section 20 (a), page 160, we believe that the first part of the proviso, from the words "no action" through the words "except that," well might be deleted in the interest of brevity with no change in meaning.

In section 29 (a), page 165, substitution of the word "except" for the word "and" in the 10th line from the bottom of the page would make the meaning clearer.

We are pleased to note that section 38 (b), page 178, embodies our recommendation in audit reports of the last several years that the calendar year be made the fiscal year of the Corporation, and that our audits and related reports be made accordingly. This provision, if enacted, will facilitate our audit. We do, however, have the following recommendation with respect to the balance of section 38. Subsections (a), (c), and (d) thereof are merely a restatement of the audit authority and procedures contained in the Government Corporation Control Act. We note that the legislative program outlined in the President's budget message of January 16, 1957, contains a recommendation for amendments to the Government Corporation Control Act which would apply to the Corporation. We believe it would be preferable, therefore, and we recommend, that subsections (c) and (d) of section 38 be deleted, and that subsection (a) be rewritten to provide simply that our audit be in accordance with the Government Corporation Control Act. Any subsequent amendments to that act would then be applicable in connection with our audit of the Corporation without the necessity for amending the Federal Deposit Insurance Act. This could be accomplished by striking out the last part of subsection (a) beginning with "and," the last word on page 177, and substituting in lieu thereof the words "as provided by the Government Corporation Control Act, as amended."

Section 39, pages 179–180, embodies a recommendation we have made that the Corporation pay the Government's share of the cost of retirement, disability, and compensation benefits for employees of the Corporation. We note that provision is made for the Corporation to pay its share of administrative costs connected with the Federal employees' compensation fund only for periods after January 1, 1957. We believe that the provision should be changed to cover past periods also, and we believe provision should be made for payment of the administrative costs incident to retirement and disability benefits for both past and future periods. This could be accomplished by inserting the following sentence in section 39:

"The Corporation shall also pay into the Treasury as miscellaneous receipts such sums as shall be agreed upon by the Civil Service Commission and the Corporation as a fair portion of the cost of administration of the civil-service retirement system for all periods subsequent to the creation of the Corporation."

and by rewording the third sentence of the section to read as follows:

"The Corporation shall, on the basis of billings as agreed upon by the Secretary of Labor and the Corporation and for all periods subsequent to the creation of the Corporation, pay into the employees' compensation fund the amount of benefit payments made from such fund on account of the Corporation's officers and employees and into the Treasury as miscellaneous receipts a fair portion of the cost of administration of such fund."

If these changes should be made, we believe the next two sentences of the section would be unnecessary, since the succeeding portion of the section makes it clear that any payments applicable to periods prior to January 1, 1957, shall be paid out of the Corporation's capital account, and that payments for subsequent periods are to be included as administrative and operating costs.

Titles IV, V, and VI of the bill deal with the Federal home-loan banks, Federal savings and loan associations, and the Federal Savings and Loan Insurance Corporation.

At the present time the General Accounting Office conducts an audit of the Federal Home Loan Bank Board, the 11 Federal home-loan banks, and the Federal Savings and Loan Insurance Corporation. We think the language of subsection 17 (c), title IV, pages 198–199, which would make the financial transactions of the Board and Corporation subject to no other requirements, scrutiny, or review than are now applicable to the Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation, respectively, might be interpreted to mean that the Board would not be subject to audit by the General Accounting Office inasmuch as the Board of Governors is not. We understand that this result was not intended, particularly since an audit of the Corporation could not be performed without an audit and review of many of the operations that are handled on behalf of the Corporation by the Board.

If the language mentioned is to remain in the bill, we believe it would be desirable to state specifically that the Board and Corporation shall be audited by the General Accounting Office. In this connection, we also believe consideration well might be given to making the calendar year the fiscal year of the Board and Corporation. This could be accomplished by inserting the following sentence in subsection 17 (b) immediately before the next to the last sentence of the subsection:

"The fiscal year of the Board and the Federal Savings and Loan Insurance Corporation shall be the calendar year."

We suggest, as to our audit, the changing of the period at the end of subsection 17 (c), page 199, to a semicolon, and the addition of the following language: "and the Federal Home Loan Bank Board and the Federal Savings and Loan

Insurance Corporation shall be audited annually by the General Accounting Office."

Our audits and related reports would, of course, be made on the basis of the fiscal year of the Board and Corporation.

The intended effect of subsection 17 (c), title IV, pages 198–199, is stated by the Federal Home Loan Bank Board to be to give to the Board and to the Federal Savings and Loan Insurance Corporation the authority "* * * to incur proper expenditures without the necessity for annual budgeting and authorization and for freedom to operate without regard to restrictive statutes."

It would also permit the Board to depart from the requirements of the Civil Service Act and the Civil Service Retirement Act upon a determination of necessity or advisability for the efficient conduct of operations of the Board or Corporation. We are opposed to a change in existing law so far as concerns the exemption of the Board and Corporation from budgetary requirements. With regard to the exemption from civil-service laws, we neither advocate nor oppose the proposal. However, if the principle of exemption set forth in the subsection should be adopted, we believe the powers and authority to be vested in the Board and Corporation should be stated in detail rather than by reference to those now exercised by the Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation.

In any event, we believe the Board and the Federal Savings and Loan Insurance Corporation should be required to pay the Government's share of the cost of civil-service retirement and disability benefits, and Federal employees compensation benefits, including administrative expenses, for past and future periods, as we have suggested for the Federal Deposit Insurance Corporation. This could be accomplished by adding another subsection to section 17 patterned after section 39, title III, page 179.

The remaining suggestion of substance we have with respect to titles IV, V, and VI concerns the present requirement that the Federal Savings and Loan Insurance Corporation assess insurance premiums against an insured institution on the basis of its total share liability plus creditor obligations at the beginning of its insurance policy year. We have consistently recommended in our audit reports that the National Housing Act be amended to provide that insurance premiums be assessed on the basis of the average share liabilities plus creditor obligations during the policy year. It may be noted that the Federal Deposit Insurance Corporation uses an average as the assessment base. See section 7 (a) of the existing law, continued as section 16 (c), title III, page 158, of the proposed bill.

Title VII of the bill deals with Federal credit unions, and the only suggestion we have concerning this title is with respect to the composition of the supervisory committee of unions. The supervisory committee is charged with internal audit responsibility for the union. It would be in accordance with sound principles of internal control to prohibit the treasurer, who is also a director and the general manager of the union, and any member of the credit committee from serving as a member of the supervisory committee. This could be accomplished by deleting the parenthetical phrase in line 4 of section 12, page 234, and inserting in lieu thereof the following: "(a majority of whom shall not be directors and none of whom shall be a member of the credit committee or treasurer of the corporation)."

We notice that the bill proposes to add new subsections to several titles thereof which would make it a criminal offense for any employee or former employee of the agency involved to accept employment in any institution supervised or insured by that agency except pursuant to such agency's regulations. The subsections referred to are 8 (b), title I, page 3; 38 (i), title II, page 113; 40 (d), title III, page 180; 19 (b), title IV, page 200; and 21 (i), title VII, page 240. Apparently through inadvertence, title VI does not contain a comparable provision which would apply to employees of the Federal Savings and Loan Insurance Corporation. We notice also that title VIII, subsections 803 (a) and 803 (b), pages 247–249, would greatly enlarge the scope of sections 217 and 218 of the Criminal Code. We are not expert, of course, in the field of criminal law, but it seems to us that the changes these provisions would make in existing law are so drastic that the committee should obtain the views of the Attorney General thereon. We merely point out the possibility of considerable differences between regulations issued by different agencies and the resulting differences in criminal liability of their employees.

We believe the word "free" as used in certain subsections in connection with mailing privileges should be deleted. See subsection 8 (a), third sentence, title

III, page 152: subsection 19 (a), title IV, sixth line from bottom of page 199; and line 1, page 217, title VI.

We appreciate the opportunity given us to comment on the proposed bill, and we trust our suggestions and views may be of value to the committee in the commendable task it has undertaken.

Sincerely yours,

JOSEPH CAMPBELL,
Comptroller General of the United States.

Senator ROBERTSON. There are several letters and statements that have been received that will go in the record.

(The material referred to follows:)

STATEMENT OF MILTON O. SHAW, PRESIDENT, NATIONAL ASSOCIATION OF STATE SAVINGS AND LOAN SUPERVISORS

Some of the provisions of said act appear to invade the rights of the States and are repugnant to the wording and intent of the 10th amendment to the Constitution. In my opinion, Federal laws and regulations of State associations should be restricted to matters affecting the risk of the Federal Savings and Loan Insurance Corporation.

Specific provisions which do not affect such risks are:

1. Title VI, paragraph 404 (c) (p. 221 of the bill) authorizes the Federal Savings and Loan Insurance Corporation "to impose such conditions to insurance, which conditions may be conditions precedent or conditions subsequent, as it may deem necessary." This provision would give the insurance corporation unlimited authority. Any provision authorizing conditions precedent should require that such conditions be applied uniformly to all associations. Unlimited authorization for conditions subsequent should be eliminated. All insured associations should be governed by the same laws and regulations and special conditions which could be applicable to particular associations and could be without limit as to duration should not be sanctioned.

2. Title VI, paragraph 404 (e) (p. 221 of the bill) gives the Insurance Corporation unlimited authority over mergers and transfers. Under this proposal approval of said Corporation would be required should a State insured association sell even one loan to another State insured association. Such a transfer could not affect the insurance risk and the provision is unnecessary. No loss to the insurance corporation is believed to have resulted from existing laws and procedures regarding mergers and transfers.

3. Under title VII, section 217 (p. 247 and p. 248 of the bill) any insured association and any person holding 10 percent of the stock thereof are prohibited from offering employment to State examiners and supervisory officers and such examiners and officers are prohibited from accepting employment by such an association for a period of years. State employees have nothing to do with the granting of insurance of accounts and the Federal Savings and Loan Insurance Corporation does not accept the reports of examination made by State examiners. The employment of former State personnel could not affect the insurance risk, and the provisions relating to State employees should be eliminated. The State should have sole authority to regulate the conduct of its employees.

4. Title VIII, section 218 (d) (p. 249 of the bill) would prohibit contributions or expenditures by a director, officer, employee, or the holder of 10 percent or more of the stock of an insured savings and loan association in connection with any election at which any official who has authority to regulate or supervise savings and loan associations is to be elected. The wording of this measure is so broad that such persons would be prohibited from making campaign contributions for the election of members of State legislatures, governors, Members of Congress and even the President of the United States. It is believed that such officers, directors, employees, and stockholders should have the same rights as other citizens.

Title V, section 501, paragraph 5 (i) (4) (p. 210 of the bill) requires clarification.

The Federal Home Loan Bank Board on or about October 18, 1956, wrote to the various State supervisory officers as follows:

"When an institution converts, without Board approval, it must remain mutual in character until dissolution. * * * A subsequent change to a permanent stock structure would be regarded by the Board as a violation of the statute and a basis for terminating insurance of accounts."

This new position of the Board is based on a new and completely about-face interpretation of said clause (4) which reads: "that, in the event of dissolution after conversion, the members or shareholders of the association will share on a mutual basis in the assets of the association in exact proportion to their relative share or account credits;" without regard to section 5 (i) (5) which reads: "that such conversion shall be effective upon the date that all the provisions of this act shall have been fully complied with and upon the issuance of a new charter by the State wherein the association is located; * * *"

Said Federal Home Loan Bank Board had interpreted these sections and had acted under an opposite interpretation for many years. Please note the following excerpt of letter from Dr. William H. Husband, General Manager of the Insurance Corporation, to the California commissioner dated February 16, 1950:

"Second, you raise the very interesting point as to that section of our reconversion bill which requires proportionate sharing in the assets by the mutual shareholders in event of dissolution following conversion. Personally, I had the feeling that this section of our law applied only to dissolution following the first conversion; namely, from Federal to State mutual. It did not seem to me that such a right could continue thereafter and, particularly do I question its applicability when a State-chartered institution converts to another form of corporate entity. Again, no one can forecast how a court would hold but at least I can say our legal department agrees with the view I just expressed."

The right of Congress to control forever the form of State corporations is seriously questioned. We do not believe Congress so intended.

May I suggest that said clause (4) of paragraph 5 (i) of title VI be deleted in order to restore some measure of sanity to the situation.

Ohio Bankers Association

Recommendations of the Legislative Committee in Regard to Proposed Financial Institutions Act of 1957 and Related Matters

Cumulative voting

Section 26 (c): Permission for shareholders of national banks to use cumulative voting in the election of directors when the articles of association so provide, should be supported.

Temporary stock in another bank

Section 32 (b): If this proposal can be properly safeguarded so that it will not be an instrument used primarily for the promotion of mergers, it should be supported. Is 90 days too long?

Real-estate loans

Section 36 (a): The proposal to allow an aggregate of national bank real-estate loans outstanding up to 20 percent of all deposits as an alternate yardstick, should be supported.

Section 36 (a): A redefinition providing that a leasehold pledged as security for a real-estate loan would be one having maturity of not less than 10 years beyond the final maturity of such loan, should be supported.

Construction loans

Section 36 (c): The proposal to permit national banks to make construction loans on industrial and commercial buildings, with maturity not to exceed 18 months, provided there is a valid takeout agreement from a financially responsible concern, should be supported. The increase in the aggregate amount of construction loans which a national bank can hold from 50 percent of capital to 50 percent of combined capital and surplus, should be supported.

Industrial loans

Section 36 (e): The proposal to permit national banks to make loans to established industrial or commercial businesses with repayment from the operation of such borrowers, and with a maturity of not more than 10 years, whether or not secured by a mortgage on real estate, should be supported. The committee feels that amortization should be required.

Limit of indebtedness

Section 37: The proposal that national banks be permitted to borrow up to an amount not exceeding the amount of the combined capital paid in and unimpaired surplus of such national bank, should be supported.

Reports by national banks

Section 52 (a): The proposed extension to allow national banks 10 days to comply with call reports, should be supported. The repeal of present law requiring national banks to report declaration of dividends to the Comptroller, should be supported—the information is otherwise available.

Loans to executive officers

Section 28 (e): The proposal to permit executive officers to borrow up to $5,000 unsecured from their own institutions, and the right to borrow up to $25,000 on homes for personal occupancy, should be supported.

Federal home-loan bank—supervisory authority

Section 4 (d): The proposals to have the powers, present and future, of the Federal Home Loan Bank Board spelled out in the statutes, should be supported.

The work "Bank" should be eliminated from the Federal Home Loan Bank Board.

Federal savings and loan association branches

Section 6 (c): The proposal that Federal savings and loan associations should not be permitted to establish branches, except in conformity with the laws and practices of the States governing the establishment of branch offices of State-chartered savings and loan associations, should be supported. Branches across State lines should be prohibited.

Federal credit unions

Section 15: Maximum loan limits on Federal credit unions should not be increased and control over such limits should remain in the statutes.

Payment of insurance

Section 406: Extreme care should be taken to prevent the nature of an insured deposit or an insured account from being changed by either the Federal Deposit Insurance Corporation or the Federal Savings and Loan Insurance Corporation.

MISCELLANEOUS

Bank mergers

Control over bank mergers should be in the hands of appropriate bank supervisory agencies, but without prejudice to the powers of the various State authorities when a State-chartered institution is involved.

National branches and States rights

If a national bank acquires another bank located within the same county, the purchasing bank should be governed by its State law in regard to the operation of branches.

Postal savnigs

The Postal Savings System should be abandoned as early as practicable.

Equal taxes

Whether in the proposed bill or otherwise, provision should be made for at least approximate equal taxation of all financial institutions regardless of their corporate nature. The same principle should apply to other fields of business.

COLUMBUS, OHIO, *February 1, 1957.*

HOMLER CREDIT UNION,
New York, N. Y., February 5, 1957.

Re Omnibus Banking Bill Forced Audits of Credit Unions.

SENATE BANKING COMMITTEE,
Washington, D. C.

GENTLEMEN: As a founder of Homler Credit Union, organized under the New York State banking laws in 1917, and as the chairman of the supervisory committee for the last 36 years, I urge you to recommend the forced audits law.

Anyone who appears before your important committee to speak against the proposed law is not familiar with the problem.

A great number of the supervisory committees and directors of a credit union do not know how to audit books. Many credit committees are indifferent to their financial responsibilities. They rely on the honesty of their managers and other officers.

Because of this, many shareholders have lost their investments in some credit unions, due to mismanagement and defalcation.

The cost to a shareholder, whatever it may be, is negligible compared to what could happen.

Audit and controls should always be welcomed.

I urgently ask you to disregard any objection to audits, and recommend favorably this most important law, to protect the savings of shareholders in a credit union.

The law should be extended to all credit unions from $1,000 and up.

Respectfully yours,

SAMUEL ZACHARIN,
Vice President, Central Industrial Bank, Brooklyn, N. Y.

PHILADELPHIA, PA., *January 23, 1957.*

Senator JOSEPH S. CLARK, Jr.,
Washington, D. C.

DEAR SENATOR CLARK: Once again I find myself bringing a matter to your attention in regard to corporate procedure, because I understand that the subject of mandatory cumulative voting will be brought up in the Senate Banking Committee in regard to the application to national banks.

I have had a very rough time in my work at the Philadelphia Transportation Co. even with cumulative voting, so I am naturally a great supporter of any committee which will sponsor that democratic procedure for proportional representation.

The continuity of management is a great thing, but only provided that it does not get stuffy and inefficient. Even with cumulative voting, it is extremely difficult to get a majority representation on a board, and when a group has only a minor proportion of the stock, but perhaps a greater quantity than any other individual group, it only seems fair that they be allowed to express their views in the board room, even though outvoted.

I hope that in your studies of this subject you will remember that the "old guard" in management can be as detrimental to the progress of a corporation as the same kind of crowd in political strongholds.

Thanking you for your consideration of this subject, I am,

Very sincerely yours,

JOSEPH N. JANNEY.

WEST FARGO STATE BANK,
West Fargo, N. Dak., February 4, 1957.

Re section 803 (2) sections 217 and 218 of title 18, of the United States Code and a bill to amend and revise the statutes governing financial institutions and credit.

Hon. MILTON R. YOUNG,
United States Senator,
Senate Office Building, Washington, D. C.

DEAR SENATOR YOUNG: It has come to my attention that a bill to amend and revise the above statute is to be presented in Congress, to which I, and many others to whom I have spoken, object in part very strongly.

Objection is to parts (ii) and (iii) of the above section, wherein penalty and imprisonment can be made against the bank, State, or Federal agency, or individual as the case may be in offering employment to or seeking employment by an examiner, assistant examiner or individual in any institution which is under State or Federal supervisory authority.

Realizing what such a regulation, if allowed, would do to the freedom of individuals and the recruiting of administrative forces for Government agencies and other corporations, I ask that you endeavor to prevent such legislation from being passed. Qualified personnel in the past have always been from the line of experience and if such freedom is not allowed to continue, deterioration will result.

I sincerely ask that you will use your ability and sound reasoning in voting against this amendment.

Yours very truly,

K. A. NIELSEN.

Senator ROBERTSON. The committee will stand in recess until 10 o'clock tomorrow morning when Governor James Robertson of the Federal Reserve Board will be the witness.

(Whereupon, at 3:40 p. m. the committee was recessed until 10 a. m., Tuesday, February 12, 1957.)

STUDY OF BANKING LAWS

(Financial Institutions Act of 1957)

TUESDAY, FEBRUARY 12, 1957

UNITED STATES SENATE,
COMMITTEE ON BANKING AND CURRENCY,
SUBCOMMITTEE ON BANKING,
Washington, D. C.

The subcommittee met, pursuant to recess, in room 301, Senate Office Building, at 10 a. m., Senator A. Willis Robertson, chairman of the subcommittee, presiding.

Present: Senators Robertson, Douglas, Monroney, Lausche, Clark, Bricker, Bennett, and Payne.

Senator ROBERTSON. The subcommittee will please come to order. Chairman Fulbright has received a letter from the Chairman of the Federal Reserve Board dated January 23, 1957, in which the Board reports on the bill that we have under consideration. If there is no objection I will have this letter printed in the record at this point.

(The letter referred to follows:)

BOARD OF GOVERNORS,
OF THE FEDERAL SYSTEM,
Washington, January 23, 1957.

HON J. W. FULBRIGHT,
Chairman, Committee on Banking and Currency,
United States Senate, Washington 25, D. C.

DEAR MR. CHAIRMAN: This is in response to your letter of January 5, 1957, requesting a report by the Board on a committee print draft of a bill to amend and revise the statutes governing financial institutions and credit.

The draft bill embodies a complete revision of existing statutes relating to national banks, member banks, insured banks, savings and loan associations, and Federal credit unions. Because of the bill's length and great number of changes which it would make, it would be impracticable for the Board to attempt to comment on all its provisions in detail. Many of them, of course, relate to matters beyond the Board's jurisdiction and have no direct effect upon the Federal Reserve System. Accordingly, it seems desirable at this time to limit the Board's comments to that portion of the bill which would revise the Federal Reserve Act and to certain other provisions which are of direct interest to the Board and the System.

It is noted that the bill would incorporate most of the technical and clarifying changes in Federal Reserve laws which were recommended by the Board to your committee in October 1956, and in the course of the hearings held by the committee in November. Certain of the changes recommended by the Board have been followed in the bill with modifications; and the Board sees no objection to the modifications made in the bill with respect to recommendations 51, 60, and 66, relating respectively to residence of Federal Reserve bank directors (title II, sec. 17 (a)), stock acquisitions in connection with bank absorptions (title II, sec. 23 (d)), and concurrence of a majority of Board members in taking certain actions (title II, secs. 10 (b), 39 (1), 42 (a) and (b)). Nor would the Board interpose objection to the provision of the bill (title II, sec. 28 (e)) which, in addition to increasing the dollar exemption from the prohibition upon loans by member banks to their executive officers, as recommended by the Board (No. 81), would also liberalize present requirements as to reports by such officers of their indebtedness to other banks.

On the other hand, the bill would not carry out the recommendations made by the Board with respect to elimination of the provision of section 7 of the present Federal Reserve Act as to the application by the Treasury of funds received from the Federal Reserve banks (No. 55), taxation of dividends on Federal Reserve bank stock (No. 56), fiscal agency operations of the Federal Reserve banks (No. 67), repurchase agreements by the reserve banks (No. 72), revocation of trust powers of national banks (No. 69), and payment of interest on deposits by member and nonmember insured banks (No. 77). For the reasons stated when these recommendations were submitted, the Board continues to feel that they should be adopted; and the Board hopes that at least recommendations 77, 72, and 67, in that order of importance, will be given further consideration by your committee.

Title II of the bill, revising the Federal Reserve Act, contains a number of changes in present law which were not included in the recommendations submitted by the Board last October. The Board will wish to give further study to the effect of these changes. However, it may be stated at this time that, as indicated at the committee hearings in November, the Board approves those new provisions of the bill which relate to audits of the Board and the Federal Reserve banks (title II, secs. 38 (h) and 39 (m)); and the Board would have no objection to the proposed repeal of the business loan authority of the Reserve banks now contained in section 13b of the Federal Reserve Act or to the proposed transfer of regulatory authority over trust powers of national banks from the Board to the Comptroller of the Currency. On the other hand, the Board questions the desirability of certain of the other changes which would be made by title II of the bill.

Section 33 (b) (3) of title II would authorize a holding company affiliate to use the reserve of readily marketable assets required by the statute for additions to capital in its affiliated banks as well as for replacement of capital. The Board feels that the proposed use for capital additions would be inconsistent with the general purposes of the reserve requirement of the law and the Board would question the advisability of broadening the provision as proposed in the bill. The statutory reserve was intended to enable a holding company affiliate to come to the assistance of its subsidiary banks in times of local or national emergency. If the reserve were to be used in normal times for additions to capital, it might well be depleted and not be available when it would be needed in unusal circumstances in order to maintain the sound condition of the banks.

Section 29 of title II would incorporate in provisions relating to removal of officers and directors of State member banks a new specific requirement that the hearing in connection therewith shall be held in accordance with the Administrative Procedure Act and be subject to review as therein provided and that review by the court shall be upon the "weight of the evidence." The Board sees no need for this special provision, since hearings under this section would be subject to the Administrative Procedure Act without the provision; and the Board questions the desirability of departing from the provisions of that act which, among other things, states that the reviewing court may set aside agency action if it is "unsupported by substantial evidence."

Section 38 (i) of title II would prohibit employees and former employees of the Board and the Federal Reserve banks from accepting employment in member banks except pursuant to regulations of the Board. While the Board understands and concurs in the general objective of this provision, it believes that it would be unduly severe. Although subject to regulations, the provision would place a heavy burden upon individuals who may have been employed by the Board 20 or 25 years ago; the provision should at least be qualified so as to apply only for a specified period, such as 2 years. Moreover, while insolated abuses may be cited, it seems probable that the employment by banks of former employees of the supervisory agencies would in general be beneficial rather than injurious to both the public service and the banking system. In addition, the provision would be likely to impede the recruitment of personnel by the supervisory agencies. It should also be noted that this section may be somewhat inconsistent with some of the criminal provisions of section 803 of the committee print, as to which comment will be made later in this letter.

With respect to provisions of the bill other than those contained in title II, the Board wishes to comment at this time on four provisions which appear to be directly related to the Federal Reserve System.

Provisions which would make reports of examinations and related correspondence privileged against disclosure except with the consent of the supervisory agency are incorporated in titles I and III, with respect to national banks and insured nonmember banks. No similar provision is found in title II. The Board believes that a comparable provision should be included in title II regarding the confidentiality of examination reports of State member banks.

Section 6 of title III of the bill would replace the Board of Directors of the Federal Deposit Insurance Corporation with a single Administrator, and section 7 would create an advisory board consisting of the Comptroller of the Currency, the Chairman of the Board of Governors of the Federal Reserve System or his designee, and one person selected by the President who would be a State officer exercising functions relating to the supervision of State banks. The Board believes that, in view of the extensive nature of the Board's functions in other important fields, it would not be appropriate or desirable for the Chairman of the Board or his designee to serve as a member of the proposed Advisory Board.

Section 26 of title III would eliminate a requirement of the present Federal Deposit Insurance Act that "the board of directors [of the Federal Deposit Insurance Corporation] shall by regulation prohibit the payment of interest on demand deposits in insured nonmember banks" and would substitute language providing that "no insured bank shall, directly or indirectly, by any device whatsoever, pay any interest on any deposit which is payable on demand." This change would not, in the Board's opinion, be adequate to meet the administrative problems and inequities which have arisen in the administration of these provisions. On the contrary, the Board believes that the proposed change would further complicate the situation, since the language of the bill would literally authorize the Administrator of the Federal Deposit Insurance Corporation to define the term "demand deposits" (though not the term "interest") for all "insured banks," both member banks and nonmember insured banks.

In its recommendation No. 77 on this subject, the Board proposed that the words "directly or indirectly, by any device whatsoever" be deleted from the provisions of the Federal Reserve Act relating to payment of interest on deposits by member banks, and that a "payment of interests" be defined as including only cash payments made, or credits given, by a bank for the account or benefit of a depositor. The Board also recommended that competing member and nonmember insured banks be made subject to the same rules as to what constitutes a payment of interest on deposits, particularly with respect to absorption of exchange charges; and, to this end, the Board suggested that the relevant provisions in the Federal Reserve Act and in the Federal Deposit Insurance Act should contain an explicit identical statement on this point, or, in the alternative, that the Board or the Federal Deposit Insurance Corporation should be authorized to define "interest" for both classes of banks.

In its report of December 17, 1956, the Advisory Committee that assisted your committee in its study, recommended that provisions of the Federal Deposit Insurance Act on this subject be changed to read like those in the Federal Reserve Act so that uniform interpretations would necessarily follow, and that the Board's ruling as to absorption of exchange as a payment of interest should be applicable to all insured banks alike. The change made by section 26 of title III of the committee print may have been designed to follow the Advisory Committee's recommendation; but, in the Board's opinion, it falls short, perhaps inadvertently, of achieving that committee's stated objection.

This objective could be achieved, and in a manner which would be in accord with the Board's recommendation, if the words "directly or indirectly, by any device whatsoever" were omitted from the provisions of law regarding payment of interest on demand deposits by member banks (contained in sec. 41 of title II of the bill) and if the provisions regarding payment of interest on demand deposits by nonmember insured banks (contained in sec. 26 of title III of the bill) were made to read exactly like those with respect to member banks but were made applicable only to nonmember insured banks, and if in both instances a proviso were added to the effect that a "payment of interest" shall include only cash payments made, or credits given, by a bank for the account or benefit of a depositor, and that absorption of exchange charges shall be deemed to be a payment of interest.

Section 803 of the bill would revise sections 217 and 218 of the Criminal Code, which now relate to the making of loans and gratuities by a bank to examiners authorized to examine such bank and, conversely, to the acceptance of loans and gratuities by examiners from banks examined by them. The proposed revision of these sections would make them applicable not only to member and insured banks but also to institutions insured by the Federal Savings and Loan Insurance Corporation, Federal credit unions, and any stockholder of any such bank or other institution holding 10 percent or more of the stock thereof. The revision would also extend these sections to apply not only to examiners but to officers and employees of the Federal supervisory agencies; and they would cover not only loans and gratuities but also employment or offers of employment.

While some expansion of these criminal provisions along the lines indicated may be desirable, the Board believe that the revision proposed by the bill would be unduly rigid and severe and give rise to difficult problems of interpretation and administration. For example, the bill would seem to make it a crime for any insured savings and loan association or Federal credit union, as well as any member bank, to make a loan or offer of employment to any employee of the Board of Governors without the Board's written approval. Again, it would be made a crime for any member, officer, or employee of the Board to accept a loan or offer of employment from any member bank with respect to which the individual may have performed any "duties" in the preceding 2 years. Moreover, the provisions in question appear to be inconsistent with other provisions of the bill relating to the employment by banks of employees and former employees of the supervisory agencies. The Board, therefore, would be strongly opposed to the revision of sections 217 and 218 of the Criminal Code as contemplated by the committee print.

As previously indicated, the Board may wish, on the basis of further study, to submit additional comments with respect to other provisions of the bill. The Board may also wish to submit certain comments and suggestions of a technical nature; and as to such matters the Board's legal staff will be glad to render any assistance which may be desired.

In conclusion, the Board would like to compliment your committee and its staff for the care with which this comprehensive bill has been prepared.

Sincerely yours,

WM. McC. MARTIN, Jr.

Senator ROBERTSON. The witness today on behalf of the Federal Reserve Board is the Honorable James Robertson, a member of the Board of Governors of the Federal Reserve System.

Those who were present last November remember how helpful his testimony was to us at that time. I am sure it will be equally helpful to us today.

Governor, we will be pleased to hear from you.

STATEMENT OF J. L. ROBERTSON, MEMBER, BOARD OF GOVERNORS, FEDERAL RESERVE BOARD

Mr. ROBERTSON. Thank you very much, Mr. Chairman. I am perfectly willing to do this in any way that meets the wishes of the committee. I do have a statement and I can read that if it is agreeable, and at any time if you would like to break in I wish you would, or I can do it in any other way you deem appropriate.

Senator ROBERTSON. We have been permitting the members of the committee to break in when they thought there was something pertinent. So, if that is agreeable to you, you may proceed until you are interrupted.

Mr. ROBERTSON. Very well.

Mr. Chairman, the Board of Governors is in full accord with the committee's objective of streamlining the present banking laws; and the committee print which is the subject of these hearings in an admirable step in that direction. For the most part, its effect would be to rearrange provisions of existing law in a more orderly manner, eliminate obsolete provisions, correct technical defects, and clarify ambiguous provisions. At the same time, it would also make a number of substantive changes, and it is to be expected that there may be differences of opinion as to the desirability of some of these changes.

Most of the provisions of the committee print relate to matters which are beyond the Board's jurisdiction and have no direct effect upon the Federal Reserve System. The Board's comments, therefore, are limited primarily to the provisions of title II of the bill revising the Federal Reserve Act and to certain provisions of other titles of the bill which directly affect the system or are of interest to the Board.

TITLE II (FEDERAL RESERVE ACT)

Title II of the committee print would make numerous technical and clarifying changes in the Federal Reserve Act that are obviously desirable and appear to require no special comment.

Most of the changes of substance are in general accord with the legislative recommendations made by the Board to the committee last October and during the committee's hearings in November. These changes include restoration of a requirement for payment of a franchise tax by the Federal Reserve banks to the United States; removal of the present statutory dollar limitation on the cost of Federal Reserve bank branch buildings; provision for rotation in office of Federal Reserve bank directors and of members of the Federal Advisory Council; authority for the requirement of reports from state member banks on a sample basis; a requirement that Federal Reserve bank directors reside within the Federal Reserve district or within a radius of 50 miles of the Reserve bank; authority for the temporary acquisition of bank stock by a member bank in connection with the absorption of another bank; a liberalization of restrictions on loans by member banks to their executive officers; and a limited extension of the authority of foreign branches of national banks to enable them to compete on more equal terms with banks in foreign countries. All of these changes are desirable, in the Board's opinion, as tending to improve and facilitate the operational activities of the Federal Reserve System and its member banks.

The bill contains a new provision which would require annual audits of the accounts of the Board of Governors by a firm of certified public accountants. Another provision would require the Board to take measures to assure that examinations of the Federal Reserve banks meet the highest standards of commercial audits, and the Board would be authorized to arrange for review by certified public accountants of the procedures followed in the examination of the Reserve banks. All such audits of the Board and reports of examinations of the Reserve banks would be required to be transmitted to the Banking and Currency Committees of Congress. As indicated at the hearings held by the committee last November, the Board would favor the enactment of these provisions of the bill.

The bill contains some additional substantive changes in Federal Reserve law which have not been suggested by the Board. To certain of these changes the Board would have no objection; as to others it would have reservations.

The bill would require every State member bank to keep, and transmit to the Board on demand, a full list of its shareholders, and to notify the Board of any purchase or sale of its shares involving 10 percent or more of the number outstanding. The Board believes that these requirements have merit and would not be unduly burdensome.

Investments in bank premises by a State member bank would, under the bill, require the Board's approval only if they should exceed 100 percent of the bank's capital stock or 50 percent of the bank's capital and surplus, whichever might be greater, whereas present law requires Board approval in all cases in which the investment would exceed 100 percent of capital stock. The Board would have no objection to this change.

The bill would have the effect of repealing the present authority of the Reserve banks under section 13 (b) of the Federal Reserve Act to make working capital loans and commitments to business enterprises. The repeal of this authority, which has been utilized very little in recent years, would be in accord with the position heretofore taken by the Board in this matter.

The bill would transfer to the Comptroller of the Currency the present authority of the Board to grant trust powers to national banks and to regulate the exercise of such powers. As indicated at the committee hearings last November, the Board would have no objection to the transfer of that authority to the Comptroller of the Currency.

Section 29 of title II would make certain changes in the provisions now contained in section 30 of the Banking Act of 1933 regarding the removal from office of directors and officers of member banks. A new provision would require that hearings under this section be held in accordance with the Administrative Procedure Act and be subject to review as therein provided and that review by the court shall be upon the "weight of the evidence." Since any such hearings would be subject to the Administrative Procedure Act without this provision, the Board sees no need for its inclusion. Moreover, the provision for judicial review on the weight of the evidence would be a departure from the general rule, as stated in the Administrative Procedure Act, that the reviewing court may set aside agency action if it is "unsupported by substantial evidence"; and the Board would not favor this departure from the general rule.

Senator BRICKER. I do not see how anybody can argue that if a citizen of the country is to have his day in court he could argue against a finding on the weight of the evidence. It is incomprehensible to me. I know they do it all over, for example, in the Interstate Commerce Commission. To have it decided on the substantial evidence rule on the finding of the court is to me as a lawyer just as unsound as it can be. I will be perfectly frank about it.

Mr. ROBERTSON. On my side, Senator, I will say I think Congress should decide whether there should be judicial review on the weight of the evidence or whether a court should upset a specialist agency only in cases where there is not substantial evidence. But I think the rule should be uniform and not a rule of one kind for one agency and another rule for other administrative agencies of the Government.

Senator BRICKER. An administrative board is not a court, and when you are through with your findings there you have not had a day in court. Although it is not required of Federal agencies, I grant you, it is of all State agencies under the Constitution. Yet, I think, a review of the evidence is the right of every American citizen. I do not care what right is taken away from him or decided, I firmly feel a review is essential. It may not be of the Supreme Court, but some court impartially constituted. I think this idea of a specialized agency has been entirely overlooked in the whole administrative system. That is a personal feeling.

Mr. ROBERTSON. I think it may well have been that this administrative agency empire has grown up recently in the last quarter of a century. It may be there needs to be revision in the kind of review, but it ought to be uniform.

Senator BRICKER. I agree with you entirely on that.

Senator BENNETT. Then is not the question that my colleague is suggesting a possible amendment to the Administrative Procedure Act?

Senator ROBERTSON. Indubitably. We just followed the existing law. Every time there is evidence of what would look like a lot of bureaucratic action, they say, "This law ought to be changed." Yet it is a general law and was passed primarily to facilitate the transaction of Government business. The Government is in too many businesses, but it has to have some law to expedite it, I reckon, and this is one of the expediters.

Senator BRICKER. I think inherently it gives too much power to the administrative agency. I like to have a citizen have his day in court.

Senator ROBERTSON. You may proceed.

Mr. ROBERTSON. Section 33 of title II would permit a holding company affiliate to use the reserve of readily marketable assets required by present law for the purpose of making additions to the capital of its affiliated banks as well as for replacement of capital. This reserve was intended to enable a holding company affiliate to come to the aid of its subsidiary banks in times of stress or emergency. If it could be used in normal times for additions to capital in order to enable expansion and growth, the reserve fund might be depleted and not be available at the very time when it would be needed to maintain the sound condition of the subsidiary banks.

The same section contains a new provision which, in a situation in which there are several holding company affiliates with respect to the same bank or group of banks, would permit the statutory reserve to be maintained by only one of such companies to be designated by the Board. The Board would have no objection to this provision if, in order to prevent possible evasions of the law, a proviso were included to the effect that, of the holding company affiliates involved, only the designated holding company affiliate shall own stock of the subsidiary banks in the group.

Mr. ROGERS. Would you explain that a little bit more, Governor?

Mr. ROBERTSON. Yes. This particular provision is applicable, so far as I know, only to one holding company group. In that particular group there are holding companies on top of another. It is a pyramid. It is perfectly proper that only the lowest of the affiliates should hold the reserve, but after having been designated as the company to hold the reserve it should not be put in a position where it can distribute its stock to the other holding company affiliates and thus minimize the requirement for building up a reserve. You can accomplish that very easily without any harm to the affiliate group if you merely require that the lowest level in the pyramid hold all of the stock of those banks.

Finally, as far as title II of the committee print is concerned, the Board would not favor, at least in its present form, the new provision in section 38 (i) prohibiting employees and former employees of the Board or the Federal Reserve banks from accepting employment in member banks except pursuant to regulations of the Board. This provision, which carries heavy criminal penalties, would place an unduly severe restriction on individuals who may have been employees of the Board or the Reserve banks many years ago. If this provision should be enacted. it would undoubtedly increase the difficulty of recruiting qualified new employees. Moreover, we know of no abuses within the Federal Reserve System; and furthermore, an oppropriate path for employees between banks and the supervisory agencies would, on the whole, be beneficial rather than injurious to the public service and the banking system.

Senator ROBERTSON. The Chair interrupts to say up to this point in the hearings that section of the bill has had no friends, so I suspect it will be lonesome when we mark up the bill.

Mr. ROBERTSON. That being so, I will skip the rest of that part.

Senator ROBERTSON. Let it go in the record, though.

Mr. ROBERTSON. Yes, certainly.

The Board sees no need for such a "conflict of interests" provision, but it would not object to the provision if it were made inapplicable to any former employee after a specified period, such as 2 years. At a later point, comment will be made on the even more severe provisions of section 803 of the bill affecting the employment by banks of former employees of the Federal supervisory agencies.

It is noted that the committee print's revision of the Federal Reserve Act does not include provisions to carry out a few of the Board's recommendations. Some of the more important omissions may be mentioned.

For many years, the Federal Reserve banks in connection with their open market operations have utilized repurchase agreements as a convenient and flexible means of helping to smooth out temporary irregularities in the money market. These agreements are in the form of a purchase and sale and they are used only to implement open market policies under regulations of the Federal Open Market Committee. However, they have some of the attributes of a loan and the law now contains no specific reference to such transactions. Accordingly, the Board recommended an amendment specifically authorizing such repurchase agreements; and we continue to believe that such a clarifying amendment would be desirable.

Another of the Board's recommendations omitted from the committee print was that the activities of the Federal Reserve banks as fiscal agents of the United States and of various agencies of the Government should be made specifically subject to supervision and regulation by the Board. Such activities have increased substantially in recent years. More than 3,300 of the System's employees are engaged in fiscal agency activities for more than 25 governmental agencies in approximately 50 different capacities. It has become more and more evident that, in addition to the general authority of the Board to supervise the Federal Reserve banks, there should be some more specific authority for the overall coordination of the fiscal agency operations of the Reserve banks. Such authority would help to prevent Government departments and agencies from requiring the Reserve banks to perform functions which may be inconsistent with their overall purposes and unduly burdensome.

Senator BRICKER. Give us some examples of that.

Mr. ROBERTSON. Yes. We act as fiscal agents for the Post Office Department. We act as fiscal agents for the Treasury Department.

Let us take one example on that. Under the law the Treasury Department has the right to tell the Federal Reserve banks that they shall act as fiscal agents in connection with the destruction of Treasury currency. In my opinion I think the Federal Reserve System should not be destroying currency at all. For many, many years, that currency has been sent into Washington and cut in half before being sent in. One-half is sent in and when it is received you send the other half. They are both counted by different groups of people, and if they are correctly counted then they are destroyed.

The safeguarding of the currency of the country I think warrants even a greater number of safeguards than might be considered necessary. In the Federal Reserve banks you do not have that sort of safeguard, because it is almost impossible, in my opinion, to prevent collusion. We hope we never have any.

Senator BRICKER. You have not had any?

Mr. ROBERTSON. One case, and that was in a very small amount. But the mere fact that it is there indicates the possibility of collusion, and it would not take much to destroy the confidence of the people in the currency of the country. The Treasury Department has the right to tell the Federal Reserve banks to act in that capacity, and the Federal Reserve banks must act in that capacity, and they do, and do a very good job. The purpose was to save money, but it is not really saving a great deal, because instead of the cost being paid by the Treasury Department out of appropriated funds, the cost is paid by the Federal Reserve banks, and thus there are less earnings coming back into the Treasury. It is a sort of round-the-rosy proposition.

I doubt that the Federal Reserve banks should be conducting that sort of thing.

Senator BRICKER. Of course, it is high anyway.

Mr. ROBERTSON. Well, that is an example of the kind of services, and we think they ought to be coordinated.

Senator BRICKER. That is what I wanted to get clarified. Thank you.

Senator ROBERTSON. Governor, this was one of the original recommendations of the Board last November.

Mr. ROBERTSON. That is right, sir.

Senator ROBERTSON. It did not receive the endorsement of our advisory committee and was strenuously opposed by the Treasury Department. We did not ask Mr. Gidney about it yesterday, we just assumed he was still against it. However, there is just a little division of opinion.

You think it is a good provision and you would like us to put it in the final bill?

Mr. ROBERTSON. That is right.

Senator ROBERTSON. Thank you.

Mr. ROBERTSON. Finally, the committee print does not carry out the recommendations made by the Board on the subject of payment of interest on deposits by member and nonmember insured banks. The bill would make only one change in present law in this respect. At present, the Federal Deposit Insurance Act provides that—

the board of directors shall by regulation prohibit the payment of interest on demand deposits in insured nonmember banks and for such purpose it may define the term "demand deposits."

Senator BENNETT. Before we get into that very difficult question, I would like to return to this matter that has just been discussed, namely, the question of service to the Treasury.

Mr. ROBERTSON. Right.

Senator BENNETT. As I read your recommendation, you are not attempting to get away from the service, but you are asking that the Board be given supervision over the services that are now performed independent of the board by individual member banks.

Mr. ROBERTSON. Individual Federal Reserve banks.

Senator BENNETT. I mean individual Federal Reserve banks.

Mr. ROBERTSON. That is right, sir.

Senator BENNETT. I think it is important that that be clear. You are perfectly willing to perform the services and are willing to continue to destroy currency, but you want the Board to supervise it rather than leaving it to the individual member banks.

Mr. ROBERTSON. That is correct, sir. We want to coordinate activities of the entire system. For example, let me give you another instance.

We do perform certain services for the Post Office Department. That was under an arrangement whereby we would be compensated, or the Federal Reserve banks would be compensated for the services performed. These were in connection with handling the deposits by postmasters but there are a number of them for the post office. The reimbursable expenses amount to $450,000 a year, but because of a difference of view between the Treasury and the Post Office Departments as to which funds should pay for that, the Federal Reserve banks are not compensated.

We think there ought to be some way in which to coordinate all of those activities and make certain that there are definite understandings before the services are performed. I think you are very nice to bring out the point that we do want to perform those services. We think that is a part of the function of the Federal Reserve banks, to perform those fiscal agency services, but it ought to be done on a coordinated and unified basis.

Senator BENNETT. I was afraid from your previous testimony you were leaving the impression that you wanted to get out from under the services, and that was not the way I read the language of the statement.

Mr. ROBERTSON. I would regret very much if I gave that understanding. I certainly did not intend to.

Senator BENNETT. You simply want to have a central authority to supervise and coordinate the services.

Mr. ROBERTSON. That is right.

Senator BENNETT. Rather than leaving it to the responsibility of each Federal Reserve bank.

Mr. ROBERTSON. That is exactly right.

Senator ROBERTSON. The Chair just said that the Treasury Department does not like it to get out to the public too much on this, but they are against it. They say in the opinion of the Treasury officials it is not quite as innocent as it looks on the face of it, or words to that effect.

Mr. ROBERTSON. It is more innocent than that, even.

Senator ROBERTSON. You may proceed.

Mr. ROBERTSON. Section 26 of title III of the committee print would change this language to read:

No insured bank shall, directly or indirectly, by any device whatsoever, pay any interest on any deposit which is payable on demand and for such purpose the Administrator may define the term "demand deposits."

Mr. ROGERS. May I interrupt? There is a typographical error there.

Mr. ROBERTSON. I think that is so, and I do refer to it later.

Mr. ROGERS. It should be "no nonmember."

Mr. ROBERTSON. I am sure that is so. My next sentence relates to that and I am sure it is just an inadvertency.

In the Board's opinion, this change would not only be inadequate to meet the problems and inequities which have arisen in this particular field, but would actually multiply the existing difficulties because, while it may not have been intended—and that is what you are referring to?

Mr. ROGERS. Yes. Right.

Mr. ROBERTSON. While it may not have been intended, the new language would authorize the Federal Deposit Insurance Corporation to define "demand deposits" for all insured banks. In order to avoid any misunderstanding, we should like to restate and attempt to clarify the two objectives of the Board's recommendations on this subject.

In the first place, it has become clear over a period of many years that the present law on this subject is completely unworkable. This has been due to the difficulty of determining whether various services offered by banks to their depositors, such as free parking facilities, special printing of checks, and so forth, refraining from making charges against banks that they otherwise would make; making loans at a 2 percent rather than a 3 or 4 percent rate—constitute indirect payments of interest under the broad language of the statute. Accordingly, the Board recommended that the words "directly or indirectly, by any device whatsoever," be deleted from the statute anr that a "payment of interest" be defined as including only cash payments made, or credits given, by a bank for the account or benefit of a depositor. The Board believes that such a change would carry out the basic purpose of the statute and at the same time make it more workable.

The second objective of the Board's proposal on this subject is to make clear that the same rules as to what constitutes a payment of interest on deposits should apply, as Congress obviously intended, to member banks and nonmember insured banks alike. In applying the present law, the Board has ruled that absorption of exchange charges by member banks is a payment of interest, whereas the Federal Deposit Insurance Corporation has taken the opposite position with respect to nonmember insured banks. As a result, member banks in some sections of the country have been placed at a serious competitive disadvantage with respect to nonmember insured banks, and the check collection process has been slowed up by the unnecessary circuitous routing of checks drawn on nonpar banks. If the law were amended as suggested by the Board to define interest as including only cash payments or credits, the Board believes that absorption of exchange would come within that definition. However, in order to remove any doubt on this question, the Board recommended last fall, and continues to recommend, that the law be amended either by including an explicit statement with respect to absorption of exchange charges by both member and nonmember insured banks, or by authorizing the Board or the Federal Deposit Insurance Corporation to define "interest" for both classes of banks.

Senator ROBERTSON. Most of the testimony is that they wanted all banks to be on the same basis, but with respect to the absorption of exchange they favor the recommendation of express language in the bill, so that there will not be any ifs, ands, or buts about what it means.

Mr. ROBERTSON. I think that is fine.

Senator ROBERTSON. You may proceed.

Mr. ROBERTSON. In this connection, the Board wishes to make clear that its proposal on this subject is not intended to force "par clearance" upon those banks that now charge exchange. The Board's proposal relates not to the making of exchange charges but to the absorption of such charges as a means of paying interest on deposits; and the purpose of the Board's proposal is simply to make the same rules applicable to all insured banks and to preclude situations in which nonmember insured banks are permitted to absorb exchange while competing State and national member banks are not allowed to do so.

TITLE I (NATIONAL BANK ACT)

Turning now to title I of the committee print relating to national banks, the Board recognizes that the changes in law which would be made by that title are matters primarily within the jurisdiction of the Comptroller of the Currency. Certain of these changes, however, are of concern to the Board because of their possible effect upon the soundness of the banking system.

Sections 20 and 21 of title I would permit national banks to issue preferred stock and capital notes and debentures under certain restrictions. In the past, the issuance of preferred stock and capital notes and debentures has been authorized only as an emergency measure. The Board questions the desirability, without further study, of authorizing national banks to issue such stock except in emergencies. It has even greater reservations as to the proposed authority for nonequity capital notes and debentures, since, although they may be subordinated to deposits, they are difficult to distinguish from deposits on which interest is limited by law. The Board suggests that this authority should be stricken from the bill, along with the reference thereto contained in section 37 (h). In any event, if this should not be done, the authority should be limited to emergency situations.

Senator CLARK. May I ask a question on that point?

Senator ROBERTSON. The Senator from Pennsylvania.

Senator CLARK. Governor, could you tell us why you object to the issuance of voting preferred stock for nonemergency purposes as a legitimate method of raising additional capital, which is available to all industrial corporations? I can see the objection for notes and I agree with you on that. I can see the objection to nonvoting preferred stock. But what would be the objection to a preferred stock which had equal voting rights with common?

Mr. ROBERTSON. I would say that the objection, as I see it, Senator, would be that over many, many years the capital structure of national banks has been kept very simple. It can be understood by anybody.

It does not require an expert to analyze the capital structure of a national bank.

Senator CLARK. Do you not think the spread of education in the high schools and common schools would make it possible for people to understand it?

Mr. ROBERTSON. It is very possible, but having sat on the opposite side of the desk from many bankers, over the past quarter of a century, trying to get them to increase their capital and trying to analyze the way in which they have done it, I have been very much impressed with the difficulties which I think would exist if a national bank were to have issued preferred stock, not in an emergency, but in the regular course of events, and then find itself in a position where it had to increase its capital further. It is very probable, in my opinion, that it would find it difficult to issue more common capital. It would find it difficult to issue more preferred stock unless the new issue was made even more preferred. As a result I think it is very possible that the ease with which banks can raise new capital in order to meet the growth of their communities would be diminished through that method. The ease would diminish.

Senator CLARK. Why would that be any more true of a bank than of an industrial corporation?

Mr. ROBERTSON. An industrial corporation has much greater facility for distributing its shares of stock than a bank. Banks as a whole—large ones do not fall in this category—but banks as a whole find their stock is pretty much limited to a group of local people. That is not true of Chase and the First National City of New York. The newcomers in the field of stock ownership in national banks in most communities or in the great majority do so because of the influence of friends, and not because they analyze a bank and say it is going to be a profitable investment. As a result I think you have a very different problem in the case of banks than ordinary corporations.

Section 26 (c) of title I would have the effect of eliminating the present mandatory requirement for cumulative voting in elections of directors of national banks, but would permit cumulative voting if so provided in the bank's articles of association. Cumulative voting is based on the principle of permitting due representation of minority shareholders on the board of directors; and the principle has been applied to elections of national bank directors since 1933. The Board believes the principle is sound and questions whether the proposed change should be made unless Congress is satisfied that cumulative voting has produced undesirable results so great as to outweigh the obvious justice of giving proper representation to minority interests.

Senator ROBERTSON. Governor, I may ask you there if you heard or read the testimony given a few years ago by a Pennsylvania banker who outlined the history of cumulative voting in 1933? Are you familiar with that?

Mr. ROBERTSON. I am sure I have read it sometime.

Senator ROBERTSON. Do you know why Senator McAdoo had that put in the Banking Act of 1933?

Mr. ROBERTSON. Yes; I have read that testimony, Senator, but I am not really convinced that that is right.

Senator ROBERTSON. What do you mean, "It is not right"? Do you mean he did not put it through to get Mr. Gianini on the board up in

New York, or do you mean that it was all right for Gianini to get a special order to get on the board?

Mr. ROBERTSON. No. I mean merely to say that the testimony was secondhand hearsay and I am not sure that that was the real motivating influence behind this legislation which Carter Glass put into the act in 1933.

Senator ROBERTSON. Well, he is dead now and we cannot call him to refute that, or challenge it, but you do not challenge the fact that Gianini was active up there; would you?

Mr. ROBERTSON. No. I would not question it.

Senator ROBERTSON. And that he finally did get on the board of the bank that he wanted to get on, but he found it so unpleasant that he finally decided to give up as a New York banker and confined his activities to the west coast, where he finally became the biggest bank in the world.

Tell us in all sincerity if there was only to be one action taken under that and it was to help Mr. Gianini of California to get on the board of a bank in New York, where nobody on the board wanted him, do you think that that is a proper protection of minority rights, or was that a smooth device to help an ambitious banker?

Mr. ROBERTSON. Well, Senator, I think I would have to answer that on the basis that I am not so much interested in what use he made of the statute, as I am in the principle of cumulative voting—the principle of permitting minority interests to be represented on the board of directors of national banks. I have seen a great number of these cases and I have never seen a case where there was real abuse of this. I have heard allegations of it, and maybe it is true, but I have also seen a number of cases where one who was not desired did get on the board of directors, and did make that board of directors consider problems which they should have considered, and as a result the bank was benefited by it.

Senator ROBERTSON. As I recall it, this is the same recommendation that your Board gave us on my bill last year on this subject?

Mr. ROBERTSON. That is right, sir.

Senator ROBERTSON. It was not an unqualified disapproval. You said then, as you say now, unless we think that the undesirable results outweigh the possible good, we should not change it. We did not have any evidence of the good, but we had plenty of the bad. That has been the same thing here, except that the two witnesses who appeared and wanted it, said from their standpoint what they were doing was plenty good. But then the Comptroller of the Currency testified and said he did not know of any instances where this had promoted the fundamental justice and rights of the minority, but he knew of many instances where it had been abused and, therefore, was strongly of the opinion that this law should be changed and left to the Board to change it, if they thought they did not want cumulative voting.

The Senator from Pennsylvania.

Senator CLARK. Mr. Chairman.

Governor, yesterday we had a little colloquy with Mr. Gidney, the Comptroller of the Currency, in which Senator Douglas, who unfortunately cannot be here at this time, raised the position which you just indicated. As it developed, the Comptroller's view was that it was wise and sound from a banking point of view, and I think I am quoting him correctly, that we should follow a sort of trustee process in the selection of directors of national banks. That is to say, those on the Board, generally speaking, know best. They should select who would fill in any vacancies, and that the process of stockholder elections tended to be disruptive and created dissension within the Board, which was perhaps unfortunate.

I raised a slight eyebrow on the Comptroller's point of view and I gather you do not share that point of view, either.

Mr. ROBERTSON. I certainly do not share it.

Senator CLARK. Thank you.

Mr. ROBERTSON. It seems to me if you do you might as well take away the power to vote with shares and give it solely to the directors. You make a club out of it instead of a business corporation.

Senator CLARK. We think alike. I commented yesterday that perhaps the board of directors of a bank is not quite the same thing as a club.

Mr. ROBERTSON. Section 31 of title I contains a provision which would authorize national banks to grant stock-purchase options to their employees. The Board recognizes the advantages which stock-option plans might have in enabling national banks to recruit and maintain high-caliber personnel. The requirement of the bill for approval by the Comptroller of the Currency of the terms and conditions of such options would help to prevent possible abuses, although it is possible that the last sentence of the new provision might authorize a bank's directors to override any terms or conditions prescribed by the Comptroller of the Currency with respect to the consideration for the issuance of such options. The Board suggests that, at least with respect to some banks, the application of the proposed authority would not be compatible with the public interest. Some banks might be encouraged by this authority to develop unduly profit-minded, expansion-minded managements. Even though employees' stock-option authorizations may be appropriate for other types of corporations, the Board questions whether they are appropriate in the case of commercial banks which are quasi-public institutions entrusted with other peoples' money. At any rate, the Board believes that the statute should include more specific limitations on the terms and conditions under which the options may be granted. We suggest that the provision should be dropped from this bill and made the subject of separate legislation after a period sufficient to permit careful study of both the merits of such an authorization and the limitations which should be placed on its use.

Senator CLARK. Could I ask what I hope will be my last question this morning?

I wonder, Governor Robertson, whether you are concerned, as a number of the other witnesses have been, about the ability of our banking system to recruit adequate executive personnel, and their feeling that since we have a deficit ability in this country in practically every field of endeavor today because of the enormous expansion of our economy, whether the banks do not need, as a competitive weapon to gather their fair share of ability, this kind of stock option provision which is available to almost every other field within the private economy where a young man coming out of school or college is making up his mind as to what career he will follow.

Mr. ROBERTSON. I am sure that is true. I am sure that the banks of this country need some method of attracting better talent than they get today; a higher percentage of the top students of the business schools of the country, for example. I am just not sure that the stock option proposal is the one by which to do it. I would hate very much today to see banks motivated solely by profit. They should not be trying to expand loans for profit. They must have a much greater public interest than a private interest.

I am afraid that the stock option proposals, just like the profit-sharing plans in banks, might develop into a profit motive expansion type of management.

Senator CLARK. Of course, before this committee you would never suggest that the representation in Congress and the Senate is inadequate because of the failure of any such system?

Mr. ROBERTSON. I certainly would not.

Senator ROBERTSON. Governor, is it not a fact that if the banks are to have means of attracting the highest type of young men and holding them, they have to pay them someway?

Mr. ROBERTSON. Oh, yes; they do. They should.

Senator ROBERTSON. Is it not a fact that the pay of the banks in the past has been notoriously low?

Mr. ROBERTSON. In the past it has been. But it has gradually come up and they have made great progress in the last few years.

Senator ROBERTSON. Is it not a fact that all corporations except banks have the privilege of stock option?

Mr. ROBERTSON. Yes. I think that is true.

Senator ROBERTSON. Is it not a fact that 40 percent of the corporations represented on the New York Stock Exchange use that device?

Mr. ROBERTSON. I am sure that is true, also.

Senator ROBERTSON. I have been astounded sometimes at what the officers of a corporation can get as a bonus in the way of a stock option. They get stock, and unless it goes up they do not buy it. If they do buy it and do not want to hold it they can sell it after 6 months and take a capital gains tax, and it is a tremendous income for them.

Mr. ROBERTSON. There have been abuses.

Senator ROBERTSON. There would not be any such duplication in a bank that I know of. Even the Bank of America, or Chase Manhattan. They could not give such things, but I was rather intrigued by the recommendations of our Advisory Committee about this privilege. When we come to mark up this bill, the chairman, acting on the advice given yesterday by the Comptroller, and your advice today, will recommend to the committee that additional safeguards be thrown around this provision.

Mr. ROBERTSON. Thank you.

Section 36 of title I would permit a national bank to make real-estate loans in a total amount up to 20 percent of its demand deposits if that amount were greater than its capital and surplus or 60 percent of its time and savings deposits, the alternative limits provided by present law. Since 1913, the aggregate limitation on real-estate loans has been increased on two occasions, once in 1927, and again by the Banking Act of 1935; but Congress has consistently considered it advisable to relate these limitations to the amount of the permanent capital structure of national banks or the amount of their time deposits. It has always been felt that demand deposits are an unsuitable basis for real-estate loans, and that the aggregate amount of such loans should be based either on the magnitude of the equity cushion in the bank (i.e., capital and surplus) or on the amount of its time deposits which are less likely than demand deposits to be withdrawn suddenly in large volume. The Board does not believe there has been such a substantial change in banking conditions as to justify using demand deposits as a basis for long-term real-estate loans, and therefore would oppose the proposed change.

I might add at that point, there are very few banks in the United States which could benefit from this proposal.

Senator LAUSCHE. May I ask you whether it is your opinion that by the adoption of this proposal you would be sliding back into the situation where loans, frequently perilous, might be made, and thus return to the situation which prevailed back in 1929 and 1930?

Mr. ROBERTSON. I rather doubt it, Senator. I do not think that the loans would be made perilously, but they would be illiquid. To some extent, yes, like 1929 and 1930. Not because loans would be bad, but because they would be illiquid and frozen and the banks could not dispose of them.

Senator LAUSCHE. Following the crash of the twenties it was deemed advisable for the purpose of guaranteeing liquidity, not to go beyond certain measures in the making of real-estate loans.

Mr. ROBERTSON. Long-term real-estate loans. That is true.

Senator LAUSCHE. Your recommendation is intended to avoid what took place in the crash and to adhere to the judgment that was reached based upon the experience of the crash?

Mr. ROBERTSON. I would agree with that completely.

Senator BENNETT. Was it possible prior to 1930 to make real-estate loans on the basis of demand deposits? This rule has not been changed, has it?

Mr. ROBERTSON. No. This particular rule has not, but the same percentage which is now authorized by law was in force at that time.

Senator BENNETT. That is right.

Mr. ROBERTSON. And those particular loans did turn out to be frozen loans and were illiquid. This would merely expand it.

Senator BENNETT. That is right, but there was no change in the rule after that experience. To say it another way, the rules were not different before that experience. We have just continued the same rules and it would be possible again to create the situation of lack of liquidity under the present set of rules if a similar set of unfortunate circumstances should return.

Mr. ROBERTSON. With one exception, Senator. Today the Federal Reserve Banks are in a position to unfreeze those frozen loans, whereas they were not at that time.

Senator BENNETT. That has nothing to do with the percentage.

Mr. ROBERTSON. No, but you should not put a greater burden on the Federal Reserve System by relaxing this provision.

Senator BRICKER. As I remember 1929, the banks were not in the real-estate loaning business in the sense they are at present.

Mr. ROBERTSON. Not to the extent they are today. Originally, of course, commercial banks were not in the real-estate loan business at all.

Senator BRICKER. That is right.
Senator MONRONEY. Those demand deposits would include, would they not, the deposits from correspondent banks?
Mr. ROBERTSON. As the bill is now drafted I think that is true.
Senator MONRONEY. In other words, in case of any tightness or emergency then demand deposits related to the deposits from other banks would apparently be withdrawn at a very rapid rate.
Mr. ROBERTSON. Yes. Very fast.
Senator MONRONEY. Which would leave you a very unstable base if you were figuring just demand deposits.
Mr. ROBERTSON. But in my judgement demand deposits are not a suitable basis for long-term real-estate loans. When you think in terms of 20 percent of demand deposits, the ordinary bank today has liquid assets up to 40 percent, which means 60 percent of its deposits are loans and non-Government securities. If you say 20 percent of that, or one-third, can be long-term real-estate loans, you really have a mass of illiquid assets.
Senator ROBERTSON. Governor, you will recall that one of the problems we had to consider last November was the allegation of the commercial banks that the savings and loan associations were giving them tough competition.
Mr. ROBERTSON. That is right.
Senator ROBERTSON. What is the difference in the tax structure of a savings and loan association and a commercial bank?
Mr. ROBERTSON. I am not a tax expert, but it is very different. The savings and loans do have a greater benefit.
Senator ROBERTSON. Let me develop our theory. There is a difference in the tax. What is the difference in the privilege of lending money? What percentage can one lend, and what percentage can the other lend?
Mr. ROBERTSON. The liquidity ratio of the savings and loan, of course, is much lower than the commercial banks'.
Senator ROBERTSON. That is it. In other words, of the money they have with them savings and loan associations can lend a larger percentage than the banks?
Mr. ROBERTSON. They do.
Senator BRICKER. That is practically their only business, though.
Mr. ROBERTSON. That is right.
Senator ROBERTSON. But we had the recommendation of our advisory committee that this would be one way to help the banks equalize the competition. However, you say it would not help many of them. About how many do you think it would help?
Mr. ROBERTSON. Senator, to be very honest, I must say I know of only one bank in the country this would help.
Senator ROBERTSON. That is so unusual you had better name the bank then.
Mr. ROBERTSON. I would be reluctant to name the bank. If you insist, however, I will.
Senator ROBERTSON. If it would be anything to the discredit of the bank I would not mention it. I thought there would be at least 100 banks.
Mr. ROBERTSON. I would be very surprised if you find a half a dozen banks.
Senator ROBERTSON. That is all?

Mr. ROGERS. Is one of the banks in the District of Columbia?

Mr. ROBERTSON. Yes, it is.

Senator ROBERTSON. We will not pursue that then.

Senator DOUGLAS. Why not?

Senator ROBERTSON. It might be embarrassing to the bank.

Mr. ROBERTSON. I do not think it would be appropriate to mention the bank.

Senator ROBERTSON. Anyhow, it was recommended to us and approved by the Comptroller.

Mr. ROBERTSON. I understand.

Senator ROBERTSON. Since I am just a layman, I put it in the bill, but you think it ought to come out?

Mr. ROBERTSON. I do.

Senator LAUSCHE. Are you willing to express an opinion on the soundness of the rights granted to building and loans and the preferential position on tax rates?

Mr. ROBERTSON. I am not really an expert on that, Senator. I do not think what I could say would be of great help to the committee.

Senator LAUSCHE. My view would be that if those institutions are granted rights which are not sound, it would be better to withdraw those rights than to lower the restrictions and the securities that are provided for banks.

Mr. ROBERTSON. As a principle I would certainly agree with that.

Senator MONRONEY. Would you make any distinction between the dangers of 20 percent on long-term real-estate loans and that on merely construction loans?

Mr. ROBERTSON. Oh, there is a big difference between the two, because the long-term real-estate loan is the one that becomes the frozen asset. The construction loans ordinarily are made by a bank but they are to be taken out by insurance companies or other intermediaries, as soon as the building is constructed.

Senator BRICKER. That would compare with short-term commercial loans.

Mr. ROBERTSON. Yes, it would.

Section 37 would increase the maximum limit on a national bank's total indebtedness from 100 percent of its capital stock to 100 percent of its capital stock and surplus. The advisory committee recommended that the debt limit be increased to make it less restrictive with respect to borrowings from correspondent banks. However, the increased limit provided by the bill (which, for national banks in the aggregate, would be a dollar amount 2½ times the present limit) would apply to all types of borrowings that do not fall within one of the several excepted types enumerated in the statute. In the Board's opinion, such a considerable expansion in the borrowing ability of national banks would be both unnecessary and undesirable.

Borrowing by banks occasionally is necessary and desirable in limited amounts and for limited periods in order to avoid asset liquidation that might otherwise be necessary. It is not, however, a practice that should be encouraged, because it tends to dilute the cushion of protection provided depositors by bank capital and surplus.

Banks should follow a practice of maintaining holdings of liquid assets adequate to meet ordinary needs. Enlargement of borrowing limits as proposed in this bill might encourage banks to hold smaller amounts of liquid assets and rely upon borrowing for needed adjustments. In an emergency requiring large-scale and extended borrowing the discount facilities of the Reserve banks are readily available. To enlarge the ability of national banks to borrow outside the Reserve banks would diminish the restraining influence that the Reserve banks are directed by law to exert upon borrowing banks which are making undue use of bank credit for speculative purposes.

Section 50 of title I would make reports of examinations of national banks and related correspondence confidential documents privileged against disclosure without the Comptroller's consent.

The Board concurs in this proposal but believes that it would be highly desirable to include in title II a comparable provision regarding the confidentiality of examination reports of State member banks.

To have it in one place and not in the other might cause some doubt on the other.

TITLE III (FEDERAL DEPOSIT INSURANCE ACT)

Section 23 of title III would expand provisions of existing law relating to bank mergers so as to require prior approval by the appropriate Federal bank supervisory agency for every merger or consolidation involving insured banks, with a specific requirement that the Comptroller, the Board, or the Federal Deposit Insurance Corporation, as the case may be, shall consider not only the usual banking factors but also whether the proposed transaction would unduly lessen competition or tend unduly to create a monopoly. The supervisory agency would be required to consult the other two Federal banking agencies on the question of competition and would be authorized to request the opinion of the Attorney General with respect to that question. In the Board's opinion, such an amendment would fill a gap in provisions of present law and would serve to insure consideration on a substantially uniform basis of the impact of bank mergers upon competition in the banking field. As the committee is aware, a bill along these lines which was passed by the Senate last year received the endorsement of all three of the Federal bank supervisory agencies.

It is noted that under section 6 of title III a single Administrator would replace the present Board of Directors of the Federal Deposit Insurance Corporation and that section 7 provides for an Advisory Board which would include the Chairman of the Board of Governors or his designee. Since the proper discharge of the important functions of such an Advisory Board would make heavy demands on the time of its members, we doubt the desirability of requiring Government officials to assume this added responsibility; and in any event, we seriously question whether it would be desirable or advisable for the Chairman of the Board of Governors or his designee to serve as a member.

Senator BENNETT. Mr. Chairman, it seems to me Governor Robertson may have missed the heart of this particular problem, which is the question of whether it would be advisable to continue the present Board or to repose all of its authority in one single man. Do you have any comments on that particular phase of the question?

Mr. ROBERTSON. The Board has not considered this because it did not think it was quite appropriate to make recommendations, but I have no reluctance to say, as I said at the last meeting, that I think if what you want is pure efficiency in executing these laws, you should take one man. If what you want is the best judgment you can get and different points of view focused on the same problem, then you should use a board.

This is obviously an attempt to get in the middle; you have efficiency on one side and an advisory committee on the other side. The advisory committee can serve a very worthwhile purpose if you get outside people, that is, people not in public life, but in private life, just as we have a Federal Advisory Council to bring to our Board, for example, the benefit of the viewpoints from throughout the land. But to do as this does and to compose an advisory council made up of a group of Government officials would mean that they would be located in Washington too, and their points of view would not be greater.

Senator BRICKER. You mean they would be probably much more limited.

Mr. ROBERTSON. Either way you want to take it. It would require a tremendous amount of time for one to encompass the entire operations of the Federal Deposit Insurance Corporation and really make a contribution.

Senator BRICKER. Your objection to a member of the Board of Governors serving as a member of the advisory committee would apply with much stronger force against the Comptroller sitting as a member of the Board, would it not? Which is the situation you have at the present time.

Mr. ROBERTSON. Of course, personally I do not think the Comptroller ought to sit as a member of the Board.

Senator BRICKER. That is what I said. The same logic or reasoning that you apply would apply much more strongly against the Comptroller sitting as a member of the Federal Deposit Insurance Corporation Board.

Mr. ROBERTSON. Yes. I think it is impossible for anyone who does a full-time job such as the Comptroller of the Currency, to encompass the whole operation of the Federal Deposit Insurance Corporation and sit over there 1 day a week, or a half a day 2 times a week, and really do a job. It is almost impossible.

Senator ROBERTSON. In that connection, he has asked for another deputy and the power for the deputy to act when he could not make it.

Mr. ROBERTSON. That is about the only way to do it.

Senator ROBERTSON. Governor, we have four different plans. We have a tentative plan in the tentative bill of one man with an advisory board with no real power. We have the existing plan of 3 men with 1 ex officio. We have a proposal of three men and no ex officio. Then we have an alternative that I believe you suggested last November, of a 5-man Board with 3 ex officios—the Comptroller, the Federal Reserve Board and some State official.

Mr. ROBERTSON. Someone else made that recommendation, Senator, but it is in there.

Senator ROBERTSON. Anyway, you did suggest a five-man Board as a possibility, as I recall it, last November.

Mr. ROBERTSON. I do not believe so, Senator Robertson.

Senator ROBERTSON. I am sure you remember better what you said than I do. I know you discussed this.

Mr. ROBERTSON. Yes, I did.

Senator ROBERTSON. You said if you want or if you had a super-duper man and wanted a high degree of efficiency then let one man handle it. If you want the assurance of wide judgment and discretion then you had better have a board.

Mr. ROBERTSON. That is exactly true.

Senator ROBERTSON. Of the four which have been proposed, which do you prefer? If that is too embarrassing, I do not want to press you, but that is a decision we have to make. I have given you the facts which will be before us on February 25 when we mark up the bill. One man with an advisory board with no real power; 3 men with 1 ex officio; 3 men with no ex officio or a 5-man board with 3 ex officios.

Mr. ROBERTSON. I would like very much, Senator, not to make a choice between those without giving it some real thought and maybe even carrying it back to the Board and getting all the benefit of their views, sir.

Senator ROBERTSON. When one of the old Hebrew prophets was asked to rule over all of Israel he said, "For 7 days I sat where they sat."

You can think about this and come and sit where I am sitting and tell me privately what you want to.

Mr. ROBERTSON. Very well.

Senator BENNETT. And he has approximately 7 days.

Senator ROBERTSON. Which will give you a chance to take a long look at it.

Does the Senator from Illinois wish to ask any questions on this?

Senator DOUGLAS. My attention was diverted for a moment. Do I understand that you are opposed to a one-man administrator?

Mr. ROBERTSON. No.

Senator DOUGLAS. You are not?

Mr. ROBERTSON. No; I have not expressed opposition to anything except the idea of the Chairman of the Federal Reserve Board sitting as a member of this advisory committee.

Senator DOUGLAS. You have no opinion as to whether it should be a one-man administrator or not?

Mr. ROBERTSON. That would be encompassed in this problem that I have 7 days to think over.

Senator DOUGLAS. As I remember it, you were the First Deputy Comptroller?

Mr. ROBERTSON. Yes, sir.

Senator DOUGLAS. Many of us thought you did most of the work of the Comptroller, Mr. Robertson, when you were over there.

Mr. ROBERTSON. You are probably very wrong.

Senator DOUGLAS. You are certainly highly experienced in the work of that office.

Do you think we should continue with a one-man Comptroller of the Currency, or should we have a board to serve as Comptrollers of the Currency?

Mr. ROBERTSON. I would be very much opposed—I can see where I am getting myself to—I would be opposed to a board in lieu of the Comptroller, because I think that the operation can be much more efficient through a one-man operation. I would hope that the one man was always good.

Senator BRICKER. He generally has been.

Mr. ROBERTSON. That is certainly true, in that operation. I would not want to face the next question you are going to ask.

Senator DOUGLAS. The next question is going to come immediately and you will have to face it.

Mr. ROBERTSON. All right.

Senator DOUGLAS. If you think that a one-man administrator is better for the supervision of national banks, why is not one man better for the insurance functions and the supervision of State banks not under the Federal Reserve?

Mr. ROBERTSON. I wonder if I can answer your question by going way beyond what our Board would maybe approve, but express only a personal point of view? This is not going to be a very popular statement, but I am going to make it. In the bank supervisory field I think the ideal setup would be to have a board making the rules and regulations so that you would have a variety of points of view focused on it; that that board would have nothing to do with carrying out those laws, insofar as bank supervision was concerned. You take away from the Board of Governors, for example, any power of bank supervision. The execution of the laws and the regulations would be through agencies. If it be insurance, there would be a pure insurance agency on one side, and a pure supervisory agency, and a pure regulatory agency, on the other side. You still have three agencies. The insurance agency would be one man because all it would be doing would be executing the laws and not making rules and regulations. The same would be true with respect to supervision because it would not be making rules and regulations and would not be making broad policy decisions, but would be executing those laws. That would be a one-man operation. That is the way I would do it if I had to start from scratch, but, of course, you know we have had a much different setup through the years.

Senator DOUGLAS. Let me see if I understand your outside ideas on this point. Are you saying there should be one commission to have quasi-legislative powers over what is now the Federal Deposit Insurance Corporation and what is now the Office of the Comptroller of the Currency, and then there would be an administrative head for examination and an administrative head for insurance and an administrative head for certain other functions?

Mr. ROBERTSON. Quite unrelated to this one agency.

Senator DOUGLAS. I presume one administrative head over these three administrative heads?

Mr. ROBERTSON. No. Not at all. With respect to the first agency you speak of, I think it should carry out only the functions delegated to it by Congress, and not be a quasi-legislative branch in that sense. I think it should be purely an administrative agency carrying out whatever will the Congress expresses. The other two would be merely changed into, one, a supervisory agency, and the other an insurance of deposits agency, each being operated by a head—a one-man operation. Whether they are agents of Congress or of the executive branch of the Government I have no view.

Senator ROBERTSON. Governor, you are sort of outlining a blueprint for the Monetary Commission.

Mr. ROBERTSON. That is right. It is way beyond this particular bill.

Senator ROBERTSON. It is way beyond what we are trying to do.

Mr. ROBERTSON. I think so.

Senator BRICKER. That theory has been adopted before.

Mr. ROBERTSON. Yes; it has.

Senator BRICTKER. It is something similar to what we have in the CAB and the CAA.

Mr. ROBERTSON. I understand that is true. I am not familiar with it.

Senator ROBERTSON. You may proceed.

TITLE IV (FEDERAL HOME LOAN BANK ACT)

Mr. ROBERTSON. The provisions of title IV of the committee print have no material relation to the principal functions of the Federal Reserve System. There are two points, however, with respect to which the Board would like to comment briefly.

Section 15 of title IV would make obligations of Federal home-loan banks eligible for purchase by any "agency or instrumentality" of the United States. In the judgment of the Board, it would be undesirable for the Reserve banks to be authorized to acquire obligations of the Federal home-loan banks. The language of the bill could conceivably be construed as authorizing investments in such obligations by the Federal Reserve banks, because they are certainly instrumentalities of the United States, as I see it. It is assumed that this result was not intended by the provision in question; but if there should be any doubt in this respect the Board recommends that the provision be appropriately clarified.

Senator ROBERTSON. This was a recommendation of the Federal Home Loan Bank Board.

Mr. ROBERTSON. Yes.

Senator ROBERTSON. It was submitted to our advisory committee and they approved it. I do not know, of course, whether the Bank Board had in mind members of your bank buying their securities or not. If you did not like them you would not have to buy them; would you?

Mr. ROBERTSON. No. We would not have to buy them, but it would seem a little doubtful that you should give status to certain obligations by providing they could be purchased by Federal Reserve banks, because we do not think we should buy them.

Senator ROBERTSON. What language do you think there ought to be in there to indicate we did not include you?

Mr. ROBERTSON. If you merely said, "with the exception of Federal Reserve banks" for example, it would do it. I could find more appropriate language and submit it to you if you like.

Senator LAUSCHE. Would you give me the reasons which support your statement that you deem it inadvisable for a Federal Reserve bank to buy these obligations?

Mr. ROBERTSON. Yes. We think a central banking function should be carried on through the kind of obligations that are the nearest thing to money.

Senator BRICKER. The nearest thing to what?

Mr. ROBERTSON. The nearest thing to money. Those obligations would be Treasury bills because they are the shortest term obligations. The moment you get into longer term obligations and the moment you are dealing in that kind of obligation, whether it is the Home Loan Bank Board or long-term Government bonds, you are forcing all the people who deal in those securities to guess against the Federal Reserve, which is impossible, and as a result you disrupt the market in those securities. You get away from a free market.

Whereas when you deal in bills—the things nearest to money—you disrupt it as little as possible.

That is the reason why we think the central bank should not be engaged in buying long-term obligations. We are not trying to cast aspersions at these particular obligations.

Senator ROBERTSON. But it would help the commercial market for those bonds if you were not one of the buyers. Is that your position? It would help it if you were eliminated?

Mr. ROBERTSON. If we did not engage in buying. Yes. The market would be better off than if we were in that field.

Senator ROBERTSON. All right.

Senator BRICKER. Somewhat the same position as regards commercial loans.

Mr. ROBERTSON. Yes. That is true.

Section 17 (c) of title IV, dealing with the authority of the Federal Home Loan Bank Board over its financial transactions, expenditures, and personnel, provides that it shall have the same powers and authority in this respect as are presently vested in the Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation. The existence of such a cross-reference would mean that if the relevant provisions of the Federal Reserve Act or of the Federal Deposit Insurance Act should be changed, it would be necessary to consider whether the provisions of the Federal Home Loan Bank Act should be similarly altered. The Board of Governors believes that any such description of the authority of the Federal Home Loan Board in these matters should be self-contained, without any cross-reference to the Board of Governors of the Federal Reserve System.

SECTION 803

Finally, the Board wishes to comment specially on section 803 of the committee print which would substantially revise and expand sections 217 and 218 of the Criminal Code relating to bank loans and gratuities to examiners. In brief, these provisions would be extended to prohibit (1) gifts by member banks to any officers or employees of the Board of Governors or the Reserve banks; (2) the making of loans or offers of employment by member banks to any employees of the Board or the Reserve banks who may have performed any duties in connection with the member bank in the preceding 2 years; and (3) the making of loans or offers of employment to any other employees of the Board, even though they had performed no duties in connection with the bank, unless the written approval of the Board is first obtained in each case.

Senator ROBERTSON. I may interrupt to say those sections we had amended, sections 217 and 218, will be changed some from the way they appear in the committee print.

Mr. ROBERTSON. That being so, I think I could omit reading the next two pages and save the committee some time.

Senator ROBERTSON. The committee had a lot of witnesses testify about this and they agreed it was a little too drastic. As far as the chairman is concerned he is going to propose we try to soften it so we do not make it too difficult for the examining services to get good men to enter those services, and to try to make it fair for those men who have been employed by these services, and who have an opportunity with a private bank, to take it.

We think there should be some restrictions. I believe the Comptroller said that the agencies should have the power to issue regulations, and he suggested that nobody should take a job within 2 years after examining a bank, with the bank which he examined, except with the approval of the agency concerned.

However, those matters are going to be considered and it will not be necessary for you to testify at length on them. It will go in the record.

(The remainder of the prepared statement of Mr. Robertson follows:)

Such extremely restrictive provisions are not only unnecessary but, in the Board's opinion, would impose a heavy hardship on employees of the Board and the Reserve banks and the other Federal supervisory agencies to which they would also apply. They would handicap the operations of the supervisory agencies themselves and, even more than the conflict of interest provisions of the bill already mentioned, would hinder recruitment of new personnel. The mere likelihood of enactment of these provisions might possibly bring about and exodus of present employees. Restrictions on loans and offers of employment by a member bank to employees of the Board who have performed duties in connection with that bank would have particularly harsh results; and the difficulties of determining the application of these restrictions in particular cases are apparent. The Board employee who dictates a letter regarding a particular member bank, the stenographer who types it, the lawyer who passes on its legal effect, members of the Board who approve it, and the file clerk who files it, may all be performing duties in connection with that bank.

About 95 percent of the employees of the Federal Reserve System are engaged in duties connected with services performed by the system for member banks, such as the collection of checks and the furnishing of coin and currency. All of these employees would be precluded from obtaining loans from, or accepting employment with, member banks.

Equally burdensome and severe would be the restrictions on loans or offers of employment to any employees of the Board regardless of the nature of their duties. Actually, these restrictions as written in the bill, would seem to go so far as to apply to borrowings by a Board employee from a savings and loan association or a Federal credit union. In addition, it seems inconceivable that Congress would wish to impose upon the Board and the other supervisory agencies the administrative burden of passing upon practically all borrowings, including installment purchases, by all of their employees.

For all of the reasons indicated, the Board opposes the proposed revision of sections 217 and 218 of the Criminal Code which would be made by section 803 of the committee print.

In conclusion, Mr. Chairman, we would like to reiterate that we are in complete accord with the objectives of the committee; and, with the relatively few exceptions that have been mentioned, we believe that the committee print constitutes a long step toward simplification of the banking laws. The Board and its staff will be glad to give any assistance that may be desired in connection with your committee's further consideration of this proposed legislation.

Senator Robertson. Are there any questions? We have before us a very well-informed witness if anybody wants to ask any questions on anything in the bill on which we have had some question.

Mr. Robertson. First, could I say I do propose to submit, and I have submitted to the clerk of the committee, a memorandum of some technical comments which you may want to consider or meet. I think there is only one there that would or might fall out of the purely technical category.

Senator Robertson. Without objection the technical suggestions and the full prepared statement of Mr. Robertson may be made a part of the record at the close of his testimony.

We will let the committee counsel ask the witness 1 or 2 questions about these technical changes.

Mr. ROBERTSON. Very well.

Mr. ROGERS. Governor, with respect to No. 3, would not that extend the Federal Reserve System a great deal beyond its present scope?

Mr. ROBERTSON. I do not think so. It would enable us to establish branches, for example, in Alaska, if that were deemed to be appropriate, or in Hawaii, but it would not change the principle of the System at all, and I do not think it would be a matter of substance.

Mr. ROGERS. I always thought that the idea behind the System was that these areas were beyond the benefits of being members of the System?

Mr. ROBERTSON. Oh, no. They obtain real benefits as of today. You have member banks and nonmember banks, but we do not have authority as it is now to establish branches there. Their checks are taken care of and cleared, for example, in Seattle. That is, for Alaska. But, mind you, this act was established at a time when these were very, very outlying Territories. That is not true today. Ten years hence it may be very different.

Mr. ROGERS. On page 2, No. 7.

Senator BRICKER. Could I interrupt for one question? Have you any member banks in Puerto Rico?

Mr. ROBERTSON. No, but there are branches of two member banks there.

Senator BRICKER. How many in Alaska.

Mr. ROBERTSON. I think that there is only one member bank in Alaska.

Senator BRICKER. And how many in Hawaii?

Mr. ROBERTSON. I am guessing, and I will correct it if I am wrong, but I would say two.

Senator BENNETT. The man behind you thinks he has the answer.

Mr. ROBERTSON. I understand now there are no members in Hawaii. The figures on the others are correct.

Senator BRICKER. Thank you.

Mr. ROGERS. On page 2, No. 7.

Mr. ROBERTSON. Yes. That is the one I thought was questionable as to whether it is completely technical or not. This particular suggestion relates to the provision in the bill authorizing the obtaining of reports from member banks on a sample basis. The idea behind that was that we could reduce the number of required reports from all banks, because we do not have to get that information for our purposes 4 times a year, or 3 times a year. If we get it twice from all banks, and then from selected banks during the other two parts of the year you can get the information you need, and thus reduce the burden to all banks.

We thought that the statute still referred to three reports as being mandatory. We think that can be reduced to 2 in keeping with our intention and what we thought was the intention of the committee. So we merely suggested it be reduced to 2.

Also we thought there was another phrase that could be altered. The phrase relates to dividends. We think it should be earnings and dividends, which is the statutory language now in use. These are the two changes.

Mr. ROGERS. I beg to correct you. I do not believe earnings are mentioned in the present law.

Mr. ROBERTSON. Earnings and dividends are included in the report which is filed.

Mr. ROGERS. That is right of the report, but it is not mentioned in the law. Only the dividends.

Mr. ROBERTSON. You may be correct about that. I think it would be better in any event to change it to make it conform.

Mr. ROGERS. The problem there is to develop uniformity between your report and the national banking reports.

Mr. ROBERTSON. If they are not uniform there is no sense in doing this at all.

Mr. ROGERS. The Comptroller apparently, by his testimony yesterday, wanted to keep his requirement for three reports and have no mention at all of the dividends reports.

Mr. ROBERTSON. I think that is probably so. I understand the Comptroller does not want the power to publish earnings and dividends reports. I differ from that because I think it is almost impossible for one to analyze the condition of a bank today on the published statement without seeing what the earnings statement is.

In the corporate field, if you are listed, you have to file a statement with the SEC of your earnings and dividends and expenses, and I see no reason at all why banks should not be subjected to exactly the same thing. This requirement would not require the report to be published but would give us the power to require publication, and I think that is right, and the Comptroller ought to have exactly the same power. But if the committee decides not to do it on one side it should not do it on the other side. You should have uniformity.

Mr. ROGERS. Your theory is that you publish the earnings reports of all banks, or just selected banks?

Mr. ROBERTSON. Oh, no. The earnings and dividends statement would be gotten from all banks and that could be even only one time a year. That is enough and we so state in this.

Mr. ROGERS. I am referring to your publication.

Mr. ROBERTSON. The publication is only with respect to that one. The sample reports would not be on earnings and dividends, and should not be. The sample reports would be information we need with respect to breakdown of loans and investments, which we would need in connection with our work on monetary and credit policy.

Mr. ROGERS. Then you would not object to a provision which would require the reports of all banks to be published, and all on the same date?

Mr. ROBERTSON. Not at all.

Mr. ROGERS. Thank you. I think that is clear in my mind now.

Senator ROBERTSON. Are there any further questions?

Senator DOUGLAS. Mr. Robertson, your Board made a recommendation, which is No. 73 in a special bulletin issued by our committee last October, which says that every Federal Reserve Bank director shall be a resident of the district Federal Reserve bank on whose board he is serving, and should cease to be a director when he ceases to be a resident of the district. This is a complicated bill. At first sight I do not see that provision in the bill.

Senator BENNETT. It has one slight amendment which allows him to live within 50 miles of the bank.

Senator DOUGLAS. I see.

Senator ROBERTSON. That is in recognition of the fact that we are living in the motor vehicle age.

Senator DOUGLAS. Thank you. Now, may I ask about your recommendation on page 80, which, as I understand it, was to remove the tax exemption for dividends on Federal Reserve bank stock issued before 1942, before the Public Debt Act of 1942. What has happened to that recommendation?

Mr. ROBERTSON. That is not in the bill, Senator.

Senator DOUGLAS. I wonder if you would state briefly your reason for your recommendation.

Mr. ROBERTSON. Well, yes. We can see no reason why there should be a differentiation insofar as taxation is concerned between Federal Reserve bank stock which is issued before a certain date and that which is issued after a certain date. We see no reason at all for any differentiation. Now, the opposition is that the statute is there and the taxation is different for that stock which was issued prior to the 1942 date, I think it is, and there is no reason to disturb it. As far as we are concerned, it doesn't interfere with policy matters, it doesn't affect the establishment or execution of monetary policy. It was merely one of those things in the statute for which we could see no real justification, and we recommended it be changed.

Senator ROBERTSON. If the Senator will yield—the chairman decided what was and what was not to go into the tentative bill, and didn't try to analyze this provision very carefully. He just decided as a tax measure it should go to the Finance Committee along with a recommendation that there should be a more liberal allowance for bad debt retirements—reduce taxes of banks. But that is what it is—it is outside of our jurisdiction.

Senator LAUSCHE. May I ask, is the provision——

Senator ROBERTSON. The Senator from Illinois has the floor.

Senator DOUGLAS. That's all right. I will be glad to wait for the Senator from Ohio.

Senator LAUSCHE. Is the provision of which you are now speaking within the law we are contemplating?

Senator ROBERTSON. No; that was in his recommendation of last November, but it was not carried forward into the tentative bill.

Senator LAUSCHE. For my own information, may I ask, how did it come about that there is a differentiation. Was there any reason advanced originally why one should be exempt and the other not?

Mr. ROBERTSON. Only history, I think. It was in the same category as other Government obligations, and on that basis was tax exempt. And then, when the tax exemption was taken off Government obligations, they took it off with respect to any new stock which was to be issued by Federal Reserve banks as well as other Government corporations.

Senator LAUSCHE. Thank you, sir.

Senator ROBERTSON. I think the real answer is the act of 1942 didn't make it retroactive. It may have been an oversight, but that is the law. Maybe it should be changed—but some other committee will have to handle it.

Senator DOUGLAS. Mr. Chairman, there is another recommendation that the Reserve Board made on page 96, the study of banking laws, recommendation No. 72. The Board recommended that the Federal

Reserve banks be authorized to make repurchase agreements with respect to Government securities, and that these be subject to the direction of the Open Market Committee. Now, I am not certain whether this provision is in the bill.

Senator ROBERTSON. That is not in the bill.

Mr. ROBERTSON. That was referred to in my statement before you came in, Senator. We still think it should be be incorporated in the bill. It is not there.

Senator DOUGLAS. I regret that I was late. I wonder if for the sake of the record you would give added emphasis to the reasons why you believe this to be necessary.

Senator ROBERTSON. You may proceed to explain again, because it is a matter in which the Senator from Illinois is much interested.

Mr. ROBERTSON. Repurchase agreements have been used for a long, long time, 25 years, by the Federal Reserve System in attempting to smooth out irregularities in the money market, financing dealers and enabling them to carry securities in order to make markets. Those repurchase agreements are in the form of purchase and sale contracts, but they have many of the characteristics of loans. For example, the yield is always fixed, just like a rate of interest. The statute does not refer to these repurchase agreements. The authority for using them is traditional and is somewhat in the doubtful category. We think it is good. We think all Congress should do is to specifically authorize the use of those agreements, not changing any practice, not condoning anything.

Senator ROBERTSON. With all due deference, we left this out. We were trying to sidestep the big policy questions as much as possible. Is it not true that this would be the opening wedge of a policy decision as to the scope and operations of the Federal Reserve Board, which could more properly be handled by a monetary commission than the brief study that we were able to make?

Mr. ROBERTSON. I really do not think so, Senator. I think this is a very simple matter and is not one in which there would be any differences of opinion, I don't think, anywhere.

Senator ROBERTSON. There is a difference of opinion in the committee. They turned it down.

Mr. ROBERTSON. I think they turned it down because this whole repurchase agreement field, the whole field of financing dealers in Government securities, enabling them to make markets, is under study by the New York Clearinghouse. But I really think that the committee did not think this one through far enough. I think if they had, they would have come out with the conclusion that you do no harm by clarifying it, no matter what decision is made in the future with respect to operations—all this does is to clarify the statutes and make them accord with what has actually been the practice for 25 or 30 years.

Senator DOUGLAS. I would like to ask this question, if I may. You have been moving into this field without specific statutory authority, and no one has questioned it. You have made a recommendation that it be included in the statute so that you may have statutory authority. The advisory committee has turned this down. Unless we put it in the law, may not someone raise the point that you do not have statutory authority and question your ability to operate in the future as you have in the past?

Mr. ROBERTSON. It is possible. I must clarify this by stating that this matter has been questioned innumerable times by those of us within the System. But it has also been justified, time and again, by counsel. They do contend that this is a lawful exercise of powers given to the Federal Reserve System by the Congress. But in order to reach that decision, you have to put together a great many statutes. There is no clear statement. And I think you are right that if it is not put in the statute, now that we have raised it, it will give rise to questions by others.

Senator DOUGLAS. Not necessarily confined to those inside the System.

Mr. ROBERTSON. That is right.

Senator DOUGLAS. It may well be from those outside the System.

Mr. ROBERTSON. That is right.

Senator MONRONEY. Would it not be impossible for the open market operations if the Federal Reserve tried to do it itself, rather than through this purchase and sale?

Mr. ROBERTSON. Well, we could not accomplish the same end without the use of repurchase agreements. We could buy and sell bills and affect reserves. But you could not do it in a manner which would smooth out operations. You have to do it by providing the facilities to dealers so that they can carry portfolios and make markets.

Senator MONRONEY. My question was to make this open market operation truly successful, the only way it can be done is through those why buy and sell on orders from the Federal Reserve, rather than the Federal Reserve itself.

Mr. ROBERTSON. I think that is true. We fould it a very helpful device.

Senator MONRONEY. Unless this is put into the bill, there will be some cloud over the right of the Federal Reserve to engage in open market operations through this channel.

Mr. ROBERTSON. That could be.

Senator ROBERTSON. On the contrary, if we put it into the bill, would not the chairman be inviting a full-scale discussion of open market operations and all we have done in the past, as to what extent the President and the Treasury should compel the Federal Reserve Board to support the financing of the public debt. It seemed to the chairman that as long as you thought you had enough authority already to carry on these transactions, we could leave that to another commission, and we would not inject something that would probably touch off a long debate over policy questions. We did not put any pressure on the advisory committee—we let them make a free choice. They said they did not think it necessary to put it in. But we have the technical language you have suggested. It will be available when somebody wants to put it in—the language will be here and the committee can vote on it.

Senator DOUGLAS. One final comment, Mr. Chairman, that I should like to make. I was impressed with the coyness of the last sentence of Mr. Robertson's statement—

> The Board and its staff will be glad to give any assistance that may be desired in connection with your committee's further consideration of this proposed legislation.

May I say that I frequently have disagreed on matters of policy with Mr. Robertson, and other members of the Board, but I have always acknowledged his great competence and the great competence of the staff of the Federal Reserve System. I suppose I properly should address this to the chairman, and therefore will now do so.

I personally would appreciate it if it could be possible for one of your men, a man whom you regard as most competent in banking legislation, could sit with us as we prepare the final draft of the legislation—not that he should be on top, but that he should be on tap.

Mr. ROBERTSON. Well, Senator, there was nothing coy intended by the last sentence here. The Board and its staff do stand ready to be of any assistance whatsoever. All the committee needs to do is to speak and we will do exactly what we can do.

Senator DOUGLAS. I would like to suggest to the chairman that this offered help would be very valuable, and I say this without any reflection upon the permanent staff of this committee at all. But this is a highly important and highly tricky business, and I think it would be helpful if we had available the best technicians that there are.

I suggest that to the chairman.

Senator ROBERTSON. Any further questions or comment? If not, Governor, we again thank you for your helpful contribution to our studies.

(Mr. Robertson's prepared statement and memorandum of technical comments follows:)

STATEMENT OF J. L. ROBERTSON, MEMBER, BOARD OF GOVERNORS, FEDERAL RESERVE SYSTEM

Mr. Chairman, the Board of Governors is in full accord with the committeee's objective of streamlining the present banking laws; and the committee print which is the subject of these hearings is an admirable step in that direction. For the most part, its effect would be to rearrange provisions of existing law in a more orderly manner, eliminate obsolete provisions, correct technical defects, and clarify ambiguous provisions. At the same time, it would also make a number of substantive changes, and it is to be expected that there may be differences of opinion as to the desirability of some of these changes.

Most of the provisions of the committee print relate to matters which are beyond the Board's jurisdiction and have no direct effect upon the Federal Reserve System. The Board's comments, therefore, are limited primarily to the provisions of title II of the bill revising the Federal Reserve Act and to certain provisions of other titles of the bill which directly affect the System or are of interest to the Board.

TITLE II (FEDERAL RESERVE ACT)

Title II of the committee print would make numerous technical and clarifying changes in the Federal Reserve Act that are obviously desirable and appear to require no special comment.

Most of the changes of substance are in general accord with the legislative recommendations made by the Board to the committee last October and during the committee's hearings in November. These changes include restoration of a requirement for payment of a franchise tax by the Federal Reserve banks to the United States; removal of the present statutory dollar limitation on the cost of Federal Reserve bank branch buildings; provision for rotation in office of Federal Reserve bank directors and of members of the Federal Advisory Council; authority for the requirement of reports from State member banks on a sample basis; a requirement that Federal Reserve bank directors reside within the Federal Reserve district or within a radius of 50 miles of the Reserve bank; authority for the temporary acquisition of bank stock by a member bank in connection with the absorption of another bank; a liberalization of restrictions on loans by member banks to their executive officers; and a limited extension of the authority of foreign branches of national banks to enable them to compete on more equal terms with banks in foreign countries. All of these changes are desirable, in the Board's opinion, as tending to improve and facilitate the operational activities of the Federal Reserve System and its member banks.

The bill contains a new provision which would require annual audits of the accounts of the Board of Governors by a firm of certified public accountants. Another provision would require the Board to take measures to assure that examinations of the Federal Reserve banks meet the highest standards of commercial audits, and the Board would be authorized to arrange for review by certified public accountants of the procedures followed in the examination of the Reserve banks. All such audits of the Board and reports of examinations of the Reserve banks would be required to be transmitted to the Banking and Currency Committees of Congress. As indicated at the hearings held by the committee last November, the Board should favor the enactment of these provisions of the bill.

The bill contains some additional substantive changes in Federal Reserve law which have not been suggested by the Board. To certain of these changes the Board would have no objection; as to others it would have reservations.

The bill would require every State member bank to keep, and transmit to the Board on demand, a full list of its shareholders, and to notify the Board of any purchase or sale of its shares involving 10 percent or more of the number outstanding. The Board believes that these requirements have merit and would not be unduly burdensome.

Investments in bank premises by a State member bank would, under the bill, require the Board's approval only if they should exceed 100 percent of the bank's captial stock or 50 percent of the bank's capital and surplus, whichever might be greater, whereas present law requires Board approval in all cases in which the investment would exceed 100 percent of capital stock. The Board would have no objection to this change.

The bill would have the effect of repealing the present authority of the Reserve banks under section 13b of the Federal Reserve Act to make working capital loans and commitments to business enterprises. The repeal of this authority, which has been utilized very little in recent years, would be in accord with the position heretofore taken by the Board in this matter.

The bill would transfer to the Comptroller of the Currency the present authority of the Board to grant trust powers to national banks and to regulate the exercise of such powers. As indicated at the committee hearings last November, the Board would have no objection to the transfer of that authority to the Comptroller of the Currency.

Section 29 of title II would make certain changes in the provisions now contained in section 30 of the Banking Act of 1933 regarding the removal from office of directors and officers of member banks. A new provision would require that hearings under this section be held in accordance with the Administrative Procedure Act and be subject to review as therein provided and that review by the court shall be upon the "weight of the evidence." Since any such hearings would be subject to the Administrative Procedure Act without this provision, the Board sees no need for its inclusion. Moreover, the provision for judicial review on the weight of the evidence would be a departure from the general rule, as stated in the Administrative Procedure Act, that the reviewing court may set aside agency action if it is "unsupported by substantial evidence;" and the Board would not favor this departure from the general rule.

Section 33 of title II would permit a holding company affiliate to use the reserve of readily marketable assets required by present law for the purpose of making additions to the capital of its affiliated banks as well as for replacement of capital. This reserve was intended to enable a holding company affiliate to come to the aid of its subsidiary banks in times of stress or emergency. If it could be used in normal times for additions to capital in order to enable expansion and growth, the reserve fund might be depleted and not be available at the very time when it would be needed to maintain the sound condition of the subsidiary banks.

The same section contains a new provision which, in a situation in which there are several holding company affiliates with respect to the same bank or group of banks, would permit the statutory reserve to be maintained by only one of such companies to be designated by the Board. The Board would have no objection to this provision if, in order to prevent possible evasions of the law, a proviso were included to the effect that, of the holding company affiliates involved, only the designated holding company affiliate shall own stock of the subsidiary banks in the group.

Finally, as far as title II of the committee print is concerned, the Board would not favor, at least in its present form, the new provision in section 38 (i) prohibiting employees and former employees of the Board or the Federal Reserve banks from accepting employment in member banks except pursuant to regulations of the Board. This provision, which carries heavy criminal penalties, would place an unduly severe restriction on individuals who may have been employees of the Board or the Reserve banks many years ago. If this provision should be enacted, it would undoubtedly increase the difficulty of recruiting qualified new employees. Moreover, we know of no abuses within the Federal Reserve System; and furthermore an appropriate path for employees between banks and the supervisory agencies would, on the whole, be beneficial rather than injurious to the public service and the banking system. The Board sees no need for such a "conflict of interests" provision, but it would not object to the provision if it were made inapplicable to any former employee after a specified period, such as 2 years. At a later point, comment will be made on the even more severe provisions of section 803 of the bill affecting the employment by banks of former employees of the Federal supervisory agencies.

It is noted that the committee print's revision of the Federal Reserve Act does not include provisions to carry out a few of the Board's recommendations. Some of the more important omissions may be mentioned.

For many years, the Federal Reserve banks in connection with their open market operations have utilized repurchase agreements as a convenient and flexible means of helping to smooth out temporary irregularities in the money market. These agreements are in the form of a purchase and sale and they are used only to implement open market policies under regulations of the Federal Open Market Committee. However, they have some of the attributes of a loan and the law now contains no specific reference to such transactions. Accordingly, the Board recommended an amendment specifically authorizing such repurchase agreements; and we continue to believe that such a clarifying amendment would be desirable.

Another of the Board's recommendations omitted from the committee print was that the activities of the Federal Reserve banks as fiscal agents of the United States and of various agencies of the Government should be made specifically subject to supervision and regulation by the Board. Such activities have increased substantially in recent years. More than 3,300 of the System's employees are engaged in fiscal agency activities for more than 25 governmental agencies in approximately 50 different capacities. It has become more and more evident that, in addition to the general authority of the Board to supervise the Federal Reserve banks, there should be some more specific authority for the overall coordination of the fiscal agency operations of the Reserve banks. Such authority would help to prevent Government departments and agencies from requiring the Reserve banks to perform functions which may be inconsistent with their overall purposes and unduly burdensome.

Finally, the committee print does not carry out the recommendations made by the Board on the subject of payment of interest on deposits by member and nonmember insured banks. The bill would make only one change in present law in this respect. At present, the Federal Deposit Insurance Act provides that "the Board of Directors shall by regulation prohibit the payment of interest on demand deposits in insured nonmember banks and for such purpose it may define the term 'demand deposits'." Section 26 of title III of the committee print would change this language to read: "No insured bank shall, directly or indirectly, by any device whatsoever, pay any interest on any deposit which is payable on demand and for such purpose the administrator may define the term 'demand deposits'."

In the Board's opinion, this change would not only be inadequate to meet the problems and inequities which have arisen in this particular field, but would actually multiply the existing difficulties because, while it may not have been intended, the new language would authorize the Federal Deposit Insurance Corporation to define "demand deposits" for all insured banks. In order to avoid any misunderstanding, we should like to restate and attempt to clarify the two objectives of the Board's recommendations on this subject.

In the first place, it has become clear over a period of many years that the present law on this subject is completely unworkable. This has been due to the difficulty of determining whether various services offered by banks to their depositors, such as free parking facilities, special printing of checks, etc., constitute indirect payments of interest under the broad language of the statute. Accordingly, the Board recommended that the words "directly or indirectly, by any device whatsoever," be deleted from the statute and that a "payment of interest" be defined as including only cash payments made, or credits given, by a bank for the account or benefit of a depositor. The Board believes that such a change would carry out the basic purpose of the statute and at the same time make it more workable.

The second objective of the Board's proposal on this subject is to make clear that the same rules as to what constitutes a payment of interest on deposits should apply, as Congress obviously intended, to member banks and nonmember insured banks alike. In applying the present law, the Board has ruled that absorption of exchange charges by member banks is a payment of interest, whereas the Federal Deposit Insurance Corporation has taken the opposite position with respect to nonmember insured banks. As a result, member banks in some sections of the country have been placed at a serious competitive disadvantage with respect to nonmember insured banks, and the check collection process has been slowed up by the unnecessary circuitous routing of checks drawn on nonpar banks. If the law were amended as suggested by the Board to define interest as including only cash payments or credits, the Board believes that absorption of exchange would come within that definition. However, in order to remove any doubt on this question, the Board recommended last fall, and continues to recommend, that the law be amended either by including an explicit statement with respect to absorption of exchange charges by both member and nonmember insured banks, or by authorizing the Board or the Federal Deposit Insurance Corporation to define "interest" for both classes of banks.

In this connection, the Board wishes to make clear that its proposal on this subject is not intended to force "par clearance" upon those banks that now charge exchange. The Board's proposal relates not to the making of exchange charges but to the absorption of such charges as a means of paying interest on deposits; and the purpose of the Board's proposal is simply to make the same rules applicable to all insured banks and to preclude situations in which nonmember insured banks are permitted to absorb exchange while competing State and national member banks are not allowed to do so.

TITLE I (NATIONAL BANK ACT)

Turning now to title I of the committee print relating to national banks, the Board recognizes that the changes in law which would be made by that title are matters primarily within the jurisdiction of the Comptroller of the Currency. Certain of these changes, however, are of concern to the Board because of their possible effect upon the soundness of the banking system.

Sections 20 and 21 of title I would permit national banks to issue preferred stock and capital notes and debentures under certain restrictions. In the past, the issuance of preferred stock and capital notes and debentures has been authorized only as an emergency measure. The Board questions the desirability, without further study, of authorizing national banks to issue such stock except in emergencies. It has even greater reservations as to the proposed authority for nonequity capital notes and debentures, since, although they may be subordinated to deposits, they are difficult to distinguish from deposits on which interest is limited by law. The Board suggests that this authority should be stricken from the bill, along with the reference thereto contained in section 37 (b). In any event, if this should not be done, the authority should be limited to emergency situations.

Section 26 (c) of title I would have the effect of eliminating the present mandatory requirement for cumulative voting in elections of directors of national banks, but would permit cumulative voting if so provided in the bank's articles of association. Cumulative voting is based on the principle of permitting due representation of minority shareholders on the board of directors: and the principle has been applied to elections of national bank directors since 1933. The Board believes the principle is sound and questions whether the proposed change should be made unless Congress is satisfied that cumulative voting has produced undesirable results so great as to outweigh the obvious justice of giving proper representation to minority interests.

Section 31 of title I contains a provision which would authorize national banks to grant stock purchase options to their employees. The Board recognizes the advantages which stock option plans might have in enabling national banks to recruit and maintain high-caliber personnel. The requirement of the bill for approval by the Comptroller of the Currency of the terms and conditions of such options would help to prevent possible abuses, although it is possible that the last sentence of the new provision might authorize a bank's directors to override any terms or conditions prescribed by the Comptroller of the Currency with respect to the consideration for the issuance of such options. The Board suggests that, at least with respect to some banks, the application of the proposed authority would not be compatible with the public interest. Some banks might be encouraged by this authority to develop unduly profit-minded, expansion-minded managements. Even though employees' stock option authorizations may be appropriate for other types of corporations the Board questions whether they are appropriate in the case of commercial banks which are quasi-public institutions entrusted with other peoples' money. At any rate the Board believes that the statute should include more specific limitations on the terms and conditions under which the options may be granted. We suggest that the provision should be dropped from this bill and made the subject of separate legislation after a period sufficient to permit careful study of both the merits of such an authorization and the limitations which should be placed on its use.

Section 36 of title I would permit a national bank to make real-estate loans in a total amount up to 20 percent of its demand deposits if that amount were greater than its capital and surplus or 60 percent of its time and savings deposits, the alternative limits provided by present law. Since 1913, the aggregate limitation on real-estate loans has been increased on two occasions, once in 1927, and again by the Banking Act of 1935; but Congress has consistently considered it advisable to relate these limitations to the amount of the "permanent" capital structure of national banks or the amount of their time deposits. It has always been felt that demand deposits are an unsuitable basis for real-estate loans, and that the aggregate amount of such loans should be based either on the magnitude of the equity cushion in the bank (i. e., capital and surplus) or on the amount of its time deposits which are less likely than demand deposits to be withdrawn suddenly in large volume. The Board does not believe there has been such a substantial change in banking conditions as to justify using demand deposits as a basis for long-time real-estate loans, and therefore would oppose the proposed change.

Section 37 would increase the maximum limit on a national bank's total indebtedness from 100 percent of its capital stock to 100 percent of its capital stock and surplus. The Advisory Committee recommended that the debt limit be increased to make it less restrictive with respect to borrowings from correspondent banks. However, the increased limit provided by the bill (which, for national banks in the aggregate, would be a dollar amount 2½ times the present limit) would apply to all types of borrowings that do not fall within one of the several excepted types enumerated in the statute. In the Board's opinion, such a considerable expansion in the borrowing ability of national banks would be unnecessary and undesirable.

Borrowing by banks occasionally is necessary and desirable in limited amounts and for limited periods in order to avoid asset liquidation that might otherwise be necessary. It is not, however, a practice that should be encouraged, because it tends to dilute the cushion of protection provided depositors by bank capital and surplus.

Banks should follow a practice of maintaining holdings of liquid assets adequate to meet ordinary needs. Enlargement of borrowing limits as proposed in this bill might encourage banks to hold smaller amounts of liquid assets and rely upon borrowing for needed adjustments. In an emergency requiring large-scale and extended borrowing the discount facilities of the Reserve banks are readily available. To enlarge the ability of national banks to borrow outside the Reserve banks would diminish the restraining influence that the Reserve banks are directed by law to exert upon borrowing banks which are making undue use of bank credit for speculative purposes.

Section 50 of title I would make reports of examinations of national banks and related correspondence confidential documents privileged against disclosure without the Comptroller's consent. The Board concurs in this proposal but believes that it would be highly desirable to include in title II a comparable provision regarding the confidentiality of examination reports of State member banks.

TITLE III (FEDERAL DEPOSIT INSURANCE ACT)

Section 23 of title III would expand provisions of existing law relating to bank mergers so as to require prior approval by the appropriate Federal bank supervisory agency for every merger or consolidation involving insured banks, with a specific requirement that the Comptroller, the Board, or the Federal Deposit Insurance Corporation, as the case may be, shall consider not only the usual banking factors but also whether the proposed transaction would unduly lessen competition or tend unduly to create a monopoly. The supervisory agency would be required to consult the other two Federal banking agencies on the question of competition and would be authorized to request the opinion of the Attorney

General with respect to that question. In the Board's opinion, such an amendment would fill a gap in provisions of present law and would serve to insure consideration on a substantially uniform basis of the impact of bank mergers upon competition in the banking field. As the committee is aware, a bill along these lines which was passed by the Senate last year received the endorsement of all three of the Federal bank supervisory agencies.

It is noted that under section 6 of the title III a single Administrator would replace the present Board of Directors of the Federal Deposit Insurance Corporation and that section 7 provides for an Advisory Board which would include the Chairman of the Board of Governors or his designee. Since the proper discharge of the important functions of such an Advisory Board would make heavy demands on the time of its members, we doubt the desirability of requiring Government officials to assume this added responsibility; and in any event we seriously question whether it would be desirable or advisable for the Chairman of the Board of Governors or his designee to serve as a member.

TITLE IV (FEDERAL HOME LOAN BANK ACT)

The provisions of title IV of the committee print have no material relation to the principal functions of the Federal Reserve System. There are two points, however, with respect to which the Board would like to comment briefly.

Section 15 of title IV would make obligations of Federal home loan banks eligible for purchase by any "agency or instrumentality" of the United States. In the judgment of the Board, it would be undesirable for the Reserve banks to be authorized to acquire obligations of the Federal home loan banks. The language of the bill could conceivably be construed as authorizing investments in such obligations by the Federal Reserve banks. It is assumed that this result was not intended by the provision in question; but if there should be any doubt in this respect the Board recommends that the provision be appropriately clarified.

Section 17 (c) of title IV, dealing with the authority of the Federal Home Loan Bank Board over its financial transactions, expenditures, and personnel, provides that it shall have the same powers and authority in this respect as are presently vested in the Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation. The existence of such a cross-reference would mean that if the relevant provisions of the Federal Reserve Act or of the Federal Deposit Insurance Act should be changed, it would be necessary to consider whether the provisions of the Federal Home Loan Bank Act should be similarly altered. The Board of Governors believes that any such description of the authority of the Federal Home Loan Bank Board in these matters should be self-contained, without any cross-reference to the Board of Governors of the Federal Reserve System.

Section 803

Finally, the Board wishes to comment specially on section 803 of the committee print which would substantially revise and expand sections 217 and 218 of the Criminal Code relating to bank loans and gratuities to examiners. In brief, these provisions would be extended to prohibit (1) gifts by member banks to any officers or employees of the Board of Governors or the Reserve banks; (2) the making of loans or offers of employment by member banks to any employees of the Board or the Reserve banks who may have performed any duties in connection with the member bank in the preceding 2 years; and (3) the making of loans or offers of employment to any other employees of the Board, even though they had performed no duties in connection with the bank, unless the written approval of the Board is first obtained in each case.

Such extremely restrictive provisions are not only unnecessary but, in the Board's opinion, would impose a heavy hardship on employees of the Board and the Reserve banks and the other Federal supervisory agencies to which they would also apply. They would handicap the operations of the supervisory agencies themselves and, even more than the conflict of interest provisions of the bill already mentioned, would hinder recruitment of new personnel. The mere likelihood of enactment of these provisions might possibly bring about an exodus of present employees. Restrictions on loans and offers of employment by a member bank to employees of the Board who have performed duties in connection with that bank would have particularly harsh results; and the difficulties of determining the application of these restrictions in particular cases are apparent. The Board employee who dictates a letter regarding a particular member bank, the stenographer who types it, the lawyer who passes on its legal effect, members of the Board who approve it, and the file clerk who files it, may all be performing duties in connection with that bank.

About 95 percent of the employees of the Federal Reserve System are engaged in duties connected with services performed by the System for member banks, such as the collection of checks and the furnishing of coin and currency. All of these employees would be precluded from obtaining loans from, or accepting employment with, member banks.

Equally burdensome and severe would be the restrictions on loans or offers of employment to any employees of the Board regardless of the nature of their duties. Actually, these restrictions as written in the bill, would seem to go so far as to apply to borrowings by a Board employee from a savinges and loan association or a Federal credit union. In addition, it seems inconceivable that Congress would wish to impose upon the Board and the other supervisory agencies the administrative burden of passing upon practically all borrowings, including installment purchases, by all of their employees.

For all of the reasons indicated, the Board opposes the proposed revision of sections 217 and 218 of the Criminal Code which would be made by section 803 of the committee print.

In conclusion, Mr. Chairman, we would like to reiterate that we are in complete accord with the objectives of the committee; and, with the relatively few exceptions that have been mentioned, we believe that the committee print constitutes a long step toward simplification of the banking laws. The Board and its staff will be glad to give any assistance that may be desired in connection with your committee's further consideration of this proposed legislation.

MEMORANDUM OF TECHNICAL COMMENTS SUBMITTED BY FEDERAL RESERVE ON COMMITTEE PRINT (JANUARY 7, 1957) OF PROPOSED "FINANCIAL INSTITUTIONS ACT OF 1957"

1. Title I, section 22 (b) (p. 11) requires the approval of the Comptroller of the Currency if the total of all dividends declared by a national bank in any calendar year exceeds its net profits for that year combined with its net retained profits of the preceding 2 years, less any required transfers to surplus or a fund for retirement of any preferred stock. Section 23 (a) of title II (p. 92) makes State member banks subject to provisions imposed on national banks relating to "the payment of unearned dividends." While it is not clear that section 22 (b) of title I relates to this subject, it should be made clear by some appropriate language that the Comptroller's approval is not necessary in the case of a State member bank.

2. Tit'e I, section 65 (a) (p. 65) is a restatement of provisions of section 4 of the Emergency Banking Act of March 9, 1933, relating to the power of the President to impose restrictions upon the transaction of business by member banks of the Federal Reserve System in times of emergency. It is suggested that consideration be given to making the provisions of this section applicable to all insured banks.

3. Title II, section 3 (p. 70) continues the language of present law limiting the Federal Reserve Districts to "the continental United States, excluding Alaska." This limitation, because of other provisions of the Federal Reserve Act, might be interpreted as precluding one Federal Reserve bank from receiving from another Federal Reserve bank for collection items payable in Alaska, Hawaii, Puerto Rico, or any insular possession or dependency or any part of the United States outside the United States. It also prevents the Board from authorizing the establishment of Federal Reserve bank branches in such places if they should be needed. Accordingly, it is suggested that the law be clarified by inserting after the word "Board" and before the colon in the second line on page 71 of the committee print the following language:

"and in readjusting districts the Board may include in any such district Alaska, Hawaii, Puerto Rico, or any dependency or insular possession or part of the United States outside the continental United States."

4. Title I, section 15 (b) (p. 84), providing that no Government funds shall be deposited in any nonmember bank in the continental United States, should be appropriately modified in the light of section 10 of the act of June 11, 1942 (12 U. S. C. 265), authorizing deposits of public moneys in any insured banks.

5. Title II, section 17 (b) (p. 86): In the next to last sentence it would seem more appropriate to refer to class C directors of Federal Reserve banks as being "appointed" rather than "designated" by the Board of Governors.

6. Title II, section 19, last sentence (p. 88): It is suggested that the word "monthly" be deleted, since no purpose is served by specifying a pay period in the law. Also the word "flxed" should read "fixed"; and the words "he serves" should read "they serve."

7. Title II, section 23 (b) (p. 92): The first sentence makes mandatory three reports of condition and payment of dividends each year by every State member bank. In order to reduce the reporting burden, it is suggested that the number of required condition reports be reduced to 2 and the number of dividend reports to 1. Also, since it is clear that reports of dividends include reports of earnings, the law should so state. Accordingly, this sentence should be changed to read: "Every State member bank shall make to the Federal Reserve bank of which it is a member not less than two reports of condition and at least one report of earnings and dividends during each year." If this change is made, conforming changes should be made in section 36 (a) of title II (p. 109) and section 52 (a) of title I (p. 41).

8. Title II, section 23 (k), fourth line (p. 94): Change "on June 16, 1934," to read "solely." This would conform to the change made by the act of June 30, 1954 (68 Stat. 358), when the exception as to corporations engaged on June 16, 1934, in holding bank premises was changed to refer to corporations engaged "solely" in holding bank premises.

9. Title II, sections 23 (n) and 28 (f) (pp. 96 and 100) both relate to certifications of checks drawn against insufficient funds. While the former is limited to officers, clerks, and agents of State member banks, and the latter relates to officers, directors, agents, and employees of both member banks and Federal Reserve banks, the language of the two provisions is substantially the same. It is suggested that subsection (f) of section 28 be deleted and that subsection (n) of section 23 be changed to read like subsection (f) of section 28. This would make no change in substance and would eliminate apparent duplication.

10. Title II, section 29 (a), fourth line (p. 101): Phrase "unsafe and unsound practices" should read "unsafe or unsound practices."

11. Title II, section 34 (p. 108): The words "this section" in the third and fourth sentences should read "this Act."

12. Title II, section 39 (i), second line (p. 115): A comma should be inserted after the word "collateral."

13. Title II, section 39 (1), line 9 (p. 115): Delete the words "in the form of notes." This would conform to the similar change made by section 34 (b) (8) of title I of the bill (p. 26), in the exception of Government obligations from the limits on loans to one person by national banks.

14. Title II, section 43 (b) (p. 121): Add at end of this subsection the following sentence:

"The Federal Reserve agent shall each day notify the Board of all issues of Federal Reserve notes to the Federal Reserve bank to which he is accredited." This sentence follows in substance a provision of existing law. It apparently was omitted inadvertently.

15. Title II, section 43 (j) (p. 123) appears to be of no significance in view of the elimination of present provisions of section 16 of the Federal Reserve Act regarding "redemption" of Federal Reserve notes by the Treasurer of the United States. However, in order to preserve the procedure here provided with respect to Federal Reserve notes that "cannot be identified as to the bank of issue," it is suggested that subsection (j) be deleted and that the following sentence be added to section 43 (f) of the bill (p. 122):

"When Federal Reserve notes that cannot be identified as to the bank of issue are destroyed as provided in this subsection, the amount thereof shall be apportioned among the 12 Federal Reserve banks in proportion to the amount of Federal Reserve notes of each Federal Reserve bank in circulation on the 31st day of December of the preceding year."

16. As a matter of style, reference to the Board of Governors throughout the bill (e. g., p. 88, line 3) should refer to the "Board" with a capital letter.

17. Title II, section 55 (a) (p. 140): In the second line of subparagraph (2), insert after the word "bank" the following language which was apparently omitted through inadvertence: "holding company, whichever is later, retain direct or indirect * * *."

18. Title III, section 2 (e), first line (p. 148): The words "national member bank" should read "national nonmember bank."

FEBRUARY 8, 1957.

Senator ROBERTSON. We will have no session tomorrow. On Thursday we will hear the Federal Deposit Insurance Corporation and hope to dispose of that with a morning session. On Friday we will hear the Federal Home Loan Bank Board, and we expect to dispose of that with a morning session. On Monday we will hear the Bureau of Federal Credit Unions and the Justice Department, and we expect to dispose of their testimony in the morning session. We want to get the testimony revised and down to the printer that night so we can have the printed hearings available for the committee the latter part of next week. Then the committee will meet on Monday and we hope in not more than 2 days we can decide on what will go into the bill. Then the chairman of the subcommittee will ask the committee to report a bill to the Senate, as we did, for instance, last May on Senator Sparkman's housing bill. The subcommittee conducted voluminous hearings and then authorized Senator Sparkman to report a bill to the Senate.

Under that procedure, we save time and we will save some printing expense.

The bill would not have an official sponsor. A member is directed on behalf of the committee to report the bill. But, when it reaches the calendar, it then receives a calendar number. It is read for the first time by its title, but it is not sent back to the committee again. It goes on the calendar.

The chairman checked that procedure with the Parliamentarian this morning and the drafting service, and it is an established procedure.

Senator CLARK. Mr. Chairman, I was not clear as to which Monday you wanted to have the subcommittee meet to mark up the bill.

Senator ROBERTSON. The 25th of February. That is the full committee. The action then will be the full committee action.

Senator CLARK. That will be all day?

Senator ROBERTSON. Undoubtedly; yes. The Chair would like to feel we can dispose of it in 1 day, but there may be some little talk about it. We will stay here until we finish, anyway.

Senator ROBERTSON. Before we recess I have two letters that, without objection, will be inserted in the record.

(The letters referred to follow:)

FEBRUARY 12, 1957.

Reference: Financial Institutions Act of 1957, known as the Robertson bank bill.

Senator A. WILLIS ROBERTSON,
United States Senate, Washington, D. C.

DEAR SENATOR ROBERTSON: It has just come to our attention that there is proposed legislation which would change the present Federal Deposit Insurance Act.

We are particularly concerned with section 26, page 162, of the Robertson bill which reads in part as follows:

"No insured bank shall directly or indirectly by any device pay any interest on any deposit which is payable on demand and for such purpose the Administrator may define the term 'demand deposits'."

This differs from a comparable section of the present FDIC law (sec. 18, subsec. (G)) which reads in part as follows:

"The Board of Directors shall by regulation prohibit the payment of interest on demand deposits in insured nonmember banks and for such purpose it may define the term 'demand deposits'."

Under the present law the Board of Directors has by regulation (footnote 6, pt. 329, sec. 329.2) said, "The absorption of normal or customary exchange charges by an insured nonmember bank, in connection with routine collection for its depositors of checks drawn on other banks, does not constitute the payment of interest within the provisions of this part."

It is our opinion that the effect of the proposed change could—

1. Deprive the FDIC from any discretion in the formulation of regulations pertaining to the payment of interest on demand deposits.

2. Deprive the insured nonmember banks from absorbing exchange or other out-of-pocket expenses incurred in the normal collection of its customers' checks.

3. Bring undue and unnecessary pressure on nonmember State banks to remit at par. If a banker could not absorb exchange for a customer it would be most difficult and virtually impossible to charge exchange.

4. Deprive the small country insured nonmember State banks of their oldest and most reliable source of income; namely, exchange.

The FDIC was established to safeguard the banks and their depositors. It must have discretion in promulgating rules to deal with different types of banks operating in different locations. Should these small banks be deprived of one of their main sources of income and the FDIC deprived of its present powers to regulate these banks, conceivably these banks could be forced into a precarious situation and the fundamental purpose of the FDIC would be defeated.

There are one thousand-eight-hundred-odd small nonmember institutions scattered mainly in agricultural areas. Because of the present economic conditions in these areas and the ever-increasing operational cast, these nonmember banks must have this source of income to stay healthy and to provide the help and services required by the small-business men and farmers in their trade areas.

We respectfully request you to amend title III, section 26, of the proposed bill to conform to section 18, subsection (G), of the present Federal Deposit Insurance Act.

Please insert this statement in the records of your hearings of the subcommittee of the United States Senate Banking and Currency Committee.

Yours very truly,

M. W. FORMAN,
Chairman and President,
Bank of Springville, Springville, Ala.

FEBRUARY 12, 1957.

Reference: Financial Institutions Act of 1957, known as the Robertson bank bill.

Senator A. WILLIS ROBERTSON,
United States Senate, Washington, D. C.

DEAR SENATOR ROBERTSON: I have just learned that your subcommittee is holding hearings on a proposed new banking bill that will rewrite section 18, subsection (G), of the FDIC Act and insert a new section known as section 26 on page 162.

In my opinion it might do and result in the following things:

1. Do away with power of FDIC to formulate regulations governing the absorption of exchange.

2. Provoke by statute on nonmember banks rule Q of the Federal Reserve bank.

3. Deprive the insured nonmember banks from absorbing exchange and other out-of-pocket expenses incurred in the normal collection of its customers' checks.

4. Bring undue and unnecessary pressure on nonmember banks to remit at par. A banker who could not absorb exchange for a customer would be placed in a difficult position to charge exchange.

5. Deprive the small country insured nonmember State banks of their oldest and most reliable source of income through the collection of exchange.

6. Jeopardize the strength of these small banks and defeat the fundamental purpose of FDIC.

7. Cause loss to small banks of many of their larger depositors.

8. Place nonmember banks under same restrictions as to absorption of exchange as member banks without the benefits of Federal System.

9. Tend to do away with the dual banking system.

10. By indirection invade States rights to govern by statutes the practices and procedures of State-chartered banks.

11. Take away from small banks a needed revenue in the face of rising operational costs.

12. Endanger strength of banks in agricultural areas.

13. Crippling banks in territories where opportunities for revenues are less than in industrial areas.

14. Impairing the small-business man and farmer by damaging his opportunity for banking service and credit.

15. Will not benefit a national bank but will do great harm to nonmember State banks.

16. That about 1,900 banks will be seriously affected.

Please make this letter a part of the minutes of the hearings of your subcommittee.

Please help us remove section 26 and insert section 18, subsection (G), in your bill.

Yours very truly,

E. F. WALKER,
Vice President and Cashier,
Traders and Farmers Bank, Haleyville, Ala.

Senator ROBERTSON. If there are no further comments, we will stand in recess.

(Whereupon, at 11:30 a. m. the subcommittee was recessed until 10 a. m., Thursday, February 14, 1957.)

STUDY OF BANKING LAWS

(Financial Institutions Act of 1957)

THURSDAY, FEBRUARY 14, 1957

UNITED STATES SENATE,
COMMITTEE ON BANKING AND CURRENCY,
SUBCOMMITTEE ON BANKING,
Washington, D. C.

The subcommittee met, pursuant to recess, in room 301, Senate Office Building, at 10 a. m., Senator A. Willis Robertson, chairman of the subcommittee, presiding.

Present: Senators Robertson, Sparkman, Douglas, Bricker, Bennett, and Bush.

Also present: L. A. Jennings, Deputy Comptroller of the Currency.

Senator ROBERTSON. The subcommittee will come to order.

The witness before us today is the Federal Deposit Insurance Corporation.

The Chair calls attention to the fact that the Senate will be in session today, and we do not have permission to meet while the Senate is in session.

While much of the testimony to be presented for the record today of FDIC is exhibits, the brief is 27 pages. Our previous experience has been that witnesses, even if they are not asked many questions, tend to take about 2 to 2½ minutes a page, and this means a right long session. We have to be through by 12 o'clock, so I hope the witnesses for the FDIC will, on issues that are not too controversial, highlight it and we will put the entire statement and all the exhibits in the record.

We will be glad to hear from the FDIC at this time.

STATEMENTS OF H. E. COOK, CHAIRMAN; MAPLE T. HARL, DIRECTOR; ROYAL L. COBURN, GENERAL COUNSEL; NEIL G. GREENSIDES, ACTING ASSISTANT TO CHAIRMAN; EDWARD H. DeHORITY, ACTING CHIEF, DIVISION OF EXAMINATION; WILLIAM G. LOEFFLER, CONTROLLER; AND EDSON CRAMER, CHIEF, DIVISION OF RESEARCH AND STATISTICS, FEDERAL DEPOSIT INSURANCE CORPORATION

Mr. COOK. Mr. Chairman and gentlemen of the committee, with me is my Associate Director, Maple T. Harl; my administrative assistant, Mr. Greensides; and our General Counsel, Mr. Coburn.

Senator ROBERTSON. Before you start your testimony, Mr. Cook, I have a letter from you dated the 14th in which you transmit a tele-

84444—57—pt. 2——29

gram of the Farmers and Merchants Bank of Walterboro, S. C., to your associate, the Honorable Maple Harl.

If there is no objection, I will just offer that letter now for inclusion in the record, because it deals with absorption of exchange, on which the banking profession objects to our position.

(The letter referred to follows:)

FEDERAL DEPOSIT INSURANCE CORPORATION,
Washington, D. C., February 14, 1957.

HON. A. WILLIS ROBERTSON,
Committee on Banking and Currency,
United States Senate, Washington, D. C.

MY DEAR SENATOR: In view of the fact that your committee is presently considering legislation concerning absorption of exchange, we deem it pertinent to advise you of the receipt of a telegram from the Farmers and Merchants Bank of Walterboro, S. C., which telegram is as follows:

WALTERBORO, S. C., *February 12.*

MAPLE HARL,
President, Federal Deposit Insurance Corporation,
Washington, D. C.:

Strongly urge you to help eliminate from proposed Banking Act that section prohibiting nonmember banks insured by FDIC from absorbing exchange. Clear invasion of States' rights and would be heavy blow to more than 1,800 small banks mostly located in rural areas. Many would not survive without exchange.

FARMERS AND MERCHANTS BANK.

If you desire that we forward the original of this telegram, we will be glad to do so.

With personal regards, I am
Sincerely yours,

H. E. COOK, *Chairman.*

Mr. COOK. Mr. Chairman and members of the committee, we appreciate the opportunity to appear before you today to discuss the proposed bill to amend and revise the statutes governing financial institutions and credit. The members of our Board have considered the various sections of the bill and I hope that we may be of assistance in your deliberations.

Title III of the proposed bill is the Federal Deposit Insurance Act. The committee has made a number of improvements in the deposit-insurance law, some of which were recommended by the Corporation. We appreciate the inclusion of these recommendations in the bill, and there is no need for me to discuss them at this time.

There are a few sections in title III with which we are in disagreement, and it is to these that I wish to direct my remarks at this time. These are: Sections 6, 7, and 42, all of which relate to the management of the Corporation; section 10, relating to the confidentiality of Corporation records; section 26, relating to the payment of interest by insured banks; section 29 (a), relating to termination of insured status; and section 40 (d), which, together with certain amendments to the Criminal Code, relates to employment of, or loans to, Corporation personnel by insured banks.

Sections 6, 7, and 42 relate to the management of the Corporation. Sections 6 and 7 provide, respectively, for management of the Corporation by a single administrator and the creation of an advisory board consisting of the Comptroller of the Currency, the Chairman of the Board of Governors of the Federal Reserve System, and one person representing the State supervisory authorities. Section 42 of the proposed title III abolishes the Board of Directors of the Corporation.

We are strongly opposed to these sections, first, because an examination of the record of the Corporation does not warrant a change such as is contemplated here, and, second, because the independence of the Corporation, as well as its ability to fulfill its insurance function, may be seriously threatened. Let me discuss these two points in some detail.

From its first day of operation, September 11, 1933, to the present date the Federal Deposit Insurance Corporation has been managed by a Board of Directors. It is sometimes forgotten that these years have seen a variety of economic conditions, including the very sharp downturn of 1937–38. During the entire period of operation the Corporation has made disbursements to protect the depositors of 431 insured banks, as a consequence of which all insured deposits in those banks have been restored to the depositors. As a matter of fact, in those 431 banks over 99 percent of all deposits, insured and noninsured, have been paid to or have been recovered by depositors.

Protection of depositors has been achieved through disbursements in excess of a third of a billion dollars, on which the Corporation has recovered over 90 percent, or all but about $30 million, from assets or claims acquired as a consequence of the disbursements.

As a direct consequence of these operations, the confidence of the Nation's depositors in the safety and soundness of their deposits was reestablished and has since been maintained at a level unmatched in our history. We respectfully suggest that there is nothing in this record which gives any reason to advocate a change in the type of management the Corporation has had since its beginning.

Our second point is that adoption of the proposed sections may violate the independence and seriously impair the operations of the Corporation. I would point out that the Corporation was established as an independent agency because its duty is to provide all insured banks and their depositors an equal opportunity to enjoy the benefits of the Federal Deposit Insurance Act unaffected by the special interests of other banking agencies. Further, and equally important, the Corporation has an insurance function which is unique among supervisory agencies and which must and should be carried out for the protection of the depositing public. Usually this can be done with the cooperation and assistance of the interested supervisory agency; at other times it must be done without such support. In any event, independence and freedom of action are essential if this function is to be fully discharged.

To substitute a single administrator for a board and, at the same time, add an advisory board dominated by the other two Federal banking agencies, seems to us to point to only one thing: the eventual loss of the independence of the Corporation. We do not believe that this was the intent of these sections, but we most certainly believe that this will be their ultimate result.

Let me add a word here on the usefulness of the advisory board. The bankers' advisory committee gave as its only reason for recommending the creation of such a board the fact that it would assure—

> to the executive of the FDIC the benefits now derived from the presence of the Comptroller in its councils, and add the same benefits from the Board of Governors and State supervisors' viewpoint.

But the advice and counsel of the Board of Governors and of the State supervisors always have been sought, whenever appropriate, under present management procedures.

The Federal Deposit Insurance Corporation does not operate in a vacuum. It is in daily contact with all segments of the banking industry. And there are well-developed procedures for receiving the viewpoints of other bank supervisory agencies, such as the Inter-Agency Cooperation Committee and the regular fall and spring meetings with the State bank supervisors. And, of course, the Comptroller of the Currency serves on our present Board. We are, therefore, entirely unable to understand how the proposed advisory board will bring any advantages to operations of the Corporation which are not already being enjoyed.

The importance of independence of the Federal Deposit Insurance Corporation is pointed up when we now consider the possible effect of these sections on the operation of the Corporation. We would direct your attention to the fact that, because of its insurance function, the supervisory operations of the Corporation encompass all classes of banks, whereas the supervisory operations of other agencies relate to a single class of bank. Under a dual banking system there arise, of necessity, strong personal interests, often conflicting, from all segments of the banking industry. These interests must be weighed and resolved with no discrimination among the banks. Nondiscrimination among banks can better be secured from the deliberations of a balanced board than from the decisions of one individual.

This point is of sufficient importance to cite several examples of the decisions which must be made by the management of the Corporation.

In my experience, some of the most difficult decisions have been those which involved the use of the Corporation's funds in situations requiring aid to the depositors of distressed banks. Under the existing statute, these decisions, which may involve funds amounting to millions of dollars, must be made with a view to the interest of the Corporation and also with due regard to the need for banking service in the area which the bank serves.

Another example is a decision involving the admission of a bank to insurance. The Board of Directors—or the Administrator in the proposed bill—must consider, among other factors, the general character of the management of the bank and the convenience and needs of the community to be served by the bank. These factors are not subject to precise measurement. They require discussion, understanding, and the exercise of unbiased judgment. Clearly, a composite judgment is called for in situations I have described, and is preferable to the decision of a single individual.

We would also like to call attention to the necessity for nonpartisan management of the Corporation. Such management has been assured because the present act requires that not more than two members of the Board of Directors may be of the same political party. Of course, we assume that if section 6 becomes law the Administrator would be expected to be nonpartisan in his management, but this impartiality may be sometimes quite difficult to enforce. The present management gives us a bipartisan board, which is a far more practical method of assuring true nonpartisan management.

Before ending my direct testimony on these sections, I would like to take note of testimony given earlier before this committee by the chairman of the committee on Federal deposit insurance of the American Bankers Association. This testimony is of particular interest because it indicated the association's lack of confidence in the proposal to turn the management of the Corporation over to a single administrator.

You will recall that in that testimony it was suggested that there be a bipartisan board of five members appointed by the President which "should be constituted with proper authority over the Corporations policies and operations." It was made clear that this Board would be entirely different from the Advisory Board proposed in this bill, and, particularly significant, that it would be constantly in session, giving its full time to the affairs of the Corporation. I suggest that this testimony reflects the fears that many people have of turning over the Corporation to one-man rule.

In summary, we emphasize that the administration of deposit insurance is a complex task, involving more than 13,500 banks and the necessity for the disbursement of sizable amounts of money. It is my sincere conviction that these responsibilities have been ably handled by a board for more than two decades and that they should continue to be so handled, rather than placed in the hands of a single person.

Senator ROBERTSON. The Chair interrupts there to say that he recalls quite distinctly the testimony to which you have just referred of the American Bankers Association objecting to this provision of the bill. He also recalls other testimony to the same effect.

In view of that situation, it is the present intention of the chairman, when the committee meets on the 25th to take final action, to recommend some type of board rather than a single administrator.

You may proceed.

Mr. COOK. Thank you, Senator.

Section 10 relates to the confidentiality of records. Section 10 of the proposed title III provides for the confidentiality of certain Corporation records and was added in accordance with a recommendation made by us and approved by the advisory committee. However, the section also contains a proviso not recommended by the Corporation or by the advisory committee which states:

That all such records shall be made available to the committees of Congress upon request.

In view of the addition of this proviso, our feeling now is that the entire section should be deleted. The Corporation would then continue to rely, as it has in the past, on the protection which is generally afforded by the courts for the confidentiality of its records.

We make this suggestion because section 10 has particular reference to reports of examination of insured banks, and correspondence and papers related to these reports. We are concerned over the possibility that these reports might become subject to review by persons other than those in the bank supervisory field. Basic to the examination process is the knowledge by the bank, by its customers, and by the examiner that the report which results will be entirely confidential. The addition of this proviso strikes at the very heart of bank examination.

Information contained in examination reports is of a nature which, if made public, could seriously affect the interests—and in some cases the reputations—of institutions or individuals who chance to be customers of the bank. In this connection I would point out that the examination report contains not only the usual details relating to bank matters and to loans to individuals but also contains the personal conclusions and opinions of the examiner concerning the bank and its personnel, customers, and community—conclusions and opinions which may not be fully shared by others. Also, that under present procedures bankers feel free to make full disclosure to the examiner of their records, problems, and opinions, including intimate and confidential expressions relating to institutions and citizens in the community. There would not be the slightest chance of securing full and thorough examination reports if they are permitted to be circulated out of the customary bank supervisory channels.

Senator ROBERTSON. The Chair comments on this particular phase of the testimony. You understand there has always been a little disagreement between the legislative and the executive branches of the Government as to what papers they should have access to. The legislative branch always wants the privilege of seeing as many as they want to see. Sometimes the executive wants to put a highly classified secret tag on too many of them.

But, after all, we face the constitutional issue that in the final analysis Congress cannot compel the President to disclose any papers that he does not think should be disclosed, so you always have that protection there. Under this provision, if it stays in the bill and it is passed into law, if Congress wants to see something that you think would be very detrimental if it got out, you could ask the President to instruct you not to deliver it, and there would be nothing I know of Congress could do about it.

You may proceed.

Mr. COOK. Thank you.

Mr. ROGERS. Mr. Chairman, may I ask one question there?

Senator ROBERTSON. Yes.

Mr. ROGERS. Mr. Cook, the General Accounting Office has recommended that, if this provision stays in, it be amended to permit the General Accounting Office to have access to the examination reports in connection with their audits. Would you have any comment to make on that?

Mr. COOK. Well, my only comment to make is I cannot see where any advantage would be to the General Accounting Office to have the confidential, personal reports of banks. As I have stated in this statement, the confidentiality of a bank examination report—and I know this from practical experience—is such that it contains some very personal allusions to individuals, the management of banks, and if that were to become bandied about it could seriously affect the reputation of banks as well as individuals who were mentioned specifically in the examination reports.

Does that answer your question, Mr. Rogers?

Mr. ROGERS. Yes, but I think the General Accounting Office considers it is important in order to do their auditing job to have access to certain records. This is a very broad provision which includes many, many documents aside from those pink sheets in the examination reports.

Mr. COOK. Well, may I make this observation, Mr. Rogers and gentlemen: From a great many years of banking experience both on the operating and the supervisory side, I think the supervision—not because we are engaged in that now, but from my experience for many years on the operating side—has been for the good of the banks. It has helped bank management to operate banks better. And I fail to see where superimposing another agency in this would be of any avail.

I think the bank supervisory agencies, both National and State, are doing excellent work for the good of the banking industry.

Mr. ROGERS. Thank you.

SECTION 26. PAYMENT OF INTEREST

Mr. COOK. Section 26 of the proposed title III has to do with the payment of interest by insured banks and is the same as section 18 (g) of the Federal Deposit Insurance Act, except that, for the words—

The Board of Directors shall by regulation prohibit the payment of interest on demand deposits in insured nonmember banks—

there have been substituted the words—

No insured bank shall, directly or indirectly, by any device whatsoever, pay any interest on any deposit which is payable on demand.

If it is intended by this substitution that the Corporation prohibit the absorption of exchange charges as indirect payment of interest, the language does not accomplish the purpose. The Corporation has repeatedly taken the position that the absorption of exchange charges is not the payment of interest, just as the absorption of some other expenses is not considered by bank regulatory authorities as the payment of interest.

The absorption of exchange charges is a long-established banking practice, and there has always been serious question whether, by regulation alone, it can be defined to be a payment of interest. If this section is enacted into law we do not believe that the Corporation can impose such a prohibition by regulation.

I respectfully suggest that if the Congress desires to prohibit the absorption of exchange charges it do so by express legislation. This could be done very simply, by adding to the sentence quoted above the following words:

***And provided further*, That within the meaning of this provision that the absorption of exchange shall be the payment of interest.**

Senator ROBERTSON. The Chair interrupts to say that he is forced to agree with you on that.

Mr. COOK. Pardon?

Senator ROBERTSON. The Chair is forced to agree with you on that. We thought that we could sort of sidestep responsibility by the language used and unload it on you, but we have reached the conclusion that we did not quite accomplish that.

It has been suggested to me by a distinguished colleague from one of the Southern States who has been "under the guns," so to speak, from a large number of nonpar banks that, while the theory is undoubtedly right that banks should not discount the checks that they cash and that so much business is done with check money now that it ought to exchange just like currency, he could go along with us if we included in the new bill language to this effect:

On and after July 1, 1958, the absorption of exchange shall be the payment of interest on a checking account.

That would put it on ice; would it not?

Mr. Cook. If the Congress makes that the dictum, of course, we will be very glad to comply with it. I might make this statement——

Senator Robertson. What would you say as between putting the explicit language in now and having it become effective as soon as the law was passed or following the suggestion of one of the southern Senators to give the banks a year and a half—because we have been agitating it now since last December—give them all of this year and to July 1 of next year to adjust themselves to this change in the law? Which would you recommend?

Mr. Cook. If it was written into law, I think your suggestion is good, Senator. I might make this observation——

Senator Robertson. I know we are going to writ it into law, but which? Do it now? Or give them a year and a half?

Mr. Cook. I would give them a year and a half to adjust themselves. I think that would be in fairness.

I might make this observation: Two States by their own volition have laws prohibiting or regulating exchange charges.

Senator Robertson. But you do think, as I understand, that we should try to reach this goal of no more absorption of exchange, that all banks that are insured be operating on the same basis? We will not let the member banks do it, and you think it would be desirable to give them a fair period to adjust in requiring all insured banks to operate on the same basis with respect to absorption of exchange? That is your testimony?

Mr. Cook. Yes; with that proviso that they have a reasonable amount of time to adjust themselves.

I would ask my associate, Director Harl, to express his view on that.

Mr. Harl. Two States have already passed laws prohibiting or regulating exchange charges.

Senator Robertson. Will you get nearer the microphone, please?

Mr. Harl. Mr. Chairman, two States have already passed laws on exchange charges, and in Nebraska where they passed it they have had an adjudication on it, and they found that it was within the States rights category.

It would seem to me that these people who want to enforce exchange should go back to State level and enforce it at that point. From the national level we already have it enforced. A national bank cannot absorb exchange by act of Congress, or a State member bank. But it would seem that these State bankers who want exchange prohibited should take it back to State level.

Senator Bennett. Mr. Chairman?

Senator Robertson. Bear in mind there are more State banks than there are national banks, and in any State where a majority of the State banks are nonpar banks they will have more influence with the legislature of that State than those who are member banks or national banks.

While the issue is raised that we are invading the rights of the States, the fact remains that the Supreme Court has held that when any bank voluntarily comes under the jurisdiction of the FDIC, for instance, it submits itself to whatever regulations the Government deems necessary for the banking industry.

That is the reason that there was put in the law a provision—in your bill as in the Federal Reserve Board—relating to the payment of interest on a checking account.

You do not let them pay interest on an open checking account, and they never have claimed that that was any violation of States rights; have they?

Mr. COOK. That is the reason, Senator, we believe that the decision should be made by the Congress, and we will naturally be glad to abide by whatever the Congress feels.

Senator ROBERTSON. Then you think, as far as all insured banks are concerned, uniformity of operation with respect to absorption of exchange is highly desirable?

Mr. COOK. That is my personal view, sir.

Senator ROBERTSON. But you would under the circumstances like to see us give the nonpar banks a reasonable time in which to adjust to the new program?

Mr. COOK. I think that would only be fair.

Senator ROBERTSON. Any further questions on this point?

You may proceed.

Mr. COOK. I should like to make one additional comment, and that follows this thought on this matter. The prohibition of the absorption of exchange charges by nonmember banks is being sought not only to remove a competitive advantage which they may now have but also, as a number of witnesses have already pointed out, because it is anticipated that such a prohibition will have the effect of imposing par clearance on the banking system.

The number of banks not clearing at par is declining and the practice is confined mainly to a few parts of the country. We doubt that the prohibition of the absorption of exchange will, of itself, bring about nationwide par clearance, although perhaps, as Senator Robertson has indicated, it may gradually have this result.

However, if the charging of exchange is brought to an end, it may work a hardship on some banks. The committee should consider carefully an action altering present practices. Our own belief is that the practice of not clearing at par reflects regional and operating characteristics of the banks involved and is a matter which might well be left to the States for appropriate action.

Senator DOUGLAS. Mr. Chairman?

Senator ROBERTSON. The Senator from Illinois.

Senator DOUGLAS. I am puzzled by the attitude of the Chairman of the FDIC. I understood him to say just a minute ago in response to a question of the chairman that he favored congressional action to prohibit the absorption of exchange charges after a year and a half wait. Now in the final sentence which he reads, after he has made his previous statement, he seems to say that the Federal Government should keep its hands off and that this should be left to the States.

I think we ought to have some clarification. It seems to me this is an outright contradiction.

Mr. COOK. I think Mr. Harl just made that statement, sir.

Senator DOUGLAS. No, I would like to have you speak to it.

Mr. COOK. Having known nothing in my experience but par clearance, naturally I would personally be favorable to par clearance. However, if the Congress sees fit to leave this to the States and let the

States decide individually, that is a matter for the Congress to decide. If they decide to make it a mandate to the Federal Deposit Insurance Corporation, we will accept what the Congress says.

Senator DOUGLAS. Do I understand then that you do not make a recommendation in this last sentence that this matter should be left to the States? That is not a recommendation?

Mr. COOK. Not necessarily. It is just a matter of observation.

Senator DOUGLAS. What does it mean—"might well be left to the States"? The implication is it should be left to the States.

If you wish to change that, fine, but in its present form it would seem to indicate opposition by you and by the FDIC to Federal legislation prohibiting exchange absorption.

Senator ROBERTSON. The Chair makes this observation: That he assumes that the witness in that last sentence is talking about congressional action to compel all banks to clear at par. We are not proposing that in the bill or in any discussion so far had on the question of absorption of exchange. We did not propose to prohibit a bank from making a charge. We would prohibit the bank that handled that check from absorbing that exchange charge.

There is a distinction between prohibition against absorption of exchange and par clearance.

It would be pretty tough after July of next year, if that should be the law, for banks to continue, because nobody would absorb the exchange, and checks on that bank just would not pass. The people would not take them, and they would have to stop it. That is, on our theory. But those who wanted to keep it up could take a chance on doing it. We would not prohibit its making a charge.

Some banks make just a nominal charge. I know one Senator told me he understood that the maximum was 10 cents. I said, "Oh, you are very much mistaken that the maximum is 10 cents. It is more apt to be one-tenth of 1 percent on whatever the check amounted to." I said that could run into some real money on a big check.

Do you want to make any further explanation for the benefit of the Senator from Illinois of what you really mean down there in this last paragraph?

Mr. COOK. I think we have made our position clear.

Senator ROBERTSON. I did not hear you.

Mr. COOK. I said I think we have made our position clear on this.

Senator ROBERTSON. All right. You may proceed.

Mr. COOK. The next section is 29 (a), termination of insured status. Section 29 (a) of the proposed title III relates to the termination of insured status of banks participating in Federal deposit insurance. It should be noted that this section provides the sole basis upon which the Corporation may enforce any action it may take to assure a safe and sound banking system.

Section 29 (a) differs in a number of particulars from the comparable section 8 (a) of our present act. Some of these changes were recommended by the Corporation, and some others are acceptable to us. However, we want to call attention to two changes which, if allowed to stand, will seriously hamper the Corporation's authority to eliminate unsafe and unsound banking practices.

These are (1) the omission of the words "or regulation" from the sentence in the present act which authorizes the Board of Directors to institute termination proceedings when it finds that an insured bank has "knowingly or negligently permitted any of its officers or agents to violate any provision of any law or regulation * * *"; (2) the insertion in the proposed bill of the requirement that review of termination proceedings by the court "shall be upon the weight of the evidence." Since these changes may seem to involve only unimportant technical matters, I would like to dwell in some detail on their consequences.

With the elimination of the words "or regulation" it becomes impossible for the Corporation to fully discharge its statutory functions.

Senator ROBERTSON. The Chair interrupts to say that that was inadvertent.

Mr. COOK. Pardon?

Senator ROBERTSON. That was an inadvertent omission in the preparation of the bill, and it will be restored.

Mr. COOK. That has been corrected?

Senator ROBERTSON. Yes. You can just skip that argument on that because it was just a litle error.

Mr. COOK. All right. I think that disposes of the discussion on that.

Senator ROBERTSON. Your testimony will go in in full, but just get to the next item because we have a lot of ground to cover.

Senator BENNETT. Do you want to testify with respect to the weight of the evidence?

Mr. COOK. Yes.

Senator BENNETT. That is in that same section.

Mr. COOK. The requirement that court review of termination proceedings "be upon the weight of the evidence" would substitute a judicial determination for an administrative determination by the Board of Directors of the Corporation. If this is done, the prior administrative proceedings would serve no useful purpose because a final determination of the facts would be made by the court, without regard for the conclusions reached by the Corporation.

In this connection, it should be emphasized that the proceedings are already subject to the Administrative Procedure Act, section 10 of which outlines in detail the rights of review, the form of proceedings, the acts reviewable, the relief pending review, and the scope of review. These rights are adequate, fair, and proper. Thus we strongly urge the elimination from the bill of the words "and the review by the court shall be upon the weight of the evidence."

Senator ROBERTSON. The Chair wishes to comment that that was put in there on the recommendation of the advisory committee, but, of course, it depends on which side of the table you are on as to how well you like that provision. All administrative agencies do not like it, because, of course, it makes it more difficult for them to prove their case. The advisory committee like it because it would make an appeal a little easier for them.

So the full committee will have a chance to decide what the policy will be when we mark up the bill.

You may proceed.

Mr. COOK. Sections 40 (d), 217, 218. Employment of, and loans to, Corporation personnel. Section 40 (d) of the proposed title III relates to employment of Corporation personnel by insured banks. The proposed amendments in the bill to sections 217 and 218 of the Criminal Code also deal with such employment and, in addition, contain prohibitions against loans by insured banks and by certain other institutions and individuals to Corporation personnel.

Senator ROBERTSON. The chairman wishes to interrupt to say that we have gone through this very thoroughly. It has been attacked by everybody that testified. We have indicated that we thought we went too far. We are going to back off of it, and we are going to have a new provision, probably not quite so drastic.

So, while we know you have a good argument against it, we have the record full of good arguments against it, and we will just let the record show what you would have said if you had not skipped it.

Mr. COOK. You have the record, sir.

(The balance of Mr. Cook's prepared statement on the above point follows:)

The three sections are somewhat complicated, and I believe it may be helpful if I summarize both their provisions and the original recommendations by the Corporation relating to them.

Section 40 (d) is a sweeping restriction on employment, in that it makes it unlawful for any employee or even a former employee of the Corporation to accept employment in any insured bank except pursuant to regulations prescribed by the Corporation. The section does not now contain the limitation in our original recommendation to the committee, which was that a conflict-of-interest situation must be involved before the Corporation would be authorized to restrict by regulation the employment by insured banks of any State or Federal examiner and of any employee or former employee of the Corporation.

Without the amendments proposed in the bill, sections 217 and 218 of the Criminal Code prohibit loans to bank examiners by institutions which they are authorized to examine. We believe that this prohibition works a particular hardship on Corporation examiners, who are thus prevented from borrowing from any insured bank, even though only State nonmember banks are regularly examined by the Corporation.

Accordingly, we recommend that our examiners be permitted to borrow from National and State member banks under regulations by the Corporation. However, instead of following this recommendation, the proposed amendments to sections 217 and 218 have so broadened the prohibitions on loans and employment that they would prohibit or impede Corporation personnel from obtaining loans or employment from almost any financial institution or from any individual holding 10 percent or more of the stock of a financial institution.

There is no need for me to take the committee's time this morning to describe the ramifications of these three sections. All that need be said is that the restrictions are far too severe, and are not fair to the fine men and women who are serving in bank supervisory agencies. On this point we are wholeheartedly in agreement with the dissenting opinions which have been expressed earlier before this committee.

So far as specific recommendations are concerned, we believe that section 40 (d) should be rewritten along the lines of our original recommendation to this committee. That is to say, we proposed that section 9 of the Federal Deposit Insurance Act be amended by adding a subsection to read as follows:

"To prescribe, by regulations of its Board of Directors, restrictions on the employment by any insured bank of any State or Federal bank examiner and of any employee or former employee of the Corporation when such employment may involve a conflict of interest, and to prescribe penalties against the bank and the employee for the violation thereof."

We also recommend that the proposed amendments to sections 217 and 218 be deleted and that these sections be amended in the manner originally suggested by the Corporation, and which I described earlier.

Mr. COOK. Actuarial data relating to deposit insurance. I would now like to turn to a matter, not included in the bill, that has been mentioned in the testimony before this committee. It has been stated that no study has ever been made containing actuarial data relating to deposit insurance. This is not correct. Not only have we made a number of such studies, but I would also direct your attention to the hearings of the Senate and House Committees on Banking and Currency on the Banking Act of 1935, when the deposit insurance system established in 1933 was drastically altered, and to the annual reports of the Federal Deposit Insurance Corporation.

The 1935 hearings contain estimates of the losses to bank depositors from bank failures in the United States for a 70-year period prior to 1935, and of the assessment rate that would have been necessary to have met them, and a schedule showing how a hypothetic deposit insurance system operating during the 1920's would have fared.

In the annual report of the Corporation for 1934 there is a more elaborate report giving the underlying factual data; and in the annual report for 1940 there are revised tabulations taking into account additional data. There is no need to present those published studies to this committee; they are available to anyone. However, I would like to leave with the committee, for the record, a document entitled "Actuarial Data Relevant to Deposit Insurance," which brings our analysis up to date to include the experience of the Federal Deposit Insurance Corporation up to the end of 1956. That study will be presented.

The study is quite detailed, and I will not take time to discuss all of the points which it covers. However, I would like to summarize briefly its conclusions.

First: The deposit insurance fund should be adequate to provide the necessary disbursements under any circumstances short of a deep and prolonged depression. In the event of such a catastrophe, it would be necessary to rely upon the borrowing power of the Corporation, but the borrowing power should only be used in such a situation.

Senator BRICKER. What is that borrowing power now?

Mr. COOK. Three billion.

Senator BRICKER. We changed that about 5 years ago?

Mr. COOK. Yes, in the amendment of 1947.

Second: Data relating to bank failures in years other than those of deep depression, and the present concentration of risk to the Corporation, both indicate that the deposit insurance fund should be at least equal to 1 percent of total deposits—or to about 2 percent of insured deposits.

Third: At present the deposit insurance fund is equal to about eight-tenths of 1 percent of total deposits in insured banks, and to about 1.4 percent of insured deposits. Under present conditions it will take about 15 years for the fund to reach an amount equal to 1 percent of total deposits or to 2 percent of insured deposits.

In the light of these conclusions we are strongly opposed to any change in the present assessment formula which would reduce the income of the Corporation. When the fund reaches 1 percent of total deposits or 2 percent of insured deposits a reexamination of the assessment provisions would be appropriate.

Senator BRICKER. Those assessments were changed at the same time?

Mr. COOK. They were changed in 1950. The basic one-twelfth of 1 percent remains, but with a credit after the deduction for losses and operating expenses of 60 percent back to the banks and 40 percent goes into our reserve fund.

Mr. Harl calls my attention to the fact that in the last year the effective rate was one twenty-eighth of 1 percent.

Senator SPARKMAN. Does that apply to all banks regardless of the length of time they have been under the coverage?

Mr. COOK. That is correct, Senator.

Now for some comment on financial institutions.

Senator ROBERTSON. Have you finished your statement about this deposit insurance?

Mr. COOK. Yes.

Senator ROBERTSON. Then, without objection, you may insert in the record at the end of your testimony the material which you describe as actuarial data relevant to the deposit insurance.

We have said, on the matter of change in the assessment rate, to which you are opposed, that we are expecting the FDIC to make a very careful survey covering probably a period of a year of this problem. Is that going to be done?

Mr. COOK. Well, that is in large part that study which we have presented for the record, and it goes back for quite a long period of time.

I have Dr. Cramer of our Research Division present. He can give you a brief résumé of that if you so desire, Senator.

Senator ROBERTSON. We were informed that no adequate study had been made. You can tell us to what extent the material that we are now inserting in the record represents an adequate study and how much more study you think will be necessary?

Mr. COOK. That detailed study was made under the direction of Dr. Cramer, director of our research, and with your permission, sir, I will have him give you briefly his statement on that.

Senator ROBERTSON. We would like to hear from the doctor. Just very briefly, Doctor.

Mr. CRAMER. Senator, I do not think there is any more that we need to do for that study. I think we have completed it. Was that your question?

Senator ROBERTSON. That is my question. Thank you very much. You may proceed.

Mr. COOK. In section 4, page 150 of the committee print, we recommend that the word "asset" be changed to the word "surplus." The language as used in the committee print was suggested by the Corporation, but upon review we have discovered that the term "asset" is not technically correct.

This matter has been discussed with representatives of the General Accounting Office, and we are advised that they, in turn, have discussed the matter with counsel for your committee and have joined in recommending the use of the term "surplus" as here suggested.

Section 5 (e), page 150 of the committee print, gives Corporation management authority over the employment, separation, and compensation of its officers and employees without regard to the provisions of any civil-service laws. This provision was recommended by the Corporation, in support of which it was stated:

> Inasmuch as the existing statute at the time of its enactment was patterned after the authority of each of the 12 Federal Reserve banks by the use of identical language, the Corporation has maintained in view of the reenactment of this identical language in 1950 that appointments and dismissals are not now subject to the civil-service laws and regulations. This amendment is proposed to remove any doubt as to the Corporation's authority in this respect.

The Corporation has not desired to have its employees removed from the benefits of civil service, and for that reason has operated under civil-service procedures, notwithstanding the interpretation to which I have just referred.

However, we point out that the three Federal supervisory agencies must look to a very limited market for their examiner needs. The Federal Reserve banks are free from any restrictions in selecting trainees. The Comptroller of the Currency effects appointment of examiners under a civil-service schedule which allows a latitude of choice to select the most qualified applicants and offer appointment without delay.

Senator ROBERTSON. I wish to ask a question there.

Mr. COOK. Yes, sir.

Senator ROBERTSON. First, are your employees under or not under the civil service at the present time?

Mr. COOK. Mr. Greensides I think is better qualified to speak on that because he has dealt with that subject longer than I have.

Mr. GREENSIDES. I have only dealt with the recruiting procedures. I would not be able to debate the legal point.

Mr. COOK. I will turn the legal point over to General Counsel, sir.

Mr. COBURN. Senator, it has been in the realm of doubt. We have thought in some particulars it was and was not. As a matter of policy we have generally followed civil-service procedures.

Senator ROBERTSON. I discussed this at length the other day with the former distinguished chairman, Mr. Leo Crowley, and he said after full consideration of the opportunities to pick well-qualified men without civil-service restrictions he was very definitely of the opinion that it is in the interests of your employees and in the interest of the public that they have the protection and the security of civil-service coverage. He admitted that the law as it stood was ambiguous, but he said commencing with his administration he had operated under the civil service and he understood you were still doing it.

Now, I understand, you want us to change the law and get from under it?

Mr. COOK. Well, my personal observation would be only this, Senator: That it be relaxed to where we have greater latitude in selecting examiners. With this waiting period from 3 to 6 months, we lose the opportunity to select good men.

The point is we want to have greater latitude in the selection. We believe the Comptroller of the Currency is—is it not true, Mr. Counsel, that the Comptroller of the Currency has greater latitude in that than we have?

Mr. COBURN. Yes, he is operating under I think schedule B of the civil-service classifications, which has not been made available to us.

May I say that in the recruitment we find that the restrictions of Civil Service are making it impossible for us to get employees.

Senator ROBERTSON. The Comptroller's men are under the civil service. He did not want to change that. When you testified last November you wanted us to change it. So we put in the bill what you asked us to put in there. But, as I say, since we have put it in there, the issue has been challenged as to whether we were doing the right thing or not.

That is the reason I told you that I had the call from Mr. Crowley saying that in his opinion we should not make this change in the law.

Mr. COOK. We want our people to have all of the protection that we can possibly give them. All that we need is greater flexibility in our ability to employ men quickly, to pick the right men and employ them without keeping them waiting for a 3- to 6-month period during that time of examination of them. That is what we are trying to——

Senator BRICKER. You object then to employment under what you might call civil-service liaison, but having once been employed and on the payroll you do not object to their having full protection of the civil-service laws?

Mr. COOK. No.

Senator BRICKER. With all the emoluments that go with it?

Mr. COOK. That is right. It is just so we——

Senator ROBERTSON. We will consider this issue when we mark up the bill, but it might be a proper one to refer to the Post Office and Civil Service Committee that has the responsibility of handling civil-service laws and a program of uniformity for the various Government agencies.

Senator BENNETT. May I ask Mr. Cook a question at this point?

Senator ROBERTSON. The Senator from Utah.

Senator BENNETT. If the language were so written as to give you the identical rights and powers that the Comptroller now has, would that satisfy you?

Mr. COOK. I think that that would answer our problem. Would it not, Mr. Coburn?

Mr. COBURN. I think so. The Comptroller is now operating, as I understand, by agreement with Civil Service. That kind of agreement we have not been able to obtain.

Mr. ROGERS. I think, Senator, there is nothing in the National Bank Act that provides for this. It is a matter of working it out with the Civil Service Commission.

Senator DOUGLAS. How does it happen that the Comptroller has persuasive powers over the Civil Service Commission which the FDIC does not seem to have?

Senator ROBERTSON. Mr. Jennings is here, and he can tell us how he worked it, whether he had to do any dealing under the table or how he did it.

Mr. JENNINGS. Mr. Chairman, we are under Civil Service. For years we operated under schedule A of Civil Service, which in effect gave us full power to hire and fire. That had to be renewed annually.

About 3 years ago, the Civil Service Commission decided that it did not wish to renew our privilege to operate under schedule A. We discussed the matter with the Civil Service officials, explained our problem, and they decided that they could place us under schedule B.

Now, schedule B, in effect, has a closed front door but an open back door. In other words, we have to give an examination to each assistant examiner we employ. That examination is prepared by us, but it must be approved by the Civil Service Commission. The Civil Service Commission can come in and look over our records, and we send copies of the examination reports that are prepared by the assistant examiners to the Civil Service Commission.

So we have that closed front door. They have to take an examination. But we are responsible for preparing it and giving the examination.

But so far as eliminating people from our force we do not have to follow all of the rituals prescribed by Civil Service. If we think a man is not doing his job properly, we can tell him so, give him a chance to defend himself, but we can eliminate him.

Senator ROBERTSON. Do you know any inherent reason why under existing law FDIC cannot work out a satisfactory program for new employment just as the Comptroller has done?

Mr. JENNINGS. No, I do not, Mr Chairman, except I will say that we had great difficulty in getting a schedule B preferment. I would think that the Federal Deposit Insurance Corporation should have the same system that we do. I think it is very difficult to try to obtain assistant examiners from the normal civil-service lists. I think it is almost impossible. I would certainly feel that they would operate to better advantage under our system.

Senator BENNETT. May I ask another question?

Senator ROBERTSON. Yes, sir.

Senator BENNETT. Has the FDIC applied for schedule B and been refused?

Mr. COOK. Has that been applied for? This is Mr. Loeffler, our controller, under whose direction the personnel is.

Mr. LOEFFLER. No; we have not applied for that. We have held off on it because we felt that that is subject to change from time to time by the Civil Service Commission. As Mr. Jennings has just said, they took them off schedule A and they had considerable difficulty getting on schedule B.

We would prefer something where we knew that we had a program that we could go ahead with and operate under for recruitment and not be subject from time to time to change.

Senator BRICKER. Mr. Chairman?

Senator ROBERTSON. Yes, sir?

Senator BRICKER. These schedules A and B, so-called, are regulations and schedules made up by the Civil Service Commission and are not a matter of law?

Mr. LOEFFLER. Yes, sir. That is correct.

Mr. ROGERS. Mr. Cook, does not the provision in the bill apply to all employees—taking all of them out from under civil service—rather than just the examiners and assistant examiners?

Mr. COOK. It applies to all employees.

Senator DOUGLAS. Mr. Chairman, I think counsel has brought out a very important point. The testimony that has been advanced has related to examiners, the need of getting examiners by some other course than the ordinary civil-service examination. I agree with that. But, as Mr. Rogers pointed out, the language of exemption extends not merely to examiners but to all employees, and I think there is some question as to whether the clerical employees should be hired on a different basis.

Senator BRICKER. As I understand it, they have no desire to take the clerical employees and ordinary employees out from under full civil service.

Mr. COBURN. The examiner personnel is predominant. It is about 75 to 80 percent of our total personnel in the Corporation.

Senator DOUGLAS. I know, but the language as Mr. Rogers points out, refers not merely to officers but to employees, and, therefore, it is much broader than the term "examiners."

Senator BRICKER. If there could be worked out in the law something similar to schedule B, so-called, as is now in force in the Comptroller's Office, as applying to examiners only, it would be entirely satisfactory then to the Board to leave the other employees under full civil-service regulations?

Mr. COOK. Oh, yes. There would be no objection to that. What we are working for is greater flexibility, a better opportunity to get good men for the examining staff. Of course, we want good people all the way through the Corporation. That is what we are trying to have, and we think we have got them.

Senator BRICKER. According to your controller, it would be more satisfactory to you to try to work it into the law than to try to work it out with the Civil Service Commission?

Mr. LOEFFLER. I think so, Senator; yes.

Senator BENNETT. Before we finally leave the subject, may we ask Mr. Jennings if his position would not be the same as that of Mr. Cook—if he might feel more security if the law finally set the basis on which examiners could be employed?

Mr. JENNINGS. I would agree with that, Senator. We would feel more secure, although we believe——

Senator BENNETT. You are getting along all right?

Mr. JENNINGS. That we are in a firm position at the present time.

Senator BRICKER. There is no reason why one rule should apply to one and another to another department.

Mr. JENNINGS. Absolutely right, sir.

Senator BENNETT. Am I right in understanding that the Federal Reserve Board employees are all out from under civil service?

Mr. COBURN. Under present law, yes, sir. They are not subject at all to civil service.

Senator BENNETT. They have a slightly different status than you do because theoretically they must be more independent of the operation of the Government than you must be.

Senator BRICKER. Mr. Jennings, what about the personnel of the Comptroller's Office other than the examiner force?

Mr. JENNINGS. They are under civil service.

Senator BRICKER. They are?

Mr. JENNINGS. It is just in the employment of our examiners and assistant examiners.

Senator ROBERTSON. From here to the end of your testimony, when you are commenting on the testimony of other witnesses and other provisions not immediately under your jurisdiction, I would suggest that you just outline the problem and state your position. Your whole testimony will go in the record, and then any member of the committee can ask you questions.

Mr. COOK. You want that in memorandum form, sir?

Senator ROBERTSON. I would go right on through. Preferred stock for instance. You do not approve of it.

Just take up one by one your testimony.

Mr. COOK. All right.

Senator ROBERTSON. Go right through, but do not read all of the details. Just state the problem and state your position on it.

(The balance of Mr. Cook's prepared statement concerning appointment procedure for examiner personnel follows:)

The Corporation is being restricted to the general list of eligibles for Federal service and has found it impossible to obtain a sufficient number of qualified trainees from which to maintain its examining force. Under these circumstances we have been forced to request the same freedom of action as is accorded the Federal Reserve banks, in order that our needs may be supplied.

The attached exhibit A outlines appointment procedure for examiner personnel presently followed by the Corporation. We have found that under this procedure the average elapsed time from date of examination of an applicant to date of entry on a register is 6 weeks and that the time is considerably longer if measured from the date of original application. Exhibits B and C illustrate some of the consequences of following present procedures. For example, during the 3-year period 1954–56 more than 6,000 applications were received by the Corporation for the position of trainee assistant examiner but only 265 appointments could be made from this total. During this same period neither the number of examiners and assistant examiners on duty at year-end nor the average number employed during the year equalled the number authorized in the Corporation's manning table.

Mr. Cook. In section 8, page 152, of the committee print, there is a reference to "free" use of the mails by the Corporation. We suggest that the word "free" is not accurate because, while the Corporation may have the franking privilege, it is with payments to the Post Office Department substantially in an amount equivalent to that paid by the general public.

In reference to the caption for section 13, page 155 of the committee print, we recommend "Insurance Without Application" in preference to the terminology in the draft bill. Likewise, in the following section, section 14, page 156, we recommend the caption "Insurance by Application."

Another change in caption which we recommend pertains to section 23 on page 162 of the committee print, at which place we recommend the caption "Mergers, Consolidations, and Capital Reductions."

Section 27, page 164 of the committee print, is a new section, not recommended by any of the agencies, which provides that the Corporation shall be notified of any transaction involving the purchase or sale of 10 percent or more of the outstanding shares of any insured bank. If the intent of this provision is to provide disclosure of actual stock ownership, the effectiveness of the section is doubted. Stock may be issued in names other than the true owners. Even if the Corporation were able to secure information of actual ownership, it could do nothing about it unless the bank engaged in unsafe and unsound practices or in violations of law or regulations.

Senator Robertson. The Comptroller agreed with you on that—that we would not be getting anywhere fast with that.

Mr. Cook. Then you are through with that portion of it?

Senator Douglas. Just a minute. Do I understand then that the FDIC is opposed to any revelation of real ownership?

Mr. Cook. No; we court the revelation of real ownership, but it cannot always be proven, sir.

Senator Douglas. Would you be opposed to provisions which aimed to get at the real ownership of stock in banks insured by FDIC?

Mr. Cook. I did not get that question, sir.

Senator Douglas. Would you favor or would you be opposed to provisions which sought to find out where the real ownership of stock lay?

Mr. Cook. We have no objection to that, sir, but it is just that the stock may be in the name of a nominee and we cannot always prove that, sir.

Senator Douglas. I am trying to find out whether your objection goes to the technical drafting of this provision or to the intent of the provision.

Mr. Cook. We did not raise that question, did we, Mr. Counsel?

Mr. Coburn. No.

Mr. Harl. The intent is all right.

I think, replying to your question, Senator Douglas, that if we could know it, it would be very helpful. I think there was some testimony brought out in the Kefauver committee where there were objectionable characters getting into the banking field in order to make their operations a little more legitimate. But the greatest difficulty is these street names. They buy stock and carry it in street names.

If you could pass a law that would make compulsory registration of stock, it would probably be all right.

Senator Douglas. Is that the opinion of the chairman, too?

Mr. Cook. Yes.

Senator Douglas. I think practices were brought out on this point not only in the Kefauver committee but in hearings of this committee on the Hodge scandal in Illinois.

Mr. Cook. May I proceed, Senator?

Senator Robertson. You may proceed.

Mr. Cook. Section 30 (e) contains obsolete provisions relating to stockholders' double liability. We suggest that the words "and recoveries on account of stockholders' liability" in the last sentence on page 169 and the first proviso on page 170 of the committee print be deleted. Since the time that our recommendations were made to your committee, the voters of the last State in which such matter was applicable to insured banks have approved an amendment to their constitution which removes stockholders' double liability.

As an additional change for the purpose of clarity and to remove an ambiguity in terminology, we suggest that, in the event that an administrator is substituted for the Board of Directors, section 32 be amended so that the first sentence on the top of page 172 of the committee print reads as follows:

> The new bank shall not have a board of directors, but shall be managed by an executive officer appointed by, and subject to the direction of, the Administrator of the Corporation.

It is to be noted that this change does not in any way affect the intent and purpose of the proposed bill.

Senator Robertson. As the Chair said, we intended to get them all. This is one we missed. We will get that on the next go round.

Mr. Cook. This was prepared before that change in attitude, Senator.

The General Counsel of the Corporation has heretofore presented to counsel for the committee a memorandum of a United States district judge, in which it is suggested that section 192 of title 12 of the United States Code, which is included in the current bill as section 59 (pp. 55–56 of the committee print), is unconstitutional, in that it requires a "court of competent jurisdiction" to approve the sale of assets or the compromise of claims in the liquidation of the assets of a national bank. The court stated in its memorandum the general principle that the legislature could not impose administrative duties upon the judiciary. Thus, the court in its memorandum made the following statement:

If this were a matter of first impression, I should feel constrained to examine into the possible application of article III, section 2 of the United States Constitution defining the jurisdictional power of the Federal courts. I am assailed by doubts with respect to the propriety of this court's function as prescribed by the statute in question. What I am asked to do is to perform a single single administrative act, to wit, the approval of the contract of sale submitted by the receiver, in a matter outside the scope of a justiciable controversy and which is not subject to the usual judicial review. * * * In effect, the accomplishment of that single administrative act is the exercise of a supervisory power over a Federal agency—something which I believe to be alien to the Federal judicial functions.

In the case in which this memorandum was written, the court acted on the application, notwithstanding its doubts. However, our Legal Division advises me that after considerable review of legal authorities, it has concluded that there is substantial merit in the position of the court. Thus, in the liquidation of national bank assets, the Corporation finds itself, as receiver, with a statutory requirement to get court approval for sales and compromises, and the courts taking the position that they are without jurisdiction to act upon the receiver's application.

Senator BRICKER. That is on the basis that there is no justiciable question before the court, that there are no parties to the case?

Mr. COBURN. It is an ex parte procedure.

Senator BRICKER. Over which the court has no original jurisdiction?

Mr. COBURN. Yes, sir.

Mr. COOK. In order to remove this doubt, and to assure the ready liquidation of assets of national banks, we are herewith submitting an amendment to the aforementioned section which will eliminate the requirement of court approval of such sales and compromises.

Mr. ROGERS. Do you have the amendment?

Mr. COBURN. Yes; we have submitted it. It is in the statement. This suggests, Mr. Rogers, the amendment of this particular section of our law. And then there is a new proposal which we have also cited that requires court approval. And we have given you language on all three instances.

Mr. ROGERS. Are you putting that in the record?

Mr. COBURN. Yes, sir. It is in our statement.

Senator BRICKER. In other words, if anyone is dissatisfied with your administrative procedure, he would be limited then to his rights under the Administrative Procedure Act?

Mr. COBURN. Well, Senator, in this particular instance—now, let me say, as Mr. Jennings knows, in the National Bank Act there is a section that has been there for a hundred years. It has been before the courts, in the circuit court of appeals in the several circuits for at least a dozen times. It has been mentioned with approval in the Supreme Court four times. But nobody has ever challenged the constitutionality of it. The courts in discussing it spell it out that it is an administrative procedure from which there is no appeal at all. In other words, the court performs a purely administrative action to supplement the action of the receiver.

Senator BRICKER. Sort of a backup provision on the receiver's actions?

Mr. COBURN. Backup. Let me suggest one thing. In the days when there was an independent receiver there was more reason for it than there is now.

Senator BRICKER. That is when the court appointed receivers though.

Mr. COBURN. Well, it was written in there when the Comptroller appointed the receiver. Now, under our present proceedings the Corporation is always receiver in national bank cases, and so there——

Senator BRICKER. But you do not have to go into court to be a receiver.

Mr. COBURN. No, sir.

Senator BRICKER. That is the issue here.

Mr. COBURN. Yes, sir. And the proceeding is outside of court appointment and court initiation.

Senator BRICKER. If you had to get into the court to get yourself appointed receiver of banks, then there would be no constitutional question involved?

Mr. COBURN. Yes, then that would be initiated by process——

Senator BRICKER. Of law.

Mr. COBURN. Yes, sir. No notice is required in this. The receiver goes in in an ex parte proceeding.

Senator BRICKER. You take over originally?

Mr. COBURN. Yes, sir.

Senator BRICKER. And then go into court to get him to back you up in your final say?

Mr. COBURN. That is right.

Senator BRICKER. If there were some disagreement with the terms of the sale on the part of an interested party having a financial interest in it, where would he go for relief?

Mr. COBURN. Well, the cases show in several adjudicated cases that he has appeared in the hearing, the ex parte hearing, has objected to it, and the court notwithstanding objection has approved the sale, and he has appealed, and the appellate courts in several instances have held that they had no right of appeal, that his action was against the Comptroller if he had any.

Senator BRICKER. In the original action?

Mr. COBURN. In the original. It would have to——

Senator BRICKER. In other words, he had to bring an original action?

Mr. COBURN. He would have to initiate an original action; yes, sir.

Senator BRICKER. Yes. How would those rights be protected?

Mr. COBURN. Well, my point is that if you eliminate that—it does not protect a right except that it does provide an additional person passing on it. But if the judge disagrees with him he has no more rights.

Senator BRICKER. And the court of appeals has said you cannot appeal it?

Mr. COBURN. Yes, sir.

Senator BRICKER. It is arbitrary either on the part of the court or on the part of the Corporation?

Mr. COBURN. Yes, sir. Now, his action—he would have to initiate an action against the receiver to——

Senator BRICKER. Which would be the Corporation?

Mr. COBURN. Yes, sir.

Senator BRICKER. I suppose you could not keep him out of that, there is nothing in the act to prevent that.

Mr. COBURN. From him initiating; no, sir. If his rights are transgressed, he has a perfect right to litigate.

Mr. COOK. Since the current hearings have been in progress, a former official of the Treasury Department has called our attention to section 265 of title 12 of the United States Code, which was enacted in 1942 to authorize the designation of all insured banks as the depositaries of public money of the United States, to prohibit discrimination between insured banks with respect to the deposits, and to provide for separate deposit insurance for each Federal custodian of public funds. This provision was not enacted as part of section 12 (b) of the Federal Reserve Act, nor included in the Federal Deposit Insurance Act in 1950 when section 12 (b) was made the Federal Deposit Insurance Act. However, the same language as used in the underlined section of the attached provision was used in 1950 in amending section 3 (m) of the Federal Deposit Insurance Act (12 U. S. C. 1813 (m); sec. 2 (k) of the committee print, p. 149) to provide separate deposit insurance for all custodians of public funds, both State and Federal. It is recommended that this provision, except for the underscored portion, be included in the proposed Federal Deposit Insurance Act, because it is the only authorization for the designation of insured nonmember banks as depositaries of Federal public money. Separate authorizations for national banks and member State banks to be such depositaries are included in the proposed bill.

I now direct your attention to the provisions of the committee draft of the act other than those relating directly to the Federal Deposit Insurance Corporation. In these remarks, I shall not consume your time in submitting favorable comments, but rather shall address my remarks to those sections which we recommend be given further consideration.

Senator DOUGLAS. Before proceeding on this point, may I ask one question about the first paragraph?

Senator ROBERTSON. The Senator is recognized.

Senator DOUGLAS. Mr. Cook, may I ask you if you believe that Federal funds should be deposited in State banks not members of the Federal Reserve System?

Mr. COOK. If they are insured banks, certainly—no discrimination.

Senator DOUGLAS. So that the fact that they are a State bank, not in the Federal Reserve System, should not be a disqualification.

Mr. COOK. Should not be, if their deposits are insured.

Senator DOUGLAS. I wanted to find out what your position was.

Mr. COOK. There is another legislative proposal not included in this bill that we have been considering for some time. It is a plan to simplify the formula for deriving the deposit base upon which assessments are computed. Our objective is to eliminate legal and administrative technicalities, which in turn will reduce the paperwork with regard to both the insured banks and the Corporation. We have a tentative plan which we think accomplishes these objectives and would like to leave with you an explanatory statement with comments on the advantages and disadvantages. We are not proposing legislation at this time, because we wish to discuss the plan with the other banking agencies and with industry representatives to resolve certain problems. When this has been done, we should like to submit proposed legislation to your committee for your consideration.

Now, as to the National Bank Act—sections 20 and 21: Preferred Stock, Capital Notes, and Debentures—we doubt the wisdom of giving to national banks the unrestricted authority to issue preferred stock. This is a temporary medium of providing capitalization, as distinguished from common capital stock, a permanent medium. We strongly urge that, either by provisions in the law or by a statement in the legislative history of the enactment, the use of preferred stock should not be approved by the Comptroller (1) to provide capital for a newly organized institution; (2) as a basis for providing financing of the acquisition of the assets or the assumption of the liabilities of another banking institution; or (3) as the basis for the expansion of the facilities, including the establishment of a branch or branches. Such restrictions would limit the use of preferred stock to instances in which, due to the growth of the deposit volume of the bank, there was a need for capital which could not be currently supplied by the common stockholders.

It is also our view that capital notes and debentures should only be used to provide capital to banks on an interim basis, pending formulation of permanent capital adjustments, and in cases of emergency. Any general provision authorizing capital notes or debentures will be used for capital to the exclusion of common stock and preferred stock because of the tax advantages to be gained thereby. Fundamentally, these instruments provide only temporary capital, depending upon the terms of the note or debenture, and, therefore, do not provide permanent additions to the capital structure of the institutions.

We further recommend that any authorization for preferred stock, capital notes, or debentures should provide that no retirement or reduction thereof shall be permitted unless there are funds available for replacement. For example, if preferred stock is retired, the bank should replace the amount retired by adding the same amount to its common stock, surplus, or reserve for common stock dividends, unless otherwise authorized by the Comptroller of the Currency.

Senator BUSH. Right there, Mr. Chairman, if the preferred stock is retired by the operation of the sinking fund out of earnings, would you consider that as replacement?

Mr. COOK. If earnings are sufficient to make the replacement.

Senator BUSH. Pardon?

Mr. COOK. I say if the retained earnings are sufficient to make the replacement.

Senator BUSH. All right.

Mr. COOK. Does that answer your question, Senator?

Senator BUSH. Yes.

Mr. COOK. Section 29 refers to the removal of officers and directors. The committee proposal in this section, providing for the removal of officers and directors, is subject to the same criticisms that we made in reference to section 29 of the proposed Federal Deposit Insurance Act, relating to the termination of insured status, in that it provides that the court review of removal proceedings "shall be upon the weight of the evidence." This means that the evidence would be fully reconsidered in the appellate court without reference to the findings of the Board of Governors. The Administrative Procedure Act provides in full the standards for review, which are adequate, fair, and proper.

Senator BRICKER. That is, if there is any evidence to support the findings—substantial evidence. It is a question of whether action is arbitrary. In other words, the only question before the court is whether the action of the Board is arbitrary.

Mr. COBURN. Yes, sir. And there is a particular provision in the scope of the review which refers to action that is arbitrary or capricious, in addition to actions not supported by substantial evidence.

Mr. COOK. Section 36: Real Estate Loans. Subsection (a) of this section provides in part that no association shall make loans in an aggregate sum in excess of its capital stock and surplus, or in excess of 60 percent of its time and savings deposits, or in excess of 20 percent of its demand deposits, whichever is the greatest. The last phrase, "20 percent of its demand deposits," is an addition proposed by the advisory committee. We suggest that it is unsound for a bank to have its authority to make long-term real-estate loans based on a percentage of its demand deposits. We recommend that this addition be deleted from the bill.

Mr. ROGERS. Mr. Cook, we had testimony from Governor Robertson that there would be only one bank that it would apply to. Have you any knowledge of how many banks might be involved where 20 percent of the demand deposits would exceed 60 percent of its time and savings deposits?

Mr. COOK. I wouldn't have those figures, Mr. Rogers. Dr. Cramer, would you have any information on that?

Mr. CRAMER. No, sir, I have not.

Mr. ROGERS. It would be a very small number.

Mr. COOK. I would say that the number would be small.

Mr. ROGERS. Thank you.

Senator BRICKER. We don't want to be enacting legislation for one bank.

Mr. COOK. Section 61, winding up business of bank. In subsection (b) of this section there is a provision that a shareholder's agent may sell and compromise or compound the debts due to the bank—

with the consent and approval of United States district court.

There is also a provision that upon the election of a successor shareholder's agent, he shall provide a bond to—

be proved and allowed by and before a competent court * * * with a surety or sureties, to be approved by the aforesaid court.

We have heretofore called attention to the fact that the delegation of administrative authority to the court may be deemed unconstitutional. As a matter of fact, we are recommending changes in other provisions of the bill on account of this contingency. We urge that the same consideration be given to these provisions, to the end that they be deleted from the proposal.

Senator BRICKER. What protection would there be left in a case of that kind against an absolutely arbitrary position taken by the Corporation, except an original action, as suggested by counsel a moment ago, which placed the full burden of that case and cost of it upon an individual that might be affected financially.

Mr. COBURN. Well, in this one I don't think it is so important, Senator, but in reference to the other provision I call to your attention that the Corporation is in what I may characterize a complete box. In other words, we have a provision that for the sale of assets and a receiver we must get court approval. And then the court says "the provision is unconstitutional, and I cannot give you the authority." Now, we have got the assets that we must sell, and the decisions say that that approval is necessary, and we have got the court refusing to give us the approval.

Now, in this case, this is more administrative. I don't think it would be subject to the same contention. But nevertheless, we thought it appropriate to call it to your attention.

Senator BRICKER. The court may take the same attitude that they do with the other provision.

Mr. COBURN. Yes, sir. I appreciate that. And that is the reason that we do call——

Senator BRICKER. In all the history of this act, that question has never been raised before?

Mr. COBURN. No, sir. The other provision has been on the books. It was enacted in the late sixties. And it has been substantially on the books. And we want you to know that getting the court approval is not obnoxious to us.

Senator BRICKER. You do not want to be in a position where you are told to do something you cannot do.

Mr. COBURN. Yes, that is right.

Senator BRICKER. It is amazing to me that that question has not been raised in any court before before this in connection with the Comptroller's Office or the Federal Deposit Insurance Corporation.

Mr. COBURN. And it has been before the courts, no question, literally thousands of times. And millions worth of property——

Senator BRICKER. Could you raise the question in a writ of mandamus, applying to that court, or procedendo?

Mr. COBURN. I don't know. I don't know just what the procedure would be. Now, this issue was raised first by the judge's law clerk, just out of law school, in the United States district court in New York. And many learned judges have passed on it, considered it.

Senator BRICKER. Of course, it was put in here for the protection of interested parties, as kind of a backup for the arbitrary jurisdiction of the FDIC.

Mr. COBURN. It was originally put in before the FDIC was in the picture, where you had an individual acting as a receiver, and the Comptroller——

Senator BRICKER. Appointed the receiver himself, without any court action.

Mr. COBURN. Without any court action, yes, sir.

Senator BRICKER. Again I say it is an unusual question.

Mr. COBURN. It is a very unique question. And may I say we spent considerable time trying to support the authority. Our local counsel in New York did likewise. And I understand that the legal division of the Comptroller's Office has also examined this very carefully, and we cannot come up with any adjudications, decisions, that would support this.

Senator BRICKER. Of course that court doesn't bind any other court except itself. But if the practice would prevail, and if it spread across the country, you would be actually stopped in your liquidation program.

Mr. COBURN. That is the thing, sir. And now some publicity has been given to the memo.

Senator BRICKER. It will go all right. It will be in the books.

Mr. COBURN. Yes, sir.

Senator ROBERTSON. You may proceed.

Mr. COOK. Section 63 refers to purchase of bank property. This section authorizes a national bank receiver, with the approval of the Comptroller and the Secretary of the Treasury, to purchase real or personal property in which the receivership has any equity, and which is being sold under foreclosure or execution in order to protect the receivership. The provision for the approval of the Comptroller and the Secretary is in possible conflict with the provisions of the Federal Deposit Insurance Act. Section 31 (b) thereof provides that the Corporation, as receiver, shall have all the rights, powers and privileges now possessed by or hereafter granted by law to a receiver of a national bank and—

notwithstanding any other provision of law in the exercise of such rights, powers and privileges, the Corporation shall not be subject to the direction or supervision of the Secretary of the Treasury or the Comptroller of the Currency.

We recommend that the requirements of the approval by the Secretary of the Treasury and the Comptroller be eliminated from the provisions of section 63 of the proposed National Bank Act, and that the authorization of that revised section be transferred to and become a part of section 31 of the proposed Federal Deposit Insurance Act.

Section 29—and that has reference to the Federal Reserve Act—concerns removal of officers and directors. We offer no comment in reference to the Federal Reserve Act, except to call attention to the fact that in section 29 there is a repetition of the reference to a hearing for the removal of officers and directors of a bank being subject to the Administrative Procedure Act, followed by a provision for juicial review by a court "upon the weight of the evidence." We again recommend that the review should be as provided in the Administrative Procedure Act without restriction or limitation.

With reference to the Federal Savings and Loan Insurance Corporation Act, we have some comment on section 402, insurance coverage of public funds. We call attention to the fact that in section 402 there is an extension of the insurance coverage which we believe to be incompatible with the general purpose of providing a maximum insurance coverage of $10,000 for each investor. It is to be noted that in this section, by the provision defining "insured member," the committee draft extends insurance coverage of $10,000 to each separate account of each lawful custodian of public funds. Thus, the end result is that a public official may obtain full insurance coverage on all public funds in his custody or control, regardless of amount, merely by establishing several accounts in the same institution. We do not believe that it is within the contemplation of Congress that full coverage beyond the maximum of $10,000 should be granted to officials in instances wherein public funds are invested in share accounts. Yet under this proposal, such full coverage is permitted. We suggest that if it is the purpose that public funds be fully insured, it should be stated in clear, concise terms.

Mr. ROGERS. Mr. Cook, what is the present practice of the Federal Deposit Insurance Corporation in this regard?

Mr. Cook. Up to $10,000, sir.

Mr. Rogers. If a public official wants to split up a number of accounts into A, B, C, D, E, F, and G, don't you insure each of them for $10,000?

Mr. Coburn. Mr. Rogers, it is only insured if the accounts are maintained in a different capacity. Now, for instance, if the funds are irrevocably marked or allocated to a particular purpose or function, then they are separate from the general funds, or from the funds that are allocated or earmarked for another function. But if they are not irrevocably earmarked for some function or purpose, then they are insured generally as one account.

Mr. Rogers. Well, that came to mind because out in Chicago one official had 190 different accounts insured separately.

Mr. Coburn. Well, let's take as an example the Public Administrator could have accounts, various administrations under different accounts. Also it is possible for a treasurer, either municipal or State, to have funds that are for the repayment of bonds, road bonds, sewerage bonds, sinking fund obligations, that are irrevocably pledged.

Mr. Rogers. Well, in that example, could a State treasurer say that he had road bonds for roads in one county in one account, and another county another account, or would they all have to be together?

Mr. Coburn. Unless they are irrevocably pledged to a specific function or purpose, then they are considered jointly with other general deposits.

Senator Bricker. It is all determined by the nature of the trust relationship.

Senator Bennett. To ask the question again in another way, suppose the State legislature appropriated funds for an insane hospital and also appropriated funds for the board of education—would you assume that the designation of those funds, through the appropriation process, to separate institutions would be an irrevocable designation?

Mr. Coburn. Well, in the collection of those funds, if a certain portion of them, percentagewise, was for the insane institution and the other for the second purpose, then they would be separately insured. But if he just maintained a general fund out of which he was free to make his own allocations of them, then it would be a single——

Senator Bennett. If the allocation were made by the legislature in the appropriation process, you consider them separate funds.

Mr. Coburn. Yes, sir.

Senator Bricker. In a case where a treasurer has what he calls inactive funds, they are deposited in bulk, there is no designation of any trust relationship, they are not for any specific purpose, but just to be held against time of need, irreducible debt and things of that kind—there would be only on $10,000 insurance regardless of the amount.

Mr. Coburn. Yes, sir.

Senator Bricker. But on active funds which were deposited for a specific purpose, if the purposes are separate and distinct, one from the other, there would be a multiple $10,000 insurance.

Mr. Coburn. Yes, sir.

Senator Bennett. Well, going back to the objection of Mr. Cook with respect to the Federal Savings and Loan Insurance Corporation, is it your feeling that funds deposited in institutions of that kind should be subject to the same rule as applies in your case?

Mr. COBURN. Yes, sir.

Senator BENNETT. You are not asking for a narrower interpretation—simply the same rule.

Mr. COBURN. We suggested that is what the Congress has had in mind all along by providing a maximum of $10,000.

Mr. COOK. Section 402 relates to the insurance coverage of trust funds. Under existing law, funds held in a fiduciary capacity, when invested in an insured savings and loan institution, are insured in an amount not to exceed $10,000 for each trust estate. Such insurance is separate from, and additional to, the coverage on other funds maintained by the beneficiaries of such trust estates. Under the draft proposal, an account held in a fiduciary capacity would be insured to the fiduciary to the maximum of $10,000 for each beneficiary. This increases the basis for the insurance from each trust estate to each beneficiary.

The amount of insurance afforded to each trust estate would then be determined by the number of beneficiaries, although the interest of a particular beneficiary may be unascertainable. Further, the language of this provision would enable the Federal Savings and Loan Insurance Corporation to measure the insurance in any trust estate by the maximum number of beneficiaries, rather than by their respective interests. For example, if there were 10 beneficiaries, the trust estate would have a maximum insurance protection of $100,000. With the prevalence of large trust funds with multiple beneficiaries, this extension of full coverage to such funds is contrary to the concept of limited insurance protection to investors. Again, we do not believe that such extended coverage is proper and we suggest that the present language be continued in the act.

Now, I finally turn to section 406, payment of insurance, which was so ably discussed by Mr. Lyon, representing the National Association of Mutual Savings Banks, in his testimony before your committee on January 30. In this section it is provided that in the event of a default of any insured savings and loan association, the insurance corporation shall pay each insured account, either by cash or by making available a transferred account "payable on demand" in a new or another insured institution.

We call your attention to the fact that it is contrary to the concept of share accounts that such accounts shall be payable on demand. This concept marks one of the major distinctions between banks and savings and loan associations and between the insurance protection properly afforded by the Federal Deposit Insurance Corporation and that which should be provided by the Federal Savings and Loan Insurance Corporation. A depositor in a bank is a creditor of the institution; an investor in a share account of a savings and loan association is a share owner of the association. Banking institutions are subjected to many statutory restrictions and prohibitions not applicable to savings and loan associations. Many of these requirements relate directly to the liquidity of assets. Savings and loan associations have the greater portion of their funds invested in long-term obligations, and, therefore, such institutions do not maintain, nor are they required to maintain, the high degree of liquidity of assets that is required of banks. It is because of this major distinction between these two forms of financial institutions that share accounts have not been deemed to be instruments which require payment on demand. The current provision in the committee draft, inserted for the sole purpose of paralleling the provisions in the Federal Deposit Insurance Act, has no valid basis. By the deletion of the words "payable on demand" in section 406, Congress will be maintaining the traditional distinction between the two types of financial institutions.

Senator ROBERTSON. The chairman wants to indicate that he realizes, and he learned some of it since he got into these hearings, that there is quite a distinction between a deposit in a checking account that is payable on demand, or even on a time account that is payable on a specified notice, and a share in a savings and loan. But this provision was put in this bill in recognition of what the public thought they would get, that is, their cash; if the savings and loan company went broke, they were insured up to $10,000 and they would get the $10,000. You said we should take that out?

Mr. COOK. We think it should be because it is a distinction between the deposit that is payable on demand in the commercial bank and between the share account which is an equity investment in a savings and loan corporation. Don't misunderstand me, Senator.

Senator ROBERTSON. Do you have any plan to get the public better educated as to the difference between an account in a commercial bank and a share in a savings and loan association?

Mr. COOK. Well, the public in fact does not pay too close attention to that because in the past years the building and loans have been able to pay on demand, the same as banks. But some of us have lived through the time when their assets were frozen and they could not meet that demand.

Now, because a savings and loan cannot pay on demand does not mean they are insolvent. They just may be short of funds.

Senator BRICKER. What if they were insolvent?

Mr. COOK. That would be the point—if they are insolvent.

Senator BRICKER. The shares would still be insured up to the $10,000. It is only a question of when it would be paid.

Mr. COOK. Yes. Well, of course, if they were declared insolvent, I presume they would be paid on demand. But a building and loan may be perfectly solvent and yet not be in a cash position to meet the cash demand.

Senator BRICKER. When would the payment be made in that situation?

Mr. COBURN. Senator, this only refers to when there is a transfer. In other words, we, in some instances, under certain conditions, are given authority to transfer the deposit liability to another bank. Now, then, this provision in the savings and loan law is in those instances where they likewise transfer the share account from one to another and——

Senator BRICKER. You want the rights continued just as they were in the old institution.

Mr. COBURN. Yes, sir. We do not believe there is such a thing as a demand share account. Now, if the savings and loan institution is liquidated, then the insurance company steps in and pays off in cash.

Senator BRICKER. I know. But what if the shareholder does not want any shares in the purchasing institution? When does he get his money? When is his insurance available?

Senator BENNETT. Subject to the rules of the institution to which his account is transferred.

Mr. COBURN. That is right.

Senator BRICKER. What if he doesn't want to transfer it at all? Hasn't he got a right to demand his insurance?

Mr. COBURN. We take the position if any depositor does not want his account transferred, he is entitled to his insurance and we will pay it. And in every arrangement we have, we make the arrangement to pay it on demand.

Senator BRICKER. What about time deposits in a bank in the same situation?

Mr. COBURN. Time deposits?

Senator BENNETT. A short-time deposit transferred to other bank.

Mr. COBURN. When we make the transfer, we give the transfer bank cash or its equivalent, and it is available to the depositor on demand. That is what we think deposit insurance provides.

Senator BENNETT. Mr. Chairman, may I make this observation. Since these are shares and are not deposits, we must keep that in mind constantly, assume a situation in which a savings and loan association gets into trouble and the insurance is activated, and the savings and loan insurance fund decides to transfer these shares—they are not deposits—from association A to association B. If the man whose shares were guaranteed in association A but were purchased in effect by association B—if he has the right to insist upon a demand repayment of his insured shares, then he becomes a preferred shareholder in association B, and the effect of that might be to so stifle the rights of the original shareholders in association B that they take second place, and they may not be paid off until after the shares acquired in the purchase have been satisfied. So this is a very ticklish proposition.

Senator BRICKER. I see it is. And I see here if you do not pay, that you might be defeating the real purpose of the Federal savings and loan insurance. He might not want to go into the new institution. He might not want to have any shares in it. He might not want to share with the old shareholders of the purchasing institution. Under circumstances of that kind, I think he ought to have the right to his insurance immediately. If he wants to go in, I can see then why he ought to go in on the same basis as the shareholders in the new institution.

Senator BENNETT. One of the possible net effects of this might be a refusal of solvent savings and loan associations to accept the responsibility of shares transferred out of an insolvent association.

Senator BRICKER. It is not that situation I am objecting to. He ought to have the option either to take his money on his shares immediately upon dissolution or upon sale. But if he goes into the new institution, if his shares are sold, then he goes in on the same basis as the old shareholders in the purchasing institution.

Senator BENNETT. The law has to be carefully written.

Senator BRICKER. That is what I am getting at. You have to very clearly delineate those rights at that time. They must attach then, if this provision is taken out.

Mr. COBURN. I subscribe to that.

Senator DOUGLAS. Are you through with your testimony?

Mr. COOK. I am, Senator.

Senator DOUGLAS. Are there any general questions?

Mr. WALLACE. May I ask some questions?

Senator DOUGLAS. Yes.

Mr. WALLACE. Mr. Cook, I would like to go back for a moment to your opposition to the proposal for a single administrator to replace the three-man FDIC Board as it now exists.

Is it your contention that a provision for a single administrator would carry with it a danger of arbitrary decisions which would not be true in the case of a nonpartisan board?

Mr. COOK. That could be, Mr. Wallace. And I might say this: For 24 years this Corporation has operated under a bipartisan 3-man board. It has worked when the going was tough. I might make this further comment: The National Bank Act provides that every national bank must have a board of directors of at least five members. Every State has its laws that every State bank must have its board of directors. The concept is that the judgment, the experience offered by a board is better than that of one man. And we feel that this Board, under bipartisan operation, has worked well for 24 years, and when going was tougher than it is now.

To quote Patrick Henry, he once said that he knew of no way of judging the future except by the experience of the past. The experience of the past has been good, and we believe the future is assured by a bipartisan three-man board.

Does that answer your question, sir?

Mr. WALLACE. Let me ask you this question. Assuming you had a very capable and objective single administrator, would that not be preferable to a board? For you would then have pinpointed responsibility, and he could move more quickly.

Mr. COOK. To my mind, no. All of us are human. Supposing your administrator is in the hosptal. We have had times when with two men present, a quorum of the Board, we could act quickly. We meet every week, and the Board is subject to call. We can get together in 10 or 15 minutes if an emergency arises. Then we have the combined judgment of 3 men instead of the judgment of the 1 man whose experience might not be as broad as the experience of 3 men combined.

Senator BRICKER. You think the Comptroller ought to be the third member or a full-time third member.

Mr. COOK. I think the Comptroller is a third member. The way we operate now it is hardly necessary for him to be full time. Further, the Comptroller—and I have served with two of them, both capable, fine gentlemen, and it has worked out fine. And never in any instance has either Comptroller Delano or Comptroller Gidney shown any point of preference toward the national banking system. Their ideas are confined solely to the sound operation of the FDIC.

Senator BRICKER. And there is no incompatibility, of course.

Mr. COOK. No.

Senator BRICKER. But it does place a dual responsibility on the Comptroller. He has a full-time job, hasn't he?

Mr. COOK. Well, he has a full-time job. But we keep him informed by memorandum, by telephone call, if anything comes up. In the meantime, Mr. Harl and myself carry on the acting duties of the Corporation. But it has worked out splendidly.

I might say in regard to the Comptroller of the Currency—I think the figures will show there are approximately 4,900 national banks. In number they are smaller, but nearly 50 percent of the assets of the banking system of the Nation are reposed in the national banking system. That is another argument. And then from the State side, the State banks are represented—both Mr. Harl and myself, as you well know, are past superintendents of banks of our respective States. We have been on the State side. So there are really 2 State members against 1 national member on the Board.

Mr. WALLACE. Mr. Cook, is it not a fact that, for an individual member of a three-man board, the responsibility for making decisions is diluted. In other words, there are 3 people to share the responsibility rather than 1 person to take the responsibility.

Mr. COOK. There has been no instance where all 3 of us have not been willing to share our portion of the responsibility for the decisions made, because they are all fully discussed, thoroughly explored, and the decision—and I think Mr. Harl will agree with me that we have worked in harmony on these things—being the combined judgment of 3 men we feel is better than it could be as the autocratic judgment of 1 man. That is a potential.

Mr. WALLACE. In other words, the big danger in the single man would be that the strong man might be the wrong man.

Mr. COOK. That could be.

Mr. WALLACE. But it is a fact, is it not, that when you make a decision with three men, that decision is shared, so therefore the responsibility is shared and thus diluted?

Mr. COOK. Well, let's put it this way, sir. When the decision is made, it is the combined judgment of three men who have given their judgment on their experience over the years for the particular question that is involved. And of course, going back to your question, naturally each one of the three of us share the responsibility for making that conclusion.

Senator ROBERTSON. If the witness would yield there, the chairman finds he has a call from his office and he has got to go. He is going to ask the Senator from Illinois, Mr. Douglas, to preside in his absence. Before the chairman leaves, he wants to thank the FDIC, along with all the other agencies, for the help that has been given to the chairman, in assembling the laws under their jurisdiction, in making preliminary recommendations, in making final recommendations here today, and for the benefit of their advice on the recommendations made by other agencies.

The Chair has been much pleased to learn that a big publishing house, Commerce Clearing House, Inc., of Chicago, Ill., nationally known publishers of tax and business laws, has seen fit to publish a brochure, 109 pages, called New Federal Banking Code Explained. It is the first time in the 24 years the chairman has been in Congress that even a technical bill, much less a tentative one, has been so adequately analyzed and explained for the public. The chairman feels very much flattered as it is obvious that this organization has expended considerable effort and expense on this. But I will give them credit for doing a good job. And evidently they assumed that what was in the tentative bill was really worthwhile to the bankers, and they probably assumed that most of what was in it will be in the technical bill that the committee will recommend.

The chairman wants to call attention to the fact that there are only 2 more days of testimony standing between the committee and writing a technical bill. We again want to thank all of those who have contributed to the progress made up to this point.

Mr. Cook. Accept our appreciation, Senator, for the courtesy you have extended to us and your always pleasant understanding of our problems.

Senator Robertson. Mr. Wallace, our staff director, will be recognized to continue questioning.

Mr. Wallace. Mr. Cook, in a situation where you have a board rather than a single administrator, would you say that there is a greater or lesser reliance on staff to reach a decision?

Mr. Cook. I did not get that point, Mr. Wallace.

Mr. Wallace. When you have a board instead of a single administrator, is there a greater or lesser reliance on staff to reach a decision?

Mr. Cook. Well, in either case you rely greatly upon your staff who are experts in their particular field. Taking the case of our Board, we set up a committee arrangement—different committees are appointed, different points of operation. The Director meets with the committees and the matter is fully discussed with the directors. So a member of the Board of Directors is present at these committee meetings, and then reports directly to the full Board. And I presume that a single administrator would have to delegate still greater authority. But in our operation, which I have explained to you, it works fine.

Mr. Wallace. Well, suppose you were a single administrator, Mr. Cook, and some questions came up, and you knew that you would have the sole responsibility for the decision rather than a shared responsibility with other members of the Board. Would you place less reliance or greater reliance on staff?

Mr. Cook. I would have to put a great deal of reliance upon the staff, just as we do now.

Mr. Wallace. Would you make more or less sure that you were satisfied with what you were deciding and that it was right?

Mr. Cook. Well, personally I would not like that tremendous responsibility. We have here a corporation of $1.7 billion of assets, insuring the deposits and dealing with 13,500 banks. And it is just too much for one man to have all that responsibility for making those decision. As I mentioned to you, supposing he is ill? Who is going to make up their minds? This way, suppose 1 of our Board is ill—we have a quorum with the other 2 men that can decide and make up their minds.

Mr. Wallace. What is done when the Comptroller of the Currency is ill?

Mr. Cook. Mr. Jennings runs his office when the Comptroller of the Currency is ill.

Mr. Wallace. I am merely pointing out there are other agencies with one administrator that might get ill.

Mr. Cook. Should Mr. Gidney be ill, Mr. Jennings attends the Board meetings in his stead, takes his place on the Board.

Mr. Wallace. During the committee's Hodge investigation last fall, the thing which was rather impressive to those of us who participated in the investigation was the almost complete reliance by the Board on the FDIC staff. As you may know, the recommendation for the single administrator instead of a board grew out of this fact—that had there been one administrator instead of a board, there would have been a greater pinpointing of responsibility.

For example, when Mr. Beutel, in 1951, sought to get FDIC insurance for a new bank in Chicago, the West Irving Bank, he attempted to do so with only $300,000 capital. Mr. Gover, the head of the FDIC Chicago office, was insisting on $600,000. Through some sort of process within the staff, the figure was lowered to $525,000 from Gover's estimate. And it was never explained as to how this came about, other than Mr. Harl's statement, on page 16 of volume 1 of those hearings:

> This was screened by 11 people, including the head of the examination division, Research and Statistics, and came to the Board of Directors having been screened by 11 people.

In other words, he seems to me to have justified this decision purely on the basis——

Mr. HARL. That is where you are 100 percent wrong.

Mr. WALLACE. Beg pardon?

Mr. HARL. If you go back and read the record, Mr. Wallace, the thing you were very critical of this Board was because we let this bank through on a lesser capital than recommended by the Chicago office. And that was where the Board used its own discretion in that matter.

Mr. WALLACE. I don't follow you, Mr. Harl. What are you driving at?

Mr. HARL. I am driving at the fact that in the Chicago hearing, I think we were criticized because the Board insured those banks under less capital than what certain staff members recommended.

Mr. WALLACE. But it was done on the basis of other staff people, those in Washington, rather than in Chicago. It was also done after Mr. Beutel had made a personal visitation upon the staff offices in Washington, and talked with Mr. Shearer and Mr. Sailor of the FDIC staff.

Mr. HARL. That is right.

Mr. WALLACE. But what——

Mr. HARL. I thought your point was that Chicago recommended one thing and we recommended another.

Mr. WALLACE. No. We are talking about this issue of the single administrator versus a board. All I am pointing out here is that your decision for having lowered the amount of required capital was justified only on the basis of the staff recommendations. It is a simple point.

Mr. GREENSIDES. Mr. Wallace, if I may interrupt—when a matter comes before the Board, the recommendation of the district supervisor is before the Board. In other words, the staff did not conceal from the Board what Mr. Gover's recommendation had been.

Senator BRICKER. How many more questions do you have, Mr. Wallace?

Mr. WALLACE. I have 3 or 4.

Senator BRICKER. We are now operating in violation of the Senate rules. Are they questions you could submit to them and have their answers put in the record?

Mr. WALLACE. May I ask just one other question on the conflict of interests issue. Getting back to the FDIC Board reliance on staff. One of the members of the FDIC staff, Mr. John H. Russell, was one of the three persons responsible for setting up this new Elmwood Park Bank, and then he became its vice president and later its president.

Mr. COBURN. Wait a minute, let's get the record straight. He was not responsible for setting it up.

Mr. WALLACE. He was 1 of 3 people, was he not?

Mr. COBURN. No, sir; he was not 1 of 3 people that was responsible for setting up the new Elmwood Bank.

Mr. COOK. He was taken in afterward.

Mr. WALLACE. Who were the three people sent out from Washington to do this?

Mr. COBURN. Well, Mr. Russell went out—not to set up the new bank, but to do the legal work representing the Corporation.

Mr. WALLACE. He helped to set it up, did he not?

Mr. COBURN. No; the Corporation does not set up banks. The organizers or proponents of the banks set up the bank.

Mr. WALLACE. I think, Mr. Coburn, you are being misleading. He participated in the closing of the bank and setting up the new bank. He was there——

Mr. COBURN. Let's be exact, Mr. Wallace. You just don't want to be exact in your language. And that has been one of the troubles we have had here—because you want to use inexact language. Neither Mr. Russell nor anybody in the Corporation closed the existing bank, so Mr. Russell was not out there to close the bank.

Mr. WALLACE. Who said he did?

Mr. COBURN. Well, you said he was sent out there to close the bank and organize a new bank.

Mr. WALLACE. I said he participated in working out the details of the old bank which was closed and in advising on the creation of a new bank. Now, did he or did he not participate in that process?

Mr. COBURN. I say he did not.

Mr. WALLACE. What in the world would you say he did?

Mr. COBURN. He represented the Corporation as a legal adviser to the staff men that were out there and to the Board.

Mr. WALLACE. Did the Board rely on him or did they not?

Mr. COBURN. Well, to the extent that it was necessary to rely on him they did.

Mr. WALLACE. The Board relied on him, didn't they?

Mr. COBURN. To the extent necessary. There was no major decision he made out there.

Mr. WALLACE. But they relied on his judgment, and he later became president of the bank; is that correct or not?

Mr. COBURN. He ultimately became president of a bank that was newly organized after the former bank closed.

Mr. WALLACE. Now I would like to get to Mr. Cook. Does this situation seem to you something about which nothing need be done, or should you have some sort of conflict-of-interest arrangements or rules to regulate that type of a situation?

Mr. COOK. You mean so far as Russell is concerned?

Mr. WALLACE. Yes.

Mr. COOK. I might say this: Many of our men are attracted by other banks because of their ability in examination work, their personality, and possibly all of those things. Now, in the case of Russell, he was sent out there by the Corporation to attend to the Corporation's interests in this bank in the event we had to pay off, and he was looking after the Corporation's interests. Apparently, what they needed was management. They were attracted to him because they thought he had had banking experience, legal experience. They made the offer to him. He did not ask for the offer. And, this still being a free country and a country of free enterprise, where we can go and come as we please, they gave him an offer which was attractive to him. He had a family and he thought that would be a good opportunity. It was his perfect right to take that. But he did not make the advance. They made the advance to him. And, of course, there is no conflict of interest in the least.

We have had those things happen before. And while we dislike to lose good men that we have trained through the years—we have got a good investment in a good many of the men that leave us. Nevertheless, if they can better themselves—if they can go into a bank and give outstanding service to help a bank to be a better bank, it is to the good of the banking industry.

Mr. WALLACE. Mr. Chairman, I don't want to prolong this.

Senator BRICKER. We cannot prolong it any further, because I do not want to violate the rules of the Senate. Besides, I have got to get some things in the Congressional Record at the opening hour, and I would like to close this at this time if we can. If you have any particular question that you want to submit, submit it to the witness and he will reply and put it in the record.

Mr. COOK. Submit them and we will give you a reply in writing.

Mr. WALLACE. Well, I have no other questions, Mr. Chairman. I just wanted to get FDIC comments on this conflict-of-interest situation. Apparently they feel that it was perfectly proper for Mr. Russell to work as an FDIC attorney on the Elmwood Park bank situation and for the FDIC to rely on his judgment in what they did in that case. This was done even though it was later proven that Mr. Russell received a personal loan from Mr. Hodge, who was both the Illinois State auditor and also an owner of that bank. As it turned out all the major issues with respect to this bank which came before the FDIC Board were decided in favor of Hodge. There were three main issues namely, the amount of the capital, the State bank versus the national bank and the assumption transaction versus the receivership. I just want to make the record clear on that point.

Mr. COOK. I might say this, Mr. Chairman. If time permitted I would challenge that question, that every decision we made was in favor of Hodge, because that is not the case. We were simply working on the basis of the facts we had. If you think for a minute, Mr. Wallace, we played footsie with Hodge, you are just as wrong as can be. I don't like that.

Mr. WALLACE. That was not the point I was making. I said you relied on staff judgment when the staff was in a conflict-of-interest situation.

Senator BRICKER. You can prepare a statement and put it in the record, on the statement made by Mr. Wallace.

(Documents referred to by Mr. Cook in his testimony follow:)

EXHIBIT A

APPOINTMENT PROCEDURE

1. Washington office of FDIC collaborates with the United States Civil Service Commission in preparing job specification.
2. Washington office of FDIC collaborates with the United States Civil Service Commission in preparing the text of the announcement.

3. Washington office of the FDIC in conjunction with the United States Civil Service Commission arranges initial publicity on a nationwide basis. Subsequent and continuing publicity is effected by district boards of United States civil service examiners, which are composed of FDIC representatives. Additional publicity is afforded through newspaper releases and visits by Corporation personnel to colleges and universities.

4. District board receives applications forms 5000AB, which are accumulated pending periodic examinations in compliance with civil service regulations.

5. District board arranges with regional office of United States Civil Service Commission to hold written examination.

6. District board advises applicants of date, time, and place of examination.

7. The United States Civil Service Commission regional office, or the district board, grades the test papers, and the applications (form 57) are then reviewed by the district board to determine eligibility on experience and/or education. During the process, forms 57 are also reviewed for completeness and candidates are further contacted when necessary for additional information.

8. District board schedules oral interviews at various locations convenient to successful candidates and notifies them when and where to report.

9. District board conducts the oral interviews.

10. District board advises applicants of eligibility or ineligibility and establishes register of successful candidates.

11. Upon request, district board furnishes certificate of eligibles to appointing officer, from which selections are made in accordance with civil-service procedures. Final approval of the appointment is made by the Board of Directors of the Corporation.

Exhibit B

Survey of experience under U. S. Civil Service Board of Examiners program (announcement No. 401-B)

[Period, April 1954 to December 1956]

Item	Number	Percentage of item (1)
(1) Applications received	6,191	
(2) Reported for written examination	3,160	51
(3) Passed written examination (38 percent of item (2))	1,192	19
(4) Eligible on experience and/or education (32 percent of item (2))	1,016	16
(5) Withdrawals	155	
(6) Passed oral and entered on register (62 percent of item (4))	630	10
(7) Unavailable or declined appointment	203	
(8) Not selected—3 considerations	65	
(9) Appointments (26 percent of item (4), 42 percent of item (6))	265	4

Exhibit C

Field personnel of the Examination Division of the Federal Deposit Insurance Corporation—1954 to 1956

Year end	Number prescribed in manning table	Number actually on duty	Average yearly number
1954	641	592	558
1955	664	615	609
1956	671	615	618

Resignations and separations

Year	Number	Turnover
		Percent
1954	64	11.5
1955	76	12.5
1956	78	12.6

ELIMINATION OF REQUIREMENT OF COURT APPROVAL OF SALES AND COMPROMISES IN LIQUIDATION OF ASSETS OF NATIONAL BANKS

Draft of Proposed Amendment to S. —— (committee print, January 7, 1957), Financial Institutions Act of 1957, to amend subsection (b) of section 59 of title I of S. ——, Financial Institutions Act of 1957 (committee print, January 7, 1957), to read as follows:

"On becoming satisfied, as specified in sections 131 and 132 of this title, that any association has refused to pay its circulating notes as therein mentioned, and is in default, the Comptroller of the Currency may forthwith appoint a receiver, and require of him such bond and security as he deems proper. Such receiver, under the direction of the comptroller, shall take possession of the books, records, and assets of every description of such association, collect all debts, dues, and claims belonging to it, and may sell or compound all bad or doubtful debts, and may sell all the real and personal property of such association; and may, if necessary to pay the debts of such association, enforce the individual liability of the stockholders. Such receiver shall pay over all moneys so made to the Treasurer of the United States, subject to the order of the comptroller, and also make report to the comptroller of all his acts and proceedings: *Provided*, That the comptroller may, if he deems proper, deposit any of the money so made in any regular Government depositary, or in any State or national bank either of the city or town in which the insolvent bank was located, or of a city or town as adjacent thereto as practicable; if such deposit is made he shall require the depositary to deposit United States bonds or other satisfactory securities with the Treasurer of the United States for the safekeeping and prompt payment of the money so deposited: *Provided*, That no security in the form of deposit of United States bonds, or otherwise, shall be required in the case of such parts of the deposits as are insured under section 264 of this title. Such depositary shall pay upon such money interest at such rate as the comptroller may prescribe, not less, however, than 2 per centum per annum upon the average monthly amount of such deposits."

ELIMINATION OF REQUIREMENT OF COURT APPROVAL OF LOANS AND PURCHASES BY CORPORATION ACTING AS RECEIVER OF CLOSED STATE INSURED BANK

Draft of Proposed Amendment to S. —— (committee print, January 7, 1957), Financial Institutions Act of 1957, to amend the last sentence of subsection (b) of section 33 of title III of S. ——, Financial Institutions Act of 1957 (committee print, January 7, 1957) to read as follows:

"The Corporation, in its discretion, may make loans on the security of or may purchase and liquidate or sell any part of the assets of an insured bank which is now or may hereafter be closed on account of inability to meet the demands of its depositors, but in any case in which the Corporation is acting as receiver of a closed State insured bank, no such loan or purchase shall be made without the approval of a court of competent jurisdiction when such approval is required by applicable State law."

INSURED BANKS AS DEPOSITARIES OF PUBLIC FUNDS (12 U. S. C. 265)

"§ 265. Insured banks as depositaries of public money; duties; security; discrimination between banks prohibited; repeal of inconsistent laws.

"All insured banks designated for that purpose by the Secretary of the Treasury shall be depositaries of public money of the United States (including, without being limited to, revenues and funds of the United States, and any funds the deposit of which is subject to the control or regulation of the United States or any of its officers, agents, or employees, and Postal Savings funds), and the Secretary is hereby authorized to deposit public money in such depositaries, under such regulations as may be prescribed by the Secretary; and they may also be employed as financial agents of the Government; and they shall perform all such reasonable duties, as depositaries of public money and financial agents of the Government as may be required of them. The Secretary of the Treasury shall require of the insured banks thus designated satisfactory security by the deposit of —— United States bonds or otherwise, for the safekeeping and prompt payment of public money deposited with them and for the faithful performance of their duties as financial agents of the Government: *Provided*, That no such security shall be required for the safekeeping and prompt payment of such parts of the deposits of the public money in such banks as are insured deposits *and each officer, employee, or agent of the United States having official custody of public funds and lawfully depositing the same in an insured bank shall, for the purpose of determining the amount of the insured deposits, be deemed a depositor in such custodial capacity separate and distinct from any other officer, employee, or agent of the United States having official custody of public funds and lawfully depositing the same in the same insured bank in custodial capacity.* Notwithstanding any other provision of law, no department, board, agency, instrumentality, officer, employee, or agent of the United States shall issue or permit to continue in effect any regulations, rulings, or instructions, or enter into or approve any contracts or perform any other acts having to do with the deposit, disbursement, or expenditure of public funds, or the deposit, custody, or advance of funds subject to the control of the United States as trustee or otherwise which shall discriminate against or prefer national banking associations, State banks members of the Federal Reserve System, or insured banks not members of the Federal Reserve System, by class or which shall require those enjoying the benefits, directly or indirectly, of disbursed public funds so to discriminate. All Acts or parts thereof in conflict herewith are hereby repealed. The terms "insured bank" and "insured deposit" as used in this section shall be construed according to the definitions of such terms in section 264 of this title. June 11, 1942, c. 404, § 10, 56 Stat. 356."

ACTUARIAL DATA RELEVANT TO DEPOSIT INSURANCE

Presented by H. E. Cook, Chairman, Board of Directors of the Federal Deposit Insurance Corporation

Prepared by Division of Research and Statistics. Federal Deposit Insurance Corporation, February 1957

The report of the Advisory Committee for the Study of Federal Statutes Governing Financial Institutions and Credit refers in recommendation 115 (g) to the need for an actuarial basis for determining the underwriting liability of the Federal Deposit Insurance Corporation.[1] The committee regards an actuarial study of this kind to be essential for making a decision regarding revision of the present rate of assessment for deposit insurance; but recommends that pending such a study the entire net assessment income, instead of 60 percent, be credited to the insured banks.

This memorandum is designed to summarize the actuarial data regarding deposit insurance that have been accumulated by the Federal Deposit Insurance Corporation, and also to bring into clear view several considerations that should be kept in mind in connection with any proposal to reduce, even for a limited period of time, the assessment income of the Corporation. The memorandum begins with a statement of these considerations, then examines data which throw light on the risks of the Corporation from insuring deposits and therefore on the needed assessment income and size of the deposit insurance fund.

SOME IMPORTANT CONSIDERATIONS REQUIRED FOR APPRAISING THE SIZE OF RESERVE FUND AND AMOUNT OF INCOME NEEDED BY THE FEDERAL DEPOSIT INSURANCE CORPORATION

Considerations which are mentioned here as pertinent for determination of the size of the deposit insurance fund and the rate of deposit insurance assessment are: (1) Contingencies which the Corporation should be prepared to meet; (2) the function of the deposit insurance fund; (3) the relation of insurance losses and disbursements to the size of the deposit insurance fund and the assessment rate; (4) factors of improvement and deterioration in the ex-

[1] Study of Banking Laws, Report of the Advisory Committee for the Study of Federal Statutes Governing Financial Institutions and Credit to the Committee on Banking and Currency, U. S. Senate, 84th Cong., 2d sess., December 17, 1956, pp. 33–34.

posure of banks to insolvency; and (5) concentration of the Corporation's risk.

Contingencies the Corporation should be prepared to meet.—The advisory committee comments on the purpose of deposit insurance as follows: "Our concept of the purpose of FDIC is that it is unrealistic to assume that FDIC was intended to insure depositors against losses occurring on a major scale incident to economic or other disaster, any more than the fire-insurance industry can insure against losses, incident to an all-out atomic war." If this premise regarding the purpose of deposit insurance is accepted, it is clear that the analogy holds only for an all-out economic or other disaster. That is to say, the analogy implies that the Corporation is not expected to be able, under the powers and resources provided by the deposit insurance law, to handle all the bank failures that might result from a recurrence of a situation like that of the early 1930's. However, just as the fire-insurance industry is expected to be organized in a way to handle losses occurring not only from fires affecting single buildings but also those resulting from a conflagration engulfing a large number of buildings in a given area, the deposit insurance system should be prepared to handle not merely the occasional bank failures of the sort that have occurred during the past few years, but also those that would result from a serious local or regional, but not nationwide, econmic disaster, and further, that it should be prepared to meet the more widespread impact upon bank failures of periods of generally depressed business conditions of lesser magnitude than a calamitous situation like the early 1930's.

The function of the deposit insurance fund.—The report of the advisory committee mentions the aggregate amount of disbursements of the Corporation in connection with the deposit payoff and deposit assumption cases in which it has been involved. However, as in the case of recommendations from other sources that the deposit insurance assessment should be reduced or eliminated, the committee emphasizes the record of losses sustained by the Corporation up to the present time as an indicator of the amount of income and fund needed by the Corporation.

The assumption that the losses of the Corporation may be used as a criterion for judging what is a reasonable size for the deposit insurance fund is erroneous. The Federal Deposit Insurance Corporation was established to protect the depositors of failing participating banks, and to fulfill this duty the deposit insurance fund must be maintained at a level that will make possible the accomplishment of that objective, whether or not there are ultimate losses. Because the function of the deposit insurance fund is so frequently misunderstood the following statement is proposed as properly defining the function of the fund and of the assured borrowing power.

"The function of the deposit insurance fund is to serve as a reserve out of which disbursements can be made to protect depositors of distressed insured banks. Such disbursements may be in the form of direct payments (up to the insurance maximum) to individual depositors in banks placed in receivership, or to distressed banks to facilitate the assumption of their deposit liabilities by sound insured banks, or as subordinated deposits in distressed insured banks.

"For each disbursement the Corporation acquires assets which it must hold for a time: claims against the receiver of the failed bank, or assets of the bank, or a subordinated deposit. Losses that occur are absorbed by the fund but neither the absorption of loss nor the holding of assets during the liquidation process is an independent or separate function; each is a part of the fund's function of providing disbursements needed to protect depositors.

"The assured borrowing power now held by the Corporation is a resource to be used only in unusual circumstances. It is not the purpose of the borrowing power to provide the means of making disbursements except in the contingency that the deposit insurance fund becomes inadequate for this purpose."

Relation of insurance losses and disbursements to the size of the fund and the assessment rate.—In view of the function of the deposit insurance fund, it is irrelevant to use statistics which purport to show that the present fund is adequate or too large because realized losses by the Corporation since 1933 have been very small. The fund, of course, may be as large as is necessary, but this cannot be demonstrated on the basis of the loss experience, because, even if there had been no loss and even if future losses are expected to be very small, the fund still must be available to provide disbursements to protect depositors in distressed banks. However, the losses experienced by the Corporation, and those that might occur from other contingencies it should be prepared to meet, are pertinent to the assessment rate necessary to maintain the fund once it has attained an estimated requisite size.

The question of the appropriate size of the deposit insurance fund is directly related to disbursements which may be necessary to protect depositors of distressed banks. In this connection it should be remembered that disbursements by the Corporation are accompanied by claims against a receivership or by assets acquired from the distressed banks, which claims or assets may have to be held for considerable periods of time. Thus the adequacy of the fund depends both upon its size in relation to any anticipated disbursement and upon the quality of assets acquired from previous transactions, i. e., upon the degree and speed with which such assets can be converted into cash to provide funds for further disbursements. Ability to convert other assets in the fund into cash is also pertinent, but it may be assumed that the portion of the fund invested in United States Government obligations can at any time be turned into cash.

The Corporation has had little or no experience with some of the contingencies it should be prepared to meet. Consequently, in scrutinizing the record of the past for light on the actuarial basis of deposit insurance it is important to pay attention not simply to the Corporation's experience, but also to the Nation's experience with bank failures prior to 1934. This is particularly necessary as an aid in judging the probable magnitude of insurance disbursements in such a contingency as a prolonged depression in a particular industry or area. It is also well to look at the magnitude of disbursements that might have to be made in the event of another wave of bank failures accompanying a very deep depression, even though it is not assumed that the Corporation should be continuously endowed with sufficient resources to handle such a situation.

Factors of improvement and deterioration in the exposure of banks to insolvency.—In addition to using both the experience of the Corporation since 1934 and the experience of the Nation with bank failures prior to that time, attention must be given to elements of improvement and of deterioration in the status of banks from the point of view of their exposure to insolvency. Proponents of the assertion that the present fund is large enough to justify a reduction in the assessment rate stress the elements of improvement in the banking system since 1934, particularly the present high quality of bank assets, better bank supervision, and elimination of the overbanked situation of the two decades prior to the 1933 depression. Bnt there are also elements of deterioration in the banking situation, particularly in the reduction in bank capital relative to assets.

It should not be assumed that the improvement since 1933 in the banking system and in supervisory practices has overcome the deterioration of the capital position of the banks to such an extent as to rule out the possibility of numerous bank failures accompanying a business recession. If that assumption is seriously taken, it should be accompanied by more evidence than has been set forth. So long as banks remain institutions with liabilities for the most part redeemable on demand and assets for the most part not immediately convertible into cash there will be a danger of serious bank failures as a consequence of deteriorating economic conditions. We do not know of any analysis that has been made which shows how the nature of the economy or the fundamental nature of banking has so changed as to rule out this possibility.

Concentration of risk.—Concentration of risk is recognized by insurance experts as an important element in the size of the reserve fund that is needed in an insurance system. For example, one might have serious reservations about the actuarial soundness of a fire-insurance company that agreed to insure for its full value a building worth considerably more than all of the company's reserves.

One obvious aspect of concentration of risk to the Federal Deposit Insurance Corporation is that relating to size of bank. Previous experience with bank-obligation insurance suggests that this kind of concentration of risk is an element of importance. In several of the State systems operated prior to 1933 failure rates among the larger banks were higher than among smaller banks. Thus far the opposite has been true under Federal deposit insurance, as it also was in certain of the State systems prior to 1933, but there is no assurance that this will continue to be the case.

There is another kind of concentration of risk to which attention should be given. There are some insured banks in each of which the capital of the bank appears to be uncomfortably low. The risk which this entails for bank solvency in each case is real and apparent; and though supervisory officials attempt to have such situations corrected the continued presence of banks with very low capital ratios year after year indicates that this is more than a temporary problem.

ACTUARIAL DATA RELEVANT TO THE FUND NEEDED BY THE CORPORATION AS AN INSURER OF BANK DEPOSITS

There is a certain degree of risk which attaches at all times to the insurance of bank deposits. In ordinary years the actual liability which results from this risk is fairly small and well within the assessment income of the Corporation. But if deposit insurance is to serve its purpose, the deposit insurance fund of the Corporation must be sufficient to guard not only against this type of risk but also against the possibility that on some occasions disbursements may be required which will far exceed the assessment income for the given year.

No one can translate this serious risk into a precise determination of the needed size of the deposit insurance fund, but an analysis of the available data throws considerable light on this crucial question. This analysis is presented under the following subjects: (1) the relative size of the deposit insurance fund; (2) the Corporation's disbursement and loss experience; (3) other data relevant to the significance of the Corporation's experience; (4) the distribution of the Corporation's potential insurance liability; (5) the probable needed insurance fund in the event of a wave of bank failures accompanying a deep depression; and (6) the probable needed fund in the event of misfortune other than a deep depression.

Relative size of the deposit insurance fund.—That the size of the deposit insurance fund should bear some relationship to the amount of deposits in insured banks is apparent, although there may be many opinions as to how large a reserve fund is needed by the Corporation. A first step, therefore, in an actuarial study of deposit insurance is to look at the relative size of the deposit insurance fund since its beginning, and to determine what effect the present assessment provisions have on its relative size.

The ratios of the deposit insurance fund to insured deposits and to total deposits at each year-end date are shown in table 1. At the end of 1956 the deposit insurance fund was 0.80 percent of total deposits in insured banks and 1.45 percent of the estimated amount of insured deposits. These ratios are below those which prevailed in 1934, the first year of the Corporation's operation. The ratios at the end of that year were 0.83 percent and 1.84 percent, respectively.

In 1935 the ratios of the deposit insurance fund to total and to insured deposits declined because of the refunding to the banks, when the permanent insurance plan went into effect, of the assessments that insured banks had made under the temporary plan. During the next few years the ratios tended to rise. During the war years the ratios fell sharply as deposits increased rapidly, losing more than their prewar gain. With the interruption of deposit growth at the close of the war, the ratios again tended to rise. However, this upward trend was interrupted in 1947 and 1948 by repayment of the Corporation's original capital, and again in 1950 and 1951 by payment of interest on the retired capital. Also, the provision for net assessment income credits to insured banks in the 1950 law sharply reduced the tendency for the ratios to rise.

At the end of 1951, after the Corporation had completed the payment of interest on its capital, the fund amounted to 0.72 percent of total deposits in insured banks and 1.33 percent of the estimated insured deposits. Since that time, the fund has grown somewhat more rapidly than bank deposits. Specifically, during the years 1952–56, the average annual rate of increase of the fund was 6.3 percent, while the annual rate of growth of total deposits was 4.1 percent and that of insured deposits about 4.4 percent.

Maintenance of an appropriate rate of growth in the Nation's circulating medium, or money supply, of which bank deposits are now the predominant portion, is widely recognized as an important element in the economic policies of the Nation. The need for such growth was described by a congressional commission 80 years ago:

"It is in a volume of money keeping even pace with advancing population and commerce, and in the resulting steadiness of prices, that the wholesome nutriment of a healthy vitality is to be found. The highest moral, intellectual, and material development of nations is promoted by the use of money unchanging in its value. That kind of money, instead of being the oppressor, is one of the great instrumentalities of commerce and industry. * * * It is only under steady prices that the production of wealth can reach its permanent maximum, and that its equitable distribution is possible." [1]

[1] Report of the United States Monetary Commission, Senate Report No. 703, 44th Cong., 2d sess., 1877, pp. 51–52. The Commission was composed of 3 Senators, 3 Representatives, an ex-Congressman, and a university professor.

Judged both from the experience of recent years and from the record of the Nation for more than a century, an average rate of growth of bank deposits of about 4 percent per year is normal. We should anticipate the continuance of deposit growth at this rate.

A projection of the income of the Federal Deposit Insurance Corporation over the next 23 years is shown in table 2 and of its deposit insurance fund in table 3. These projections assume a deposit growth of 4 percent per year, and annual losses and operating expenses of the Corporation to be the same relative to assessments as the average of the annual rates during the time of the Corporation's operation. They show the income of the Corporation and the size of the fund under the present assessment provisions, and also the effect of crediting the entire net assessment income to the insured banks.

Unless the deposit insurance fund continues to grow by at least the same rate as deposits the size of the fund relative to total or to insured deposits will decline. The investment income of the Corporation is not sufficient, by itself, to provide a rate of growth for the deposit insurance fund that will keep pace with the anticipated growth in bank deposits. Thus, any proposal to return the entire net assessment income to the banks is, in effect, a proposal to initiate a continuing decline of the deposit insurance fund, relative to total or to insured deposits. Under such a plan the ratio of the fund to total deposits will decline to 0.7 percent in 9 years, and to 0.6 percent in 20 years, assuming a normal rate of growth in total deposits. A proposal to return the entire assessment income to the banks must therefore rest on the assumption that the present deposit insurance fund is larger, relative to deposits, than is needed by the Corporation to meet contingencies for which it should be prepared.

The Corporation's disbursement and loss experience.—From the beginning of 1934 to the end of 1956, the Federal Deposit Insurance Corporation has paid off the insured deposits, or provided sufficient funds to enable the assumption by another bank of all the deposits, of 431 insured banks. In doing so, it has made disbursements of approximately $340 million, of which $292 million were paid directly to depositors or expended to enable the assumption of their deposits by other banks, and $48 million consisted of payoff and liquidation expenses and advances for the protection of assets. During the same period the Corporation was able to build up a deposit insurance fund from assessments and investment income of $1,742 million, having had to absorb losses amounting to only $30 million. Taken as a whole, this experience is cited frequently as evidence that the present deposit insurance fund is adequate and that a reduction in the deposit insurance assessment is desirable. To determine whether such a conclusion is borne out by the data requires a more detailed analysis.

Disbursements for the protection of depositors have been made by the Federal Deposit Insurance Corporation in each calendar year beginning with 1934. The amount of disbursements, including payoff and liquidation expenses and advances for protection of assets, ranged from a high of $91 million in the case of banks closed in 1940 to a low of $276,000 for banks closed in 1946. In several years these disbursements were a sizable proportion of assessment income. In each of 2 years, 1939 and 1940, the disbursements were no only far in excess of income from assessments but also exceeded all Corporation income.

Disbursements, as indicated in the first part of this study, result in the acquisition of assets (including claims against receivers) by the Corporation. The amount of such assets held on any particular date may reasonably be considered as representing that part of the deposit insurance fund in use. Table 4 provides data showing, at each year-end date, the size of the deposit insurance fund, the Corporation's reserve for losses, and the volume of assets held by the Corporation that had been acquired as a consequence of insurance disbursements.

Reference to this table will show that the assets resulting from insurance disbursements held by the Corporation increased rapidly during the prewar period, after which the volume declined until 1952, and has tended to rise again in recent years. The peak amount was in June 1940, when the Corporation held about $147 million of such assets. This was equal to 29 percent of the deposit insurance fund plus the reserve for losses on that date. The amount of these assets in excess of the Corporation's reserve for losses was 22 percent of the deposit insurance fund.

Table 5 shows the disbursements and losses of the Corporation each year. Comparison of this table with the preceding one shows how misleading are the loss data if only losses are compared with the deposit insurance fund in an attempt to appraise the adequacy of the fund. Perhaps the best illustration of this is, again, the year 1940. The final loss from disbursements made during that year was less than $4 million, or 0.8 percent of the fund in 1940. However, the fact that the loss eventually absorbed by the fund was so small can scarcely be considered a reflection of its adequacy in 1940, when it had to provide for disbursements of about $91 million, which with previous disbursements tied up more than one-fifth of the fund after setting up reserves for losses.

Other data relevant to the significance of the Corporation's experience.—An analysis of the 1934–56 experience should not ignore Federal aid to banks by agencies other than the Federal Deposit Insurance Corporation. Such aid was given primarily by the Reconstruction Finance Corporation, the Home Owners Loan Corporation, and the Farm Credit Administration. These disbursements contributed significantly to restoring the strength of the banking system, and had these agencies not been in existence the Federal Deposit Insurance Corporation undoubtedly would have been called upon for a much larger expenditure of funds.

Together, these three agencies disbursed upward of $2 billion to aid open or closed banks in the period beginning with 1934, which was several times the amount of disbursements by the Federal Deposit Insurance Corporation. Any projection of the banking record which purports to show how much the Corporation may have to disburse in the future should take account of these disbursements by other agencies, since to the extent such disbursements are necessary again they will have to be made by the Federal Deposit Insurance Corporation.

Another important element of the experience since 1934, which has not been favorable, is the decline in the capital of insured banks relative to their assets. At the end of 1934 total capital accounts in insured commercial banks were 13 percent of all assets and 26 percent of so-called risk assets. At the end of 1956 these ratios were approximately 7 percent and 16 percent, respectively. This decline may not be quite so serious as it appears because of the fact that capital today is probably more sound than was the case in 1934 and the fact that reserves against losses, not included in capital accounts, are relatively greater now than 20 years ago. Nevertheless, the very rapid increase in bank assets since 1934 has definitely outpaced the rate of growth of bank capital, and thus the vulnerability of the banking system to adverse economic conditions has increased.

Another observation must be made about the experience since 1933. It is clear that some observers entertain the rather disquieting view that this period is unique in our history; that the United States has entered a new banking era in which the major difficulties of the past may be safely forgotten. While we are hopeful that this may indeed be the case, it must be remembered that there have been other periods in our history during which banking difficulties were small. As a matter of fact, quite early in our history there was a period of a quarter century during which there was not a single bank failure.

Another period during which the losses from bank failures were relatively light was from 1898 to 1920. During that period the average annual ratio of deposits in closed banks to the deposits of operating banks was less than one-third as high as during the preceding 25 years, and only one-seventh as large as in the subsequent decade and a half. Had a deposit-insurance fund been operating during the 1898–1920 period, with principal disbursements equal to one-half the deposits in failed banks (as in the case of the Federal Deposit Insurance Corporation during 1934–56), such disbursements would have averaged one-tenth of 1 percent per year of the deposits in operating banks. While this disbursement rate relative to deposits in operating banks is substantially higher than in the case of the Federal Deposit Insurance Corporation, it is not much higher than the Corporation's rate would have been had the disbursements to banks by the Reconstruction Finance Corporation and other agencies been made by the Federal Deposit Insurance Corporation.

Considered in its entirety and in the light of previous experience, the record since 1933 provides much less evidence than is often assumed that the developments of recent years have greatly diminished the likelihood of a relatively large number of bank failures occurring in the future.

Distribution of the potential insurance liability.—That the risk to the Corporation as an insurer of bank deposits is concentrated in a small number of banks is evident from the fact that approximately half of the deposits in the more than 13,000 insured banks are held by 100 banks. On December 31, 1956, there were 11 insured banks each of which had total deposits exceeding the entire deposit-insurance fund.

Three of these banks held deposits which not only exceeded the fund, but also exceeded the fund and the $3 billion that the Corporation is authorized to borrow from the United States Treasury. It should probably not be assumed that in the event of difficulties in any one of these banks the disbursement by the Corporation would be equal to the total deposits, or even to the insured deposits. It is more reasonable to assume that if a very large insured bank were to become involved in serious financial difficulties an effort would be made to have its liabilities assumed by another insured bank, or to have the bank reorganized with the help of the Corporation. Apart from the administrative difficulties of direct payoff in such a case is the fact that the closing of a very large bank might result in the nearly simultaneous closing of many banks keeping their correspondent balances with the distressed bank.

Disbursements to date by the Corporation in the cases of banks which have been handled on other than a payoff basis have averaged 53 percent of total deposits. This includes principal disbursements, advances for asset protection, and liquidation expenses. If we assume, conservatively, that a disbursement in the case of an exceptionally large bank would be 30 percent of its deposits, it is evident that there is still a considerable concentration of risk to the Federal Deposit Insurance Corporation. Under such circumstances there are three insured banks, the failure of any one of which would more than exhaust the deposit insurance fund. There are six other banks, the disbursement for any one of which would require from two-fifths to one-half of the deposit insurance fund; and there are still six other banks, for any one of which a disbursement equal to 30 percent of total deposits would require over one-fourth of the deposit insurance fund.

Table 6 shows the total deposits of the 25 largest insured banks at the end of 1956 and the disbursements which might be necessary, should any one of these banks become involved in serious financial difficulties. Revealing as these figures are, they do not reflect the fact that a very large commercial bank in serious financial difficulties may be a symptom (or a cause) of fundamental difficulties in the banking system, which difficulties may result in other substantial disbursements by the Corporation.

Size of bank is not the only kind of concentration of risk to which the Corporation is subjected as insurer of deposits. In table 7 the total deposits and insured deposits are given for two groups of banks with a relatively thin capital cushion. The first of these groups includes the insured banks that, on June 30, 1956, had total capital accounts amounting to less than 5 percent of their assets. The deposits of these banks were more than 5 times, and their insured deposits more than 3 times, the amount of the deposit insurance fund.

The other group of banks with thin capital margins, shown in the same table, includes those with total capital accounts amounting to less than 10 percent of "assets at risk." The term, "assets at risk," as used here, is narrowly defined; it excludes not only the types of assets usually excluded in tabulations of "risk assets," such as cash and balances with other banks and United States Government obligations, but also loans that are insured or guaranteed by agencies of the Federal Government. It is evident that a bank with total capital of less than 10 percent of "assets at risk" is in a vulnerable position. A relatively small depreciation in these assets, say 2 or 3 percent, would result in serious capital impairment, while a decline of 10 percent would wipe out the bank's capital. It is to be expected that many of these banks would be among the cases requiring Corporation disbursements in the event of even a minor depression.

On June 30, 1956, there were 226 insured banks with total capital less than 10 percent of "assets at risk." The insured deposits in these banks amount to 28 percent more than the entire deposit insurance fund, while their total deposits are more than twice the amount of the fund. The vulnerable position of these banks becomes even more apparent when we consider the fact that the assets not tabulated as "at risk" are not free from risk. Judged by current market values, these and other insured banks have large losses on their holdings of United States Government obligations. These "paper" losses do not show on the banks' books, and will not materialize if the banks hold the obligations to maturity. But whenever a bank that is close to the margin of safety runs into adverse circumstances, it is likely to face the necessity of selling United States Government obligations at market values, thus taking losses on those assets as well as on "assets at risk."

There is no mechanical or automatic method of translating these data on the concentration of bank deposits into a working rule as to the size of deposit insurance fund needed. It could reasonably be maintained that the deposit insurance fund should be at least as large as the amount of deposits insured under the $10,000 maximum in the largest bank participating in deposit insurance.

This would mean a fund equal to about 2.5 percent of all deposits in insured banks, or three times as large as the present deposit insurance fund. However, objection may be made to this figure on the ground that the Corporation is not likely to find itself in the position of paying individual depositors in the case of a very large insured bank in financial difficulties. An alternative proposition, therefore, might be that the deposit insurance fund should be at least equal to the minimum probable disbursement in the event of serious financial difficulties in any one of the largest insured banks. If this is placed at 30 percent of the deposits of such a bank, it means that the deposit insurance fund should be about 1.25 percent of the deposits in all insured banks. The present fund is less than two-thirds of this size.

Needed fund in the event of a wave of bank failures accompanying a deep depression.—The United States has had numerous periods of banking troubles when large numbers of banks have failed. Among these, there are three in which seriously depressed business conditions and widespread banking difficulties were more intense and prolonged than the others: the late 1830's and early 1840's, the 1870's, and the early 1930's. Tabulations of the number and obligations of banks that failed or suspended during the first of these periods are not available.

In the 1870's the deposits of the banks that failed in a 6-year period amounted to approximately 7 percent of the deposits of all operating banks at the beginning of the period; and in the early 1930's, in a 4-year period, failed banks had about 13 percent of the deposits of operating banks at the beginning of the period. The losses to depositors on accounts up to $5,000, which we may take as roughly equivalent to the present coverage of $10,000, adjusted for assessments collected from stockholders, are estimated at 2.4 percent of deposits in operating banks for the period of the 1870's, and 2.3 percent for the early 1930's. Table 8 contains data on deposits and losses to depositors in failed banks during the 1870's and the early 1930's.

There is no question that the present deposit insurance fund would be entirely inadequate should, for example, a situation similar to that of 1930–33 recur. After a careful analysis we have concluded that in order to make the necessary disbursements in such a situation the Corporation would need to have at its disposal available funds equal, as a minimum, to 5 percent of the total deposits in all operating banks. This figure assumes that the necessary principal disbursements would have been only 37 percent of the deposits in the closed banks in comparison with the Corporation's experience of 50 percent. Since the fund today is only 0.80 percent of total deposits (and with the assured borrowing power only 2.2 percent of total deposits) the inadequacy is obvious. As a matter of fact, it would require all of the present deposit insurance fund plus all of the $3 billion borrowing power to absorb only the losses that would occur in such an emergency.

To what extent can we expect a situation such as that of 1930–33 to recur? Certainly, we can conceive of the possibility of a severe economic downturn, accompanied by large numbers of bank failures. Neither the public confidence engendered by the existence of Federal deposit insurance nor the improvements in banking or bank supervision would be sufficient to prevent these failures, which would be a consequence of economic dislocations of a fundamental nature. However, because the Federal Government is committed, under the Employment Act of 1946, to follow policies which will stimulate full employment, and in view of the knowledge and authority now possessed by various agencies of the Federal Government, it is reasonable to assume that we will be able to avoid the prolongation of a serious depression.

Needed fund to handle contingencies other than deep depressions.—Waves of bank failures are not necesarily connected with deep depressions. They may occur during periods when the economy as a whole is stable or prosperous, because of a set of circumstances affecting a particular region or industry. The underlying causes of such a situation may be deep-rooted so that the failures tend to extend over a number of years. In such a situation there is the danger that the deposit insurance fund will come to consist largely of low quality assets acquired through disbursements to protect depositors.

The most recent such period, and the one for which the most data are available, is that of 1922–29. This 8-year period was a time of great prosperity interrupted only slightly by the mild recessions of 1924 and 1927, which were comparable in severity to that of 1954. Some of the bank failures of those years were due to mismanagement and defalcation of the sort that still produce an occasional failure among insured banks, and some were due to hangover conditions from the depression period of 1920–21, similar to some of the failures among insured banks during the first few years of Federal deposit insurance. But for the most part the failures of 1922–29 represented an inability of banks in the agricultural regions of the Nation to adjust themselves to the impact of a set of economic circumstances having an adverse effect on agriculture and on the trading centers of agricultural areas, even though business throughout the nation was generally prosperous.

The argument may be made that the situation that existed during the prosperous period of the 1920's will not recur, on the grounds that the "overbanked" condition of that period no longer exists and that improvements in bank management and bank supervision have made the banks less vulnerable to adverse economic conditions. Yet the fact is that the banks are probably more vulnerable today, rather than less, to adverse economic conditions, because of their weaker capital positions, and because their capital positions, as they are measured today, are based on the assumption that the Government obligations owned by the banks can be held to maturity and consequently exaggerate the margin of safey provided by capital funds. Economic maladjustments as serious as those of 1922–29, affecting either agriculture or another segment of the economy, may occur again, with as great an impact on the solvency of banks.

Perhaps the best method of visualizing how the Federal Deposit Insurance Corporation would be affected by a recurrence of a situation like that of the 1922–29 period is to set up a hypothetical deposit insurance fund for the period from 1900 to 1930. If established at the beginning of 1900 such a fund would have operated prior to 1922 nearly as long as the Federal Deposit Insurance Corporation has been in existence. Tables 9, 10, 11, and 12 show how such a hypothetical fund would have fared, had it been set up with a capital fund, assessment rate, insurance coverage, and assured borrowing power comparable with those of the Federal Deposit Insurance Corporation, and with various assumptions about the portion of the net assessment income retained by the fund. The first of these four tables shows the losses of that period on depositors' balances of $5,000 and under, which may be taken as the losses met by the fund, the income of the fund, and its size at the end of the year, assuming that all the net assessment income was retained by the fund. The second table shows the income of the fund, and its size at the end of each year, with 40 percent of the net assessment income retained by the fund; and also if the entire net assessment income had been credited to the banks.

The third table shows the disbursements of the fund each year on account of failed banks, on the assumption that such disbursements would have been equal to one-half of the deposits of the failed banks, and also the estimated portion of the fund that would have been tied up in assets acquired from failed banks. The fourth table deals with the adequacy of the fund's assured borrowing power to meet the situation of the middle and late 1920's.

These tables indicate that a deposit insurance fund established at the beginning of 1900 would have survived the banking difficulties of 1907 and 1908 without recourse to borrowing had the fund retained all of its net assessment income, though the assets acquired from failed banks would have absorbed a larger portion of the fund than was the case with the fund of the Federal Deposit Insurance Corporation in 1940. Had a fund established in 1900 credited the entire net assessment income to the banks borrowing would have been necessary in the 1907–08 situation, and it might have been needed with retention of 40 percent of net assessment income.

By 1920 the hypothetical fund started in 1900 would have been more than four times as large as its initial size had all assessment income been retained, but less than twice as large as its initial size if the entire net income had been credited to the insured banks. However, in 1920 the deposits in operating banks were more than five times as large as at the beginning of the century, having increased at an average rate of more than 8 percent per year. Consequently, the fund would have declined relative to deposits. Had the fund started with an amount equal to three-fourths of 1 percent of the deposits in operating banks and retained all the net assessment income, by 1920, it would have declined to about three-fifths of 1 percent of the deposits in operating banks. With retention of 40 percent of net assessment income the fund would have been reduced to two-fifths of 1 percent of the deposits in operating banks. With the entire net assessment income credited to the banks, the fund would have been reduced nearly to one-fifth of 1 percent of the deposits in operating banks.

The hypothetical fund would also have successfully weathered the depression in 1921. The wave of failures beginning in the latter part of 1920 and continuing through 1921 would not have required the fund to make use of its borrowing power; and the proportion of the fund tied up at the end of 1921 in assets acquired from failed banks would have have been considerably less than in 1908. In fact, a fund retaining all of its net assessment income would have had only one-fourth of the fund in such assets at the end of 1921—not much greater than was the case with the Federal Deposit Insurance Corporation in 1940.

Nevertheless, the bank failures of the prosperous period of 1922–29 would have been disastrous to the hypothetical fund started in 1900, particularly if the fund had retained only 40 percent or none of its net assessment income. Had it retained the entire net assessment income it could have survived, with the use of only a portion of its assured borrowing power, until 1930. But with retention of only 40 percent of net assessment income both the fund and assured borrowing power would have been exhausted by the end of 1929. With the entire net assessment income credited to the banks both would have been exhausted by the end of 1926. In these computations it is assumed that the fund would have borrowed from the United States Treasury without payment of interest; if interest were charged the exhaustion of the borrowing power would have come earlier.

Taking the year 1922–29 by themselves, the cumulative deficit of the fund incurred from the losses charged off would have been about one-half of 1 percent of the average annual aggregate deposits in operating banks. In addition, the assets acquired from failed banks in excess of the losses, and held to the end of 1929 on the assumption used in the computation that all liquidations are completed by the end of the fourth year after the year of failure, would have amounted to about three-tenths of 1 percent of the deposits in operating banks. Under the circumstances of such a period, liquidation of the acquired assets would probably proceed less rapidly than is implied by this assumption, so that a more reasonable allowance for holdings of assets acquired from failed banks would be one-half of 1 percent. This leads to the conclusion that to meet a situation like that of 1922–29, the Federal Deposit Insurance Corporation would need an accumulated fund of 1 percent of the deposits in insured banks.

The claim may be made that since the present deposit insurance fund plus the assured borrowing power of $3 billion now equals more than 2 percent of the total deposits of insured banks, though the fund itself is only 0.8 percent of such deposits, this is sufficient to prepared for a contingency such as we have been discussing here. However, as deposits in insured banks increase with the passage of time, the assured borrowing power will become relatively smaller. In addition, dependence on the Corporation's borrowing power to meet such a contingency overlooks the fact that the banking difficulties of such a period, if they occur, will appear during a stable or prosperous period for the economy as a whole. For the Corporation to resort to the borrowing power in such a period—which action is tantamount to an admission that the deposit insurance fund is insolvent—would be detrimental to public confidence.

The greatest contribution the Corporation has made, and should continue to make, is maintenance of the confidence of the depositing public. While the standby arrangement with the Treasury is a source of comfort to the Corporation, to be used in the event of a serious emergency, the minute the Corporation is forced to show bills payable in its financial statement the public confidence might be shattered.

Summary and conclusions.—Proposals to reduce the deposit insurance assessment usually compare the Corporation's loss experience since 1933 with the present assessment income and include an assumption that banking difficulties of the kind which were common prior to Federal deposit insurance will probably not recur. Such proposals state or implicitly assume that the present deposit insurance fund of 0.80 percent of the deposits in insured banks is more than adequate to meet the need of the Corporation for a reserve fund.

When all the evidence is considered, and not merely the Corporation's loss experience, there is no reason to conclude that the present deposit insurance fund is adequate to meet the disbursements which may be involved in the contingencies for which the Corporaton should be prepared. The data that the Corporation has been able to collect and analyze—relating both to historical experience and to the current distribution of the Corporation's potential liability—lead us to the conclusion that a reserve fund amounting to 1 percent of the deposits in insured banks is the smallest figure that can possibly be considered reasonably adequate in view of the Corporation's responsibilities. Under the present assessment provisions, continuance of the remarkably low losses of the Corporation to date, and continuance of a 4 percent per year rate of increase in the deposits in insured banks, it will take about 15 years for a fund of this size to be accumulated.

84444—57—pt. 2——32

TABLE 1.—*Deposits in insured banks and the deposit insurance fund, 1934–56*

[Amounts in millions]

Dec. 31	Deposits in insured banks			The deposit insurance fund		
	Total deposits	Insured deposits [1]	Percent of deposits insured	Amount of fund	Ratio of deposit insurance fund to— Total deposits (percent)	Ratio of deposit insurance fund to— Insured deposits (percent)
1934	$40,060	$18,075	45.1	$333.0	0.83	1.84
1935	45,125	20,158	44.7	306.0	.68	1.52
1936	50,281	22,330	44.4	343.4	.68	1.54
1937	48,228	22,557	46.8	383.1	.79	1.70
1938	50,791	23,121	45.5	420.5	.83	1.82
1939	57,485	24,650	42.9	452.7	.79	1.84
1940	65,288	26,638	40.8	496.0	.76	1.86
1941	71,209	28,249	39.7	553.5	.78	1.96
1942	89,869	32,837	36.5	616.9	.69	1.88
1943	111,650	48,440	43.4	703.1	.63	1.45
1944	134,662	56,398	41.9	804.3	.60	1.43
1945	158,174	67,021	42.4	929.2	.59	1.39
1946	148,458	73,759	49.7	1,058.5	.71	1.44
1947	154,096	76,254	49.5	1,006.1	.65	1.32
1948	153,454	75,320	49.1	1,065.9	.69	1.42
1949	156,786	76,589	48.8	1,203.9	.77	1.57
1950	167,818	91,359	54.4	1,243.9	.74	1.36
1951	178,540	96,713	54.2	1,282.2	.72	1.33
1952	188,142	101,842	54.1	1,363.5	.72	1.34
1953	193,466	105,610	54.6	1,450.7	.75	1.37
1954	203,195	110,973	54.6	1,542.7	.76	1.39
1955	212,226	116,380	54.8	1,639.6	.77	1.41
1956 [2]	218,000	120,000	55.0	1,742.1	.80	1.45

[1] Estimated by applying to the deposits in the various types of account at the regular call dates the percentages insured as determined from special reports secured from insured banks.
[2] All figures for Dec. 31, 1956, except the amount of the deposit insurance fund, are estimated.

TABLE 2.—*Projected income of the Federal Deposit Insurance Corporation, 1957–80*

[Amounts in thousands]

Year	Assessments becoming due [1]	Expenses and losses [2]	Net assessment income retained under 1950 law [3]	Investment income under 1950 law [4]	Total income of FDIC	
					Under 1950 law	With entire net assessment income credited to insured banks [5]
1957	$161,598	$14,544	$58,822	$43,551	$102,373	$43,551
1958	168,062	15,126	61,174	46,111	107,285	44,641
1959	174,784	15,731	63,621	48,793	112,414	45,757
1960	181,775	16,360	66,166	51,604	117,770	46,901
1961	189,046	17,014	68,813	54,548	123,361	48,073
1962	196,608	17,695	71,565	57,632	129,197	49,275
1963	204,472	18,402	74,428	60,862	135,290	50,507
1964	212,651	19,139	77,405	64,244	141,649	51,770
1965	221,157	19,904	80,501	67,785	148,286	53,064
1966	230,003	20,700	83,721	71,493	155,214	54,390
1967	239,203	21,528	87,070	75,373	162,443	55,750
1968	248,771	22,389	90,553	79,434	169,987	57,144
1969	258,722	23,285	94,175	83,684	177,859	58,573
1970	269,071	24,216	97,942	88,130	186,072	60,037
1971	279,834	25,185	101,860	92,782	194,642	61,538
1972	291,027	26,192	105,934	97,648	203,582	63,076
1973	302,668	27,240	110,171	102,738	212,909	64,653
1974	314,775	28,330	114,578	108,060	222,638	66,269
1975	327,366	29,463	119,161	113,626	232,787	67,926
1976	340,461	30,641	123,928	119,446	243,374	69,624
1977	354,079	31,867	128,885	125,530	254,415	71,365
1978	368,242	33,142	134,040	131,891	265,931	73,149
1979	382,972	34,467	139,402	138,539	277,941	74,978
1980	398,291	35,846	144,978	145,487	290,465	76,852

[1] At 4 percent increase over the preceding year.
[2] At 9 percent of assessments becoming due, the average of the annual percentages during 1934–56 (with assessments under the temporary plan in 1934–35 assumed to have been at the rate under the permanent plan).
[3] 40 percent of net assessment income, which is defined as assessments becoming due less expenses and losses.
[4] At 2.5 percent of deposit insurance fund on preceding Dec. 31, which is the approximate average rate received by the Corporation during 1934–56.
[5] Investment income only, at 2.5 percent of deposit insurance fund on preceding Dec. 31

TABLE 3.—*Projected deposit insurance fund, Federal Deposit Insurance Corporation, 1957–80*

[Amount in millions]

Dec. 31	Deposits in insured banks [1]	Deposit insurance fund [2]		Ratio of fund to deposits in insured banks	
		Under 1950 law	With entire net assessment income credited to insured banks	Under 1950 law (percent)	With entire net assessment income credited to insured banks (percent)
1957	$226,720	$1,844	$1,786	0.81	0.79
1958	235,789	1,952	1,830	.83	.78
1959	245,220	2,064	1,876	.84	.77
1960	255,029	2,182	1,923	.86	.75
1961	265,230	2,305	1,971	.87	.74
1962	275,840	2,434	2,020	.88	.73
1963	286,873	2,570	2,071	.90	.72
1964	298,348	2,711	2,123	.91	.71
1965	310,282	2,860	2,176	.92	.70
1966	322,693	3,015	2,230	.93	.69
1967	335,601	3,177	2,286	.95	.68
1968	349,025	3,347	2,343	.96	.67
1969	362,986	3,525	2,401	.97	.66
1970	377,505	3,711	2,462	.98	.65
1971	392,606	3,906	2,523	.99	.64
1972	408,310	4,110	2,586	1.01	.63
1973	424,642	4,322	2,651	1.02	.62
1974	441,628	4,545	2,717	1.03	.62
1975	459,293	4,778	2,785	1.04	.61
1976	477,665	5,021	2,855	1.05	.60
1977	496,771	5,276	2,926	1.06	.59
1978	516,642	5,542	2,999	1.07	.58
1979	537,308	5,819	3,074	1.08	.57
1980	558,800	6,110	3,151	1.09	.56

[1] At 4 percent increase over the preceding year, with deposits at the end of 1956 estimated at $218,000 million.

[2] Deposit insurance fund on Dec. 31, 1956, of $1,742,077,000, increased each year by addition of net incom of the Corporation. (See table 2.)

TABLE 4.—*Deposit insurance fund and reserve for losses, and holdings of assets acquired in deposit payoff and deposit assumption cases, 1934–56*

[Amounts in thousands]

Dec. 31	Deposit insurance fund and reserve for losses			Assets acquired in deposit payoff and deposit assumption cases			
	Total	Deposit insurance fund	Reserve for losses [1]	Amount held	Percent of fund and reserve for losses	Amount held in excess of reserve for losses	Percent of deposit insurance fund
1934	$333,393	$333,006	$387	$861	0.26	$474	0.14
1935	309,984	306,057	3,927	9,345	3.01	5,418	1.77
1936	351,113	343,405	7,708	19,099	5.44	11,391	3.32
1937	396,548	383,149	13,399	29,553	7.45	16,154	4.22
1938	441,195	420,545	20,650	47,200	10.70	26,550	6.31
1939	488,244	452,711	35,533	99,764	20.43	64,231	14.19
1940	539,626	495,985	43,641	135,813	25.17	92,172	18.58
1941	597,110	553,499	43,611	125,352	20.99	81,741	14.77
1942	661,527	616,943	43,584	106,640	16.12	62,056	10.06
1943	741,603	703,055	38,548	84,798	11.43	46,250	6.58
1944	835,055	804,341	30,714	56,783	6.80	26,069	3.24
1945	951,711	929,151	22,560	37,682	3.96	15,122	1.63
1946	1,077,477	1,058,485	18,992	24,543	2.28	5,552	.52
1947	1,021,587	1,006,090	15,497	19,076	1.87	3,579	.36
1948	1,079,537	1,065,851	13,686	16,493	1.53	2,807	.26
1949	1,217,558	1,203,943	13,615	15,686	1.29	2,071	.17
1950	1,253,370	1,243,947	9,423	11,738	.94	2,315	.19
1951	1,283,662	1,282,188	1,474	4,514	.35	3,040	.24
1952	1,365,542	1,363,492	2,050	4,075	.30	2,025	.15
1953	1,453,035	1,450,684	2,351	4,455	.31	2,103	.14
1954	1,551,744	1,542,697	9,047	10,152	.65	1,105	.07
1955	1,648,956	1,639,589	9,367	13,719	.83	4,352	.27
1956	1,750,716	1,742,077	8,639	13,064	.75	4,425	.25
June 30, 1940 [2]	508,773	469,564	43,484	146,847	28.86	103,363	22.01

[1] For 1948 and 1949 includes a special reserve for undetermined losses on assets acquired in deposit assumption cases.

[2] Date of maximum holdings of assets acquired in deposit payoff and deposit assumption cases. Includes assets to be acquired in a deposit assumption transaction not completed for which the Corporation had made the necessary commitment of funds.

TABLE 5.—*Disbursements and losses of the Federal Deposit Insurance Corporation in deposit payoff and deposit assumption cases, 1934–56*

[Amounts in thousands]

Year of closing of bank	Disbursements [1]			Losses [4]	Deposit insurance fund, June 30	Ratio to deposit insurance fund at midyear (percent)	
	Total	Principal [2]	Expenses and advances [3]			Disbursements	Losses
1934–56	$339,782	$292,235	$47,547	$29,685		[5] 3.17	[5] 0.28
1934	985	941	44	251	$318,971	.31	.08
1935	9,260	8,890	370	2,814	334,997	2.76	.84
1936	15,782	14,781	1,001	2,526	323,782	4.87	.78
1937	20,145	19,160	985	3,653	364,150	5.53	1.00
1938	35,472	30,479	4,993	2,516	401,999	8.82	.63
1939	85,531	67,770	17,761	7,315	424,482	20.15	1.72
1940	91,437	74,134	17,303	3,963	469,564	19.47	.84
1941	25,406	23,880	1,526	645	523,372	4.85	.12
1942	11,939	10,825	1,114	727	583,887	2.04	.12
1943	7,298	7,172	126	178	658,819	1.11	.03
1944	1,549	1,503	46	49	752,284	.21	.01
1945	1,865	1,768	97		868,469	.21	
1946	276	265	11		992,745	.03	
1947	2,003	1,724	279	74	1,133,687	.18	.01
1948	3,188	2,990	198	640	1,007,417	.32	.06
1949	2,717	2,552	165	369	1,134,213	.24	.03
1950	4,414	3,986	428	1,390	1,277,076	.35	.11
1951	2,002	1,885	117	10	1,243,839	.16	.001
1952	1,547	1,369	178	820	1,322,485	.12	.06
1953	5,333	5,017	316		1,406,628	.38	
1954	975	913	62	114	1,496,692	.07	.01
1955	7,147	6,787	360	492	1,590,541	.45	.03
1956	3,511	3,444	67	1,138	1,690,818	.21	.07

[1] Disbursements are those pertaining to the banks that closed in each year. They do not exactly equal the disbursements made in each year because some portions of the disbursements may have been made in years subsequent to that in which the bank closed.
[2] Deposits paid by FDIC in deposit payoff cases; principal of loan or of assets purchased in deposit assumption cases.
[3] Payoff expenses in deposit payoff cases; liquidation expenses and advances for asset protection in deposit assumption cases.
[4] Losses on principal in both deposit payoff and deposit assumption cases, plus payoff expenses in deposit payoff cases. Liquidation expenses and advances for asset protection have been fully recovered in the deposit assumption cases.
[5] Average of the annual ratios.

NOTE.—Data for recent years subject to adjustment.

TABLE 6.—*Deposits of 25 insured banks relative to the deposit insurance fund, Dec. 31, 1956*

[Amounts in millions]

Size of the 25 largest insured banks [1]		FDIC disbursement in case of financial difficulties if amount needed is— [2]			Percentage of the deposit insurance fund that would be absorbed by such disbursement— [3]		
Rank	Deposits	50 percent deposits	40 percent deposits	30 percent deposits	At 50 percent	At 40 percent	At 30 percent
1	$8,993	$4,497	$3,597	$2,698	258	207	155
2	6,928	3,464	2,771	2,078	199	159	119
3	6,672	3,336	2,669	2,002	192	153	115
4	2,845	1,423	1,138	854	82	65	49
5	2,760	1,380	1,104	828	79	63	48
6	2,649	1,325	1,060	795	76	61	46
7	2,543	1,272	1,017	763	73	58	44
8	2,497	1,249	999	749	72	57	43
9	2,484	1,242	994	745	71	57	43
10	2,338	1,169	935	701	67	54	40
11	1,854	927	742	556	53	43	32
12	1,736	868	694	521	50	40	30
13	1,654	827	662	496	47	38	28
14	1,539	770	616	462	44	35	27
15	1,539	770	616	462	44	35	27
16	1,477	739	591	443	42	34	25
17	1,389	695	556	417	40	32	24
18	1,369	685	548	411	39	31	24
19	1,362	681	545	409	39	31	23
20	1,026	513	410	308	29	24	18
21	957	479	383	287	27	22	16
22	951	476	380	285	27	22	16
23	867	434	347	260	25	20	15
24	863	432	345	259	25	20	15
25	858	429	343	257	25	20	15

[1] Includes 22 insured commercial banks and 3 insured mutual savings banks.
[2] In the banks requiring disbursements by the Corporation during 1934–56, the amount of disbursement (excluding expenses and advances for protection of assets) has ranged from 6 percent to 116 percent. In the case of banks with deposits in excess of $25 million, the range is from 29 percent to 68 percent.
[3] Deposit insurance fund on Dec. 31, 1956, was $1,742 million.

TABLE 7.—*Deposits in insured commercial banks with very small capital ratios, June 30, 1956*

Type of capital ratio	Number of bank	Deposits (in millions)		Ratio of—	
		Total	Insured [1]	Total deposits to deposit insurance fund (percent) [2]	Insured deposits to deposit insurance fund (percent) [2]
Banks with ratios of total capital accounts to total assets of—[3] Less than 5 percent	391	$9,024	$5,576	534	330
2.0 to 2.9 percent	6	124	83	7	5
3.0 to 3.9 percent	70	1,926	1,185	114	70
4.0 to 4.9 percent	315	6,974	4,308	412	255
Banks with ratios of total capital accounts to "assets at risk" of—[4] Less than 10 percent	226	3,567	2,163	211	128
5.0 to 5.9 percent	2	23	15	1	1
6.0 to 6.9 percent	3	37	26	2	2
7.0 to 7.9 percent	29	679	374	40	22
8.0 to 8.9 percent	62	916	562	54	33
9.0 to 9.9 percent	130	1,912	1,186	113	70

[1] Estimated by applying to the total deposits of each bank on June 30, 1956, the ratio of insured to total deposits as reported for its size group on the special call of Sept. 21, 1955.
[2] The deposit insurance fund on June 30, 1956, was $1,691 million.
[3] The ratio of total capital accounts to total assets for all insured commercial banks was 7.7 percent.
[4] "Assets at risk" equal assets, net of valuation reserves less: Cash, balances due from banks, cash items in process of collection, U. S. Government obligations direct or fully guaranteed, loans to farmers directly guaranteed by the Commodity Credit Corporation, and real estate loans insured by the Federal Housing Administration or the Veterans' Administration. For all insured commercial banks the ratio of total capital accounts to "assets at risk" was 16.1 percent.

TABLE 8.—*Bank failures and losses to depositors, commercial banks, 1873–78 and 1930–33*

[Amounts in millions]

Year	Deposits in operating banks [1]	Deposits in failed banks [2]	Disbursements of a hypothetical insurance fund at 50 percent of deposits in failed banks [3]		Losses to depositors in closed banks [2]		Depositors' losses as percentage of deposits in operating banks	
			Amount	Percent of deposits in operating banks	Total	On balances of $5,000 or less	Total losses (percent)	Losses on balances of $5,000 or less (percent)
1873-78		$85.8	$43.0	[4] 3.6	$29.0	$25.3	[5] 2.4	[5] 2.1
1873	$1,211	12.9	6.5	.5	4.1	3.4	.3	.3
1874	1,336	4.4	2.2	.2	1.6	1.4	.1	.1
1875	1,343	13.5	6.8	.5	5.7	4.9	.4	.4
1876	1,300	9.7	4.9	.4	3.3	2.9	.3	.2
1877	1,297	18.7	9.3	.7	5.2	4.6	.4	.4
1878	1,214	26.6	13.3	1.1	9.1	8.1	.7	.7
1930-33		6,830.2	3,415.2	[4] 6.7	1,366.6	922.0	[5] 2.7	[5] 1.8
1930	49,489	837.1	418.6	.8	237.4	158.0	.5	.3
1931	44,687	1,690.2	845.1	1.9	390.5	288.0	.9	.6
1932	36,668	706.2	353.2	1.0	168.3	131.6	.5	.4
1933	33,252	3,596.7	1,798.3	5.4	540.4	344.4	1.6	1.0

[1] Estimated average during the year. Deposits at the beginning of the year 1873 are estimated at $1,200 million, and at the beginning of 1930 at $51,066 million.

[2] For a description of sources of data see the Annual Report of the Federal Deposit Insurance Corporation for 1940, pp. 70–73.

[3] In the 431 banks for which the Federal Deposit Insurance Corporation made disbursements during 1934–56, the principal disbursements were 50 percent of deposits; the total disbursements, including payoff and liquidation expenses and advances for protection of assets were 58 percent of deposits.

[4] Percentage of deposits in operating banks at beginning of the period.

[5] Percentage of deposits in operating banks at beginning of the period. If these rates are adjusted for recoveries from assessments on stockholders, the rates on total deposits are 2.7 percent for 1873–78 and 3.4 percent for 1930–33; those on balances of $5,000 or less are 2.4 percent for 1873–78 and 2.3 percent for 1930–33.

TABLE 9.—*A hypothetical deposit insurance fund for commercial banks in the United States, 1900–30*

[Amounts in thousands]

Year	Assessments, losses, and expenses			Income and size of fund with retention of all net assessment income			
	Assumed assessments [1]	Estimated losses on depositors' balances of $5,000 or less [2]	Assumed operating expenses [3]	Assumed net assessment income [4]	Investment income [5]	Assumed fund at end of year [6]	Estimated ratio of fund at end of year to deposits at midyear (percent) [7]
1900	$5,094	$2,341	$306	$2,447	$1,250	$53,697	0.79
1901	6,086	3,221	365	2,500	1,342	57,539	.71
1902	6,535	1,945	392	4,198	1,438	63,175	.73
1903	6,830	2,439	410	3,981	1,579	68,735	.75
1904	7,304	7,960	438	−1,094	1,718	69,359	.71
1905	8,271	4,724	496	3,051	1,734	74,144	.67
1906	8,843	3,565	531	4,747	1,854	80,745	.68
1907	9,545	18,243	573	−9,271	2,019	73,493	.58
1908	9,319	13,823	559	−5,063	1,837	70,267	.57
1909	10,342	6,215	621	3,506	1,757	75,530	.55
1910	10,983	5,108	659	5,216	1,888	82,634	.56
1911	11,589	4,435	695	6,459	2,066	91,159	.59
1912	12,341	3,223	740	8,378	2,279	101,816	.62
1913	12,606	5,080	756	6,770	2,545	111,131	.66
1914	13,355	7,746	801	4,808	2,778	118,717	.67
1915	13,959	7,711	838	5,410	2,968	127,095	.68
1916	16,960	2,172	1,018	13,770	3,177	144,042	.64
1917	19,876	2,627	1,193	16,056	3,601	163,699	.62
1918	21,531	3,595	1,292	16,644	4,092	184,435	.64
1919	24,941	3,446	1,496	19,999	4,611	209,045	.63
1920	27,512	15,162	1,651	10,699	5,226	224,970	.61
1921	25,074	49,096	1,504	−25,526	5,624	205,068	.61
1922	26,649	33,667	1,599	−8,617	5,127	201,578	.57
1923	28,631	54,804	1,718	−27,891	5,039	178,726	.47
1924	31,007	68,112	1,860	−38,965	4,468	144,229	.35
1925	33,923	53,530	2,035	−21,642	3,606	126,193	.28
1926	35,214	72,358	2,113	−39,257	3,155	90,091	.19
1927	36,528	51,432	2,192	−17,096	2,252	75,247	.15
1928	37,187	37,795	2,231	−2,839	1,881	74,289	.15
1929	37,039	63,880	2,222	−29,063	1,857	47,083	.10
1930	38,450	157,966	2,307	−121,823	1,177	−73,563	−.14

[1] Assessments becoming due during the year, estimated at $0.075 percent of deposits at the middle of the year. This is the average rate of deposit insurance assessments becoming due for the years 1951–56; it is less than 1/12 of 1 percent because of the deductions from deposits that are permitted in calculating assessments, and because assessments becoming due during a year are based on deposits at 4 dates, of which 3 are prior to June 30 of the year in which they become due. The deposits used in the computation are from an unpublished series, subject to revision, compiled by the Board of Governors of the Federal Reserve System with the cooperation of the Federal Deposit Insurance Corporation and the Comptroller of the Currency.

[2] For description of sources of data, see the Annual Report of the Federal Deposit Insurance Corporation for 1940, pp. 70–73.

[3] Estimated at 6 percent of assessments, the annual average for the Federal Deposit Insurance Corporation.

[4] Assumed assessments, less estimated losses on depositors' balances of $5,000 or less and assumed operating expense.

[5] At 2½ percent of the deposit insurance fund at the end of the preceding year.

[6] Initial fund of $50 million, which is ¾ of 1 percent of estimated deposits in commercial banks at the beginning of 1900, plus the increments from assessment income and investments.

[7] The actual ratios at the end of the year would be somewhat lower, because of seasonal variation and growth in deposits.

TABLE 10.—*A hypothetical deposit insurance fund for commercial banks in the United States, 1900–30*

[Amounts in thousands]

Year	Income and size of fund with retention of 40 percent of net assessment income [1]				Income and size of fund with entire net assessment income credited to insured banks [1]			
	Net assessment income retained [2]	Investment income	Assumed fund at end of year	Ratio of fund at end of year to deposits at midyear [3]	Net assessment income retained [4]	Investment income	Assumed fund at end of year	Ratio of fund at end of year to deposits at midyear [3]
				Percent				*Percent*
1900	$979	$1,250	$52,229	0.77	----------	$1,250	$51,250	0.75
1901	1,000	1,306	54,535	.67	----------	1,281	52,531	.65
1902	1,679	1,363	57,577	.66	----------	1,313	53,844	.62
1903	1,592	1,439	60,608	.67	----------	1,346	55,190	.61
1904	−1,094	1,515	61,029	.63	−$1,094	1,380	55,476	.57
1905	1,877	1,526	64,432	.58	1,094	1,387	57,957	.53
1906	1,899	1,611	67,942	.58	----------	1,449	59,406	.50
1907	−9,271	1,699	60,370	.47	−9,271	1,485	51,620	.41
1908	−5,063	1,509	56,816	.46	−5,063	1,291	47,848	.39
1909	3,506	1,420	61,742	.45	3,506	1,196	52,550	.38
1910	5,216	1,543	68,501	.47	5,216	1,314	59,080	.40
1911	5,951	1,713	76,165	.49	5,612	1,477	66,169	.43
1912	3,351	1,904	81,420	.49	----------	1,654	67,823	.41
1913	2,708	2,036	86,164	.51	----------	1,696	69,519	.41
1914	1,923	2,154	90,241	.51	----------	1,738	71,257	.40
1915	2,164	2,256	94,661	.51	----------	1,781	73,038	.39
1916	5,508	2,367	102,536	.45	----------	1,826	74,864	.33
1917	6,422	2,563	111,521	.42	----------	1,872	76,736	.29
1918	6,658	2,788	120,967	.42	----------	1,918	78,654	.27
1919	8,000	3,024	131,991	.40	----------	1,966	80,620	.24
1920	4,280	3,300	139,571	.38	----------	2,016	82,636	.23
1921	−25,526	3,489	117,534	.35	−25,526	2,066	59,176	.18
1922	−8,617	2,938	111,855	.31	−8,617	1,479	52,038	.15
1923	−27,891	2,796	86,760	.23	−27,891	1,301	25,448	.07
1924	−38,965	2,169	49,964	.12	−38,965	636	−12,881	−.03
1925	−21,642	1,249	29,571	.07	−21,642	----------	−34,523	−.08
1926	−39,257	739	−8,947	−.02	−39,257	----------	−73,780	−.16
1927	−17,096	----------	−26,043	−.05	−17,096	----------	−90,876	−.19
1928	−2,839	----------	−28,882	−.06	−2,839	----------	−93,715	−.19
1929	−29,063	----------	−57,945	−.12	−29,063	----------	−122,778	−.25
1930	−121,823	----------	−179,768	−3.5	−121,823	----------	−244,601	−.48

[1] Assumed assessments, losses, operating expenses, initial funds, and rate of investment income the same as in table 9.

[2] 40 percent of net assessment income (except when negative), adjusted in years following a negative assessment income to cover such amounts.

[3] The actual ratios at the end of the year would be somewhat lower because of seasonal variation and growth in deposits.

Negative amounts are losses and expenses in excess of assessments due; positive amounts are the net assessment income in succeeding years sufficient to replace such losses.

TABLE 11.—*Disbursements and portion of funds tied up in assets acquired from failed banks in a hypothetical deposit insurance fund for commercial banks in the United States, 1900–30*

[Amounts in thousands]

Year	Principal disbursements in banks closed during year	Investment at end of year in assets acquired from failed banks			Percentage of fund in assets acquired from failed banks with retention of following percentage of net assessment income		
		From current year's disbursement [2]	From disbursements in prior years [3]	Total	100 percent	40 percent	None
1900	$5,766	$3,425		$3.425	6.4	6.6	6.7
1901	10,447	7,226	$2,055	9,281	16.1	17.0	17.7
1902	6.032	4.087	5,364	9,451	15.0	16.4	17.6
1903	10,275	7,836	4,963	12,799	18.6	21.1	23.2
1904	19,222	11,262	6,651	17.913	25.8	29.4	32.3
1905	11.078	6,354	9.517	15,871	21.4	24.6	27.4
1906	10,234	6.669	7,975	14.644	18.1	21.6	24.7
1907	70,602	52,359	7.033	59,392	80.8	98.4	115.1
1908	36,736	22,913	34,051	56,964	81.1	100.3	119.1
1909	13,786	7,571	30,123	37.694	49.9	61.1	71.7
1910	12,213	7,105	16,653	23,758	28.8	34.7	40.2
1911	11,072	6,637	8,825	15,462	17.0	20.3	23.4
1912	7,853	4,630	6,871	11,501	11.3	14.1	17.0
1913	20,513	15,433	5,480	20,913	18.8	24.3	30.1
1914	18,108	10,362	11,313	21,675	18.3	24.0	30.4
1915	21,874	14,163	11,310	25,473	20.0	26.9	34.9
1916	5,436	3,264	13,150	16,414	11.4	16.0	21.9
1917	7,578	4,951	7,243	12,194	7.4	10.9	15.9
1918	7,717	4,122	5,366	9,488	5.1	7.8	12.1
1919	8,518	5,072	4,284	9,356	4.5	7.1	11.6
1920	32,677	17,515	4,775	22,290	9.9	16.0	27.0
1921	86,403	37,307	12,443	49,750	24.3	42.3	84.1
1922	45,591	11,924	28,146	40,070	19.9	35.8	77.0
1923	74,801	19,997	20,098	40,095	22.4	46.2	157.6
1924	105,075	36,963	19,306	56,269	39.0	112.6	[4]
1925	83,468	29,938	29,369	59,307	47.0	200.6	[4]
1926	130,077	57,719	31,052	88,771	98.5	[4]	[4]
1927	99,666	48,234	47,308	95,542	127.0	[4]	[4]
1928	71,193	33,398	49,250	82,648	111.3	[4]	[4]
1929	115,322	51,442	40,276	91,718	194.8	[4]	[4]
1930	418,548	260,582	45,707	306,289	[4]	[4]	[4]

[1] At ½ of the amount of deposits in the failed banks. For 1934–56 the principal disbursements by the Federal Deposit Insurance Corporation in deposit payoff and deposit assumption cases equaled 50 percent of the deposits of the banks; if payoff and liquidation expenses and advances for protection of assets are included the disbursements equaled 58 percent of the deposits of the banks.

[2] Principal disbursements in excess of losses, on assumptions: (1) that reserves for losses have been established sufficient to meet all losses on the principal disbursements; (2) that payoff and any other nonrecoverable expenses have been charged off; and (3) that by the end of the year recoveries have equaled but not exceeded liquidation expenses and advances for protection of assets. In some of the cases a portion of the recovery on principal would have been received by the end of the year, but neglect of this here is offset by the assumption (see note 3) of a relatively rapid rate of recovery in the succeeding 3 years.

[3] 60 percent of disbursements in excess of losses of the preceding year, plus 30 percent of disbursements in excess of losses of the second preceding year, and plus 10 percent of disbursements in excess of losses on the 3d preceding year, based on assumption that the recoveries on principal disbursements are distributed as follows: 40 percent in the year following the disbursement, 30 percent in the next year, 20 percent the next year, and 10 percent in the next year. This assumes that in all cases the termination of liquidation of the assets is not more than 4 years from the end of the year in which the disbursement occurred.

[4] Fund exhausted.

Table 12.—*Adequacy of borrowing power of a hypothetical deposit insurance fund established in 1900 and operating until 1930*

[Amount in thousands]

Year	Borrowing at end of year			Borrowing as percentage of assured borrowing power [4]
	To hold assets acquired from failed banks [1]	To meet cumulative losses after fund was exhausted [2]	Total [3]	
If fund retained all net assessment income:				
1927	$20,295		$20,295	14
1928	8,359		8,359	6
1929	44,635		44,635	30
1930	306,289	$73,563	379,852	253
If fund retained 40 percent of net assessment income: [5]				
1924	6,305		6,305	4
1925	29,736		29,736	20
1926	88,771	8,947	97,718	65
1927	95,542	26,043	121,585	81
1928	82,648	28,882	111,530	74
1929	91,718	57,945	149,663	100
1930	306,289	179,768	486,057	324
Entire net assessment income credited to insured banks: [6]				
1923	14,647		14,647	10
1924	56,269	12,881	69,150	46
1925	59,307	34,523	93,830	63
1926	88,771	73,780	162,551	108
1927	95,542	90,876	186,418	124
1928	82,648	93,715	176,363	118
1929	91,718	122,778	214,496	143
1930	306,289	244,601	550,890	367

[1] Assets held (see table 11) in excess of the fund (see tables 9 and 10).
[2] Deficit in fund (see tables 9 and 10).
[3] Exclusive of any interest accruing on the borrowings.
[4] On assumption that assured borrowing power was $150 million, or 3 times the assumed initial fund. With these conditions the fund and assured borrowing power together would have been 3 percent of deposits in operating banks at the beginning of operations. The combined fund and assured borrowing power of the Federal Deposit Insurance Corporation at the end of 1956 was 2.2 percent of the deposits in insured banks.
[5] A small amount of borrowing might have been necessary in 1908.
[6] Borrowing of about $9 million would have been necessary in 1907 and about $12 million in 1908.

Explanatory Statement Re Proposed Assessment Base (Proposal by Federal Deposit Insurance Corporation, January 1957)

INTRODUCTION

The Corporation has long recognized the desirability of providing a simplified base or method for the computation of assessments. Numerous plans have been considered in an effort to find one that would meet the objectives of substantially reducing, if not entirely eliminating, the many technical and oftentimes complicated problems arising under the present law and related regulations and interpretations, that would result in a reduction of required recordkeeping and clerical man-hours for the banks and the Corporation, and that would yield approximately the same amount of assessments as obtained under the present base. This objective has also been recognized in recommendations and suggestions by the banking representatives of the industry sub-task forces of the Commission on Organization of the Executive Branch of the Government, the American Bankers Association, the National Association of Bank Auditors and Comptrollers, several of the various State banking associations, and many individual bankers.

In an endeavor to accomplish this end, the Corporation recommends that the pertinent provisions of the Federal Deposit Insurance Act be amended to provide for the assessment base proposed and discussed herein.

PROPOSED BASE

It is proposed that the asssesment be based on the average amount of deposit liabilities reported on two reports of condition in each six-month calendar period after deducting 15 percent from demand deposits and 1 percent from time and savings deposits.

It is intended that the uniform deductions of 15 percent from demand deposits and 1 percent from time and savings deposits shall be in lieu of all deductions permissible under the present act including uncollected cash items in process of collection.

Under this proposed plan, there will be no change from the present requirements of the Comptroller of the Currency and the Federal Reserve Board, for preparing reports of conditions including deposit liabilities. However, State banks not members of the Federal Reserve System, making reports of condition to the Corporation, would be required to report, as deposits, amounts due to any Federal Reserve bank or any other bank for cash letters as represented by outstanding drafts, or other authorizations to charge the reporting bank's account, issued in payment of such cash letters. Federal Reserve member banks, National and State, are now required to report such items as deposit liabilities in their reports of condition but nonmember banks are not now required to do so.

ESTIMATED EFFECT ON THE FUND

It is estimated that if this proposed plan had been in effect during the 6-year period of 1951 through 1956, the banks would have paid and the Corporation retained $5,133,000 less net assessments, for an annual average decrease of $855,500 or 1.3964 percent as compared with the present assessment base.

ESTIMATED EFFECT ON INDIVIDUAL BANKS

Obviously, because of variances in kinds of accounts and predominating type of transactions in the banks, relative effect of this plan on assessments is not the same for each bank as the overall estimated assessment reduction of 1,396 percent.

Since essential data was not readily available for computing the assessment baed on four reports of condition (only two reports a year are made by State nonmember banks) the computations were based on two reports a year. It is traditionally true that deposit liabilities reported in the reports of June 30 and December 31, on which these computations were based, are higher than reported in the preceding spring and fall reports. In considering the data given below, it is necessary to keep in mind that in almost every individual case, assessments would be less when based on 4 reports a year than on 2.

Computations of assessments were made according to the proposed plan and compared with actual assessments paid in the calendar year 1956 for 13,268 banks. (There were 13,449 insured banks as of June 30, 1956, but necessary data for some of them was not readily available.) This study showed that the 13,268 banks, assessments would have been increased for 1,665 of them, and reduced for 11,603.

Those for which increases are indicated are summarized as follows:

Increased assessment	Total	National	State member	State nonmember	Mutuals
Over $1,000	167	106	48	13	
$500 to $1,000	88	47	26	15	
$250 to $500	176	79	38	54	5
$100 to $250	298	107	62	121	8
Under $100	936	340	131	428	37
Total	1,665	679	305	631	50

Those for which decreases are indicated are summarized as follows:

National	3,921
State member	1,514
State nonmember	5,998
Mutuals	170
Total	11,603

Computations for the 167 banks with an indicated annual net increase of more than $1,000 based on 2 reports were also made based on 4 reports of conditions for the year. The results of these computations show that for 28 of those banks, the assessments paid would have been less than under the present base and that for 33 of them, the assessment increase would be less than $1,000 instead of more. This, then, would leave only 106 banks for which the annual net assessment would be increased more than $1,000.

Nevertheless, for some of these banks, the dollar amount of increase would be considerable but not necessarily percentagewise. In a few of these cases for which essential data was available, it appears that if their reports of condition were properly prepared, the computed assessments would have been very substantially less than used herein.

It was also found that without regard to dollar increases, some banks had substantial percentage increases, in 2 cases as much as 54 percent. In many of these cases, it has been found that the increase occurs in banks having a high volume of personal loans where it is the practice to accumulate repayments in a separate deposit ledger control instead of applying on the reduction of the indebtedness. These balances are reported on the reports of condition as deposit liabilities and therefore assessments were computed on them under the proposed base whereas such accounts are not subject to assessment under the present law. This is particularly true of industrial-type banks in North and South Carolina, Florida, Ohio, and some in a few other States.

A summary statement showing the number of banks by percentage increases and decreases is given below:

	Total	National	State member	State nonmember	Mutuals
Increases:					
26 to 54 percent	32	2	3	27	
21 to 25 percent	18	5		13	
16 to 20 percent	53	18	11	24	
11 to 15 percent	102	36	19	47	
6 to 10 percent	277	126	45	106	
0 to 5 percent	1,183	492	227	414	50
Total	1,665	679	305	631	50
Decreases:					
0 to 5 percent	4,337	1,702	674	1,791	170
6 to 10 percent	4,588	1,524	557	2,507	
11 to 15 percent	2,297	609	249	1,439	
16 to 20 percent	363	86	29	248	
21 to 32 percent	17		4	13	
100 percent	1		1		
Total	11,603	3,921	1,514	5,998	170

No mutual savings bank had an increase of more than 2 percent and only 2 had decreases of more than 2 percent; 1 decrease for 3 percent amounted to $148.87 and the 1 for 4 percent amounted to $24.29. The decrease of 100 percent was a trust company which had no deposits to report under the requirements for the reports of condition.

PRINCIPAL ITEMS NOW EXCLUDED FROM BASE, ASSESSED UNDER PROPOSED PLAN

Among the items substantially accounting for increased assessments under the proposed plan are accounts and items required to be reported as deposit liabilities on reports of condition but which are not subject to assessment under existing law. The more important of these include the following:

Accumulated repayments on loans;

Dealers' reserves;

Other cash collateral, including brokers' "overnight" loans which are a very substantial item, particularly in New York banks;

Banks' own expense and dividend checks outstanding;

Banks' own checks for purchase of assets such as securities for their own portfolios.

There is not sufficient reliable data available on which to reliably estimate the effect exclusion of any of these items would have on assessments and the fund.

Accumulated loan repayments reported as deposit liabilities by insured commercial banks were $490 million at December 31, 1955, and $518 million at June 30, 1956. These data were not available for mutual savings banks. However, the exclusion of these items from reports of commercial banks would represent an estimated decrease of $183,000 in net assessments.

Assessments computed at one-twelfth of 1 percent per annum are as follows:

	Annual gross	Estimated net
On each $1,000 of deposit liabilities	$0.83	$0.37
On each $10,000 of deposit liabilities	8.33	3.75
On each $100,000 of deposit liabilities	83.33	37.50
On each $1 million of deposit liabilities	833.33	375.00
On each $100 million of deposit liabilities	83,333.33	37,500.00

REASON FOR NOT PROVIDING FOR EXCLUSIONS OF CERTAIN ACCOUNTS

The primary purpose of proposing a revised method of computing assessments is to simplify the requirements, to reduce the required man-hours of clerical and technical help for the banks and the Corporation, and to eliminate insofar as possible the technical and administrative problems of the banks and the Corporation arising from complicated and technical provisions and interpretations of the law and regulations.

Since the enactment of the Federal Deposit Insurance Act of 1950, which revised some of the requirements for computing assessments, the Corporation has found that substantially all of the problems and differences in interpretations of the law, as between the banks and the Corporation, have been in respect to deductions and exclusions from the assessment base.

It logically follows, therefore, that to the extent exclusions or deductions are permitted, there will arise administrative and technical problems and differences of interpretation. To the extent that exclusions or deductions are permitted, there would also have to be revisions and changes made in the requirements for preparing reports of condition and in the forms of those reports, as well. It is also necessary to give consideration to the effect that any changes in the preparation of reports of condition would have on comparative statistics obtained from those reports and on the computation of reserves required to be maintained by Federal Reserve members.

SOME SPECIAL PROVISIONS OF THE PROPOSED LEGISLATION

Other than for the proposed change in the method of computing assessments, some of the principal provisions of the law believed necessary to proper control and administration are as follows:

Section 7 (a)

Provides that the Board of Directors of the Corporation may define the terms "time and savings deposits" and "demand deposits."

Section 10 (f)

Provides that a certified, signed copy of each report of condition (on which assessments are based) shall be furnished to the Corporation.

Provides that the Comptroller of the Currency, the Federal Reserve Board, and the Federal Reserve banks shall advise the Corporation of any changes made or required to be made in respect to deposit liabilities in any such report of condition.

Section 10 (g)

Provides that reports of condition on which assessments are based shall be as of the same dates for all insured banks and that the Comptroller of the Currency, the Federal Reserve banks, or the Federal Reserve Board and the Directors of the Corporation shall jointly fix such dates.

Provides limitations as to dates for the four reports on which assessments are to be based, viz: Not more than 10 calendar days preceding or following March 31 and September 30, and "as of" one of the last 10 calendar days of June and December.

Provides that any one or all of the agencies may make such additional calls as they desire.

The provisions of these amendments would require the State nonmember banks to include in reported deposit liabilities (see item (9) in the part of sec. 10 (g) detailing items and accounts to be included as deposit liabilities) amounts due to any Federal Reserve bank or any other bank for cash letters as represented by outstanding drafts or other authorizations to charge the reporting bank's account issued in payment of such cash letters. (Federal Reserve member banks are now required to include such items as deposit liabilities in their reports, but nonmember banks are not so required.)

ADVANTAGES OF THE PLAN

Some advantages of the plan are summarized as follows:

1. Eliminates necessity for one set of complicated rules, regulations, instructions, and interpretations for banks to follow and for Corporation to promulgate and administer;
2. Assures attention of top-ranking bank officer to preparation of report on which assessment would be based;
3. Eliminates need for banks to maintain special records for assessment purposes;
4. Would result in substantial savings of time and expense for banks and the Corporation;
5. Would eliminate need for field audits by Corporation resulting in substantial savings in costs (approximately $450,000 a year);
6. Assessment base of all insured banks would be substantially verified without additional cost as bank examiners now review all reports of condition;
7. Would result in greater uniformity of assessment base.

DISADVANTAGES OF THE PLAN

Some of the disadvantages of the plan are summarized as follows:

1. Would require extensive legislative revision;
2. State nonmember banks would have to prepare and file 4 reports of condition each year instead of 2;
3. While on the average the reduced net assessments to be derived by the Corporation amounts to 1.396 percent, the difference to individual banks varies considerably, resulting in decreased assessments to some banks and increases to others. However, the banks would save on operating costs incurred in maintaining assessment records and preparing certified statements under present requirements. This saving in operating costs may well fully compensate the few banks which would pay an increased assessment under this proposal.

AN ALTERNATIVE BASE

Some suggestions and recommendations have been made for the adoption of this proposed plan (and for some others) with the provision that banks should have the privilege of computing assessments according to whatever new formula is provided, or, if they prefer, in accordance with the present base.

The permissive use of alternate bases for the computation of assessments is objectionable and undesirable for several reasons, including:

1. Such a plan would not attain the primary objective of establishing a simplified assessment base for the benefit of all banks and the Corporation;
2. It would leave the Corporation with the administrative problems arising not only from the present base but those arising from the administration of one additional set of laws, regulations, and interpretations;
3. It would leave the Corporation with a problem of planning for the workload involved and maintaining a staff of field assessment auditors since the banks would presumably have the privilege of changing from one base to another at their pleasure;
4. It would further reduce the increment to the fund from assessments as each bank would use the base resulting in the lower assessment.

OTHER PLANS CONSIDERED

Among other bases developed and studied by the Corporation were the following:

1. An assessment at an adjusted rate, to yield approximately the same amount as under the present base, computed on total deposit liabilities as shown by reports of condition without any deductions or exclusions.
2. At one-twelfth of 1 percent based on total deposit liabilities as shown by reports of condition without any deductions.

3. At one-twelfth of 1 percent on total deposit liabilities as shown by reports of condition with a flat deduction of 10 percent.
4. At one-twelfth of 1 percent of total deposit liabilities less cash items in process of collection as shown by reports of condition.
5. At one-twelfth of 1 percent per annum on total deposit liabilities as shown by reports of condition—
(*a*) less one-half of 1 percent of time and savings deposits and 15 percent of demand deposits;
(*b*) less three-quarters of 1 percent of time and savings deposits and 15 percent of demand deposits;
(*c*) less 1½ percent of time and savings deposits and 16 percent of demand deposits;
(*d*) less 1 percent of time and savings deposits and 16 percent of demand deposits;
(*e*) less 1½ percent of time and savings deposits and 16 percent of demand deposits;
(*f*) less 1 percent of time and savings deposits and 20 percent of demand deposits.

Among the plans and suggestions presented by others which were studied and considered were the following:

1. Several derivations of a plan whereby a factor to be applied to net deposit liabilities shown in reports of condition (total deposit liabilities less uncollected cash items in process of collection) would be determined and fixed for each bank according to the relationship of the 5-year sum of annual averages of the assessment base as shown on certified statements submitted for 1951 through 1955 to the 5-year sum of annual averages of net deposit liabilities as shown in reports of condition during the same period. (This would result in a different effective factor (rate) for each of the more than 13,000 insured banks.)
2. A plan somewhat similar to the foregoing (1 above) with a provision for permissive use of the present base as an alternative.
3. A plan to compute assessments on total deposit liabilities less 10 percent with the present base as an alternative. (It was estimated that such a plan would be beneficial to all but about 600 banks which would probably continue to use the present base.)

CONCLUSION

All of the foregoing plans were studied and considered before it was decided that the plan proposed herein should be recommended for adoption.

This decision was reached on the basis that this plan is probably the most direct and simple; it results in a comparatively reasonable reduction in assessments, which will be partially offset by a substantial savings in administrative (auditing) expenses; it affects only a comparatively small number of banks adversely through increased assessments which will be substantially offset by the savings in clerical man-hours from which all banks will benefit, and it will eliminate many administrative and legal problems for all banks and the Corporation.

W. G. LOEFFLER, *Controller.*

JANUARY 11, 1957.

Senator BRICKER. There are several letters which will be inserted in the record at this point.

(The letters referred to follow:)

CONGRESS OF THE UNITED STATES,
HOUSE OF REPRESENTATIVES,
Washington, D. C., February 11, 1957.

Senator J. W. FULBRIGHT,
Chairman, Senate Committee on Banking and Currency,
301 Senate Office Building, Washington, D. C.

DEAR SENATOR FULBRIGHT: Enclosed is a telegram from Mr. W. H. Martin, treasurer-manager of the Livingston Northern Pacific Employees Federal Credit Union opposing parts of the Financial Institutions Act of 1957.

I feel as he does. I feel that the type of local economic self-protection, furnished by credit unions, should be encouraged to grow instead of being knocked in the head. Since economically sound family farms in many areas of our Nation require a capital investment of upward of $200,000, it seems to me that the existing loan authority should be maintained. If the authority is reduced, it would take smaller credit unions out of the business of making loans for larger home appliances and automobiles.

I will appreciate having this letter and the enclosure made a part of your hearing record.

Sincerely,

LEE METCALF.

LIVINGSTON, MONT., *February 8, 1957.*

Representative LEE METCALF,
House of Representatives,
Washington, D. C.:

We ask that you oppose and vote against the advancement or passage of Senate bill as presented by Senator A. Willis Robertson to restrict Federal credit unions from making loans on automobiles and home appliances. Also contained in this bill to give Director of Federal Credit Unions power to set the amount credit unions may lend on a loan secured by collateral. Also the provision requiring that credit unions be examined by local C. P. A. in addition to Federal examinations.

LIVINGSTON NORTHERN PACIFIC EMPLOYEES
FEDERAL CREDIT UNION,
By W. H. MARTIN, *Treasurer-Manager.*

THE NEW YORK FURNITURE HOUSE, INC.,
Denver, Colo., February 12, 1957.

Mr. J. H. YINGLING,
Chief Clerk, United States Senate,
Committee on Banking and Currency,
Washington, D. C.

DEAR MR. YINGLING: The elimination of mandatory cumulative voting will result in an actual financial loss to the 500,000 public stockholders in our national banks.

Mandatory cumulative voting is a valuable property right and the destruction of this right will hurt the market value of bank stocks. And in the case of country banks, the decline in market values may turn out to be ruinous. For this reason I request that the mandatory cumulative voting provision that has worked so well for more than two decades be kept as a part of our national banking system.

Please make this a part of the hearings on the Financial Institutions Act of 1957.

Sincerely yours,

MARVIN SILVERBERG.

GONSER REALTY CO.,
Denver 2, Colo., February 12, 1957.

Mr. J. H. YINGLING,
Chief Clerk, Senate Committee on Banking and Currency,
Senate Office Building, Washington, D. C.

DEAR MR. YINGLING: The real reasons why bank managers want mandatory cumulative voting eliminated has never been made clear by them. I think that it should be stated in the record why bank managers really want cumulative voting eliminated. Following is a list of the reasons for their desire to eliminate mandatory cumulative voting:

1. The elimination of mandatory cumulative voting will permit bank managers to select their directors on a discriminatory basis if they wish.

2. Where bank managers represent a few wealthy stockholders in the bank, the elimination of mandatory cumulative voting will mean that they can keep the bank dividend very low for the purpose of aiding these wealthy individuals in keeping their income taxes low. The public stockholders who wish to receive a reasonable dividend will not be permitted to have a spokesman on the board protecting their interest.

3. Under cumulative voting the public stockholders are permitted to elect directors who will represent them. These directors in turn elect the president of the bank. After the elimination of mandatory cumulative voting, the bank presidents will be able to select all the directors for the bank and thus the employees become the masters of the owners.

Yours very truly,

EUGENE ZEITLIN,
National Bank Stockholder.

Senator BRICKER. We will now recess until 10 o'clock tomorrow morning.

(Whereupon, at 12:10 p. m., the subcommittee recessed until 10 a. m., Friday, February 15, 1957.)

STUDY OF BANKING LAWS

(Financial Institutions Act of 1957)

FRIDAY, FEBRUARY 15, 1957

United States Senate,
Committee on Banking and Currency,
Subcommittee on Banking,
Washington, D. C.

The subcommittee met, pursuant to recess, in room 301, Senate Office Building, at 10 a. m., Senator A. Willis Robertson (chairman of the subcommittee) presiding.

Present: Senators Robertson, Sparkman, Douglas, Monroney, Bricker, and Bush.

Senator Robertson. The subcommittee will please come to order.

We have with us today representatives of the Federal Home Loan Bank Board. The committee will be glad to hear from the Chairman of that Board at this time.

STATEMENTS OF ALBERT J. ROBERTSON, CHAIRMAN; IRA DIXON AND WILLIAM J. HALLAHAN, MEMBERS, FEDERAL HOME LOAN BANK BOARD

Mr. Robertson. Thank you, sir.

Senator Robertson. You may proceed.

Mr. Robertson. Mr. Chairman, my colleagues on the Federal Home Loan Bank Board, Mr. Ira Dixon and Mr. William J. Hallahan, and I are honored to have this opportunity to appear before you to testify with respect to the committee print for a Financial Institutions Act of 1957.

At the outset, please permit us to commend you, your committee, and its able staff for your effective efforts to bring together into one act the Federal laws relating to financial institutions. We are sure that when this is accomplished it will be helpful to all of us who work and operate under these laws.

The provisions in the committee print which directly affect the operations of our Board appear in titles IV, V, and VI. We favor and support most of the provisions in these three titles. In the interest of brevity we shall not comment on those parts of the bill with which we are in accord. Our comments this morning will relate to provisions of the committee print as to which there are some areas of disagreement which we should like to discuss with you and to some recommendations previously made by the Board to the committee which do not appear in the committee print. There are also some technical amendments which we should like to call to your attention for such action as you may wish to take.

We note that our first general recommendation, relating to the relationships between savings and loan associations and affiliates, and our second general recommendation, relating to the strengthening of our examination powers, have not been carried into the committee print.

These two recommendations appear at page 148 of the compilation of October 12, 1956, and were designed, first, to give the Board express power to make rules and regulations with respect to the relationships of and business transactions between members of the Federal home loan banks and institutions the accounts of which are insured by the Federal Savings and Loan Insurance Corporation and individuals, corporations, and organizations that are affiliated with such institutions; second, to authorize the Board to provide for the examination of such affiliates; and, third, to give it adequate power to provide for the examination of uninsured Federal Home Loan Bank members.

The Advisory Committee, in its report of December 17, 1956, disapproved the first of these recommendations on the ground of (*a*) insufficient information on which to appraise it, (*b*) what it termed the general and indefinite authority conferred on the Board in its legislative proposal, and (*c*) what it regarded as the absence of appropriate statutory tests and standards to govern the administration and enforcement of the provisions. It disapproved the second recommendation, relating to examinations, on the ground that an adequate case had not been made in support of the recommendation.

The Board's purpose was to prevent self-dealing, which can impair the safety and soundness of the institution and increase the risk of the Federal Savings and Loan Insurance Corporation. Actual experience over the years has shown the need for such examination and regulatory authority. The Board realizes that some activities which would fall within the definition of "affiliate" in the original proposal would not come within the scope of its objective, and it would have no intention of concerning itself with them under that proposal. The Board realizes that its proposal is broad in scope, and would appreciate any modification or limitation that would not affect the accomplishment of the purpose sought.

Likewise, the committee print does not contain the legislation requested in the third general recommendation of the Board, which appears at page 149 of the compilation of October 12. The object of this recommendation was to make uninsured members of the Federal Home Loan Bank System subject to the same regulation as insured institutions with respect to advertising, sales plans and practices, and other operating practices.

Senator BRICKER. Do you not have that power now?

Mr. ROBERTSON. No; we do not.

The Advisory Committee disapproved this recommendation on the same ground as in the case of the second recommendation, namely, that an adequate case had not been made in support of it.

Senator BRICKER. That covers the situation where every once in a while there breaks out a lot of giveaway programs for deposits and that kind of thing?

Mr. ROBERTSON. Yes, sir.

Senator BRICKER. Skillets, toasters, and the like?

Mr. DIXON. Radios?

Senator BRICKER. Yes.

Mr. ROBERTSON. Again the Board wishes to assure the committee that the Board's recommendation was not made without actual experience to support it. However, the Board wishes to offer an alternative proposal for consideration if the committee is not inclined to accept the original wording. Accordingly, there is submitted as amendment No. 1 in addendum A a suggested modification which would confer on the Board power to regulate advertising and sales plans and practices of uninsured bank members to the same extent as in the case of insured institutions, but which would not confer on the Board power to regulate "other operating practices" of such uninsured members as originally suggested by the Board.

The fourth general recommendation of the Board, appearing at page 150 of the October 12 compilation, is likewise not contained in the committee print. That recommendation, if adopted, would have given the Federal Home Loan Bank Board power with respect to the removal or suspension of any director or officer of a Federal home-loan bank member or an institution insured by the Federal Savings and Loan Insurance Corporation, where such director or officer violated any law or regulation relating to the institution, engaged in unsafe or unsound practices in conducting its business, or violated his duty to the institution as a director or officer. It was related to that portion of item 144, at page 178 of the compilation of October 12, which would have conferred on the Board authority to suspend or remove any director or officer of a Federal savings and loan association on similar grounds.

The Advisory Committee disapproved this recommendation on the ground that it seemed unduly stringent and severe and would result in too great a concentration of power in the Board without adequate safeguards.

So far as it concerns insured institutions, the Board is unable to agree that the proposed provision would be too stringent or too severe. The importance of protection of the investing public and the Federal Savings and Loan Insurance Corporation would indicate that the Board should have effective authority to separate from the management of an insured institution a director or officer whose violation of law or regulation, unsafe or unsound practices, or breach of duty threatens the safety of the institution. Clearly, this is a less stringent and less severe step than termination of the institution's insurance. As to the question of adequate safeguards, the proposal as submitted by the Board provides, by incorporation of provisions proposed with relation to item 144, for hearing in accordance with the Administrative Procedure Act and for court review.

Senator BRICKER. You could have members of the Federal Home Loan Bank that do not have insurance?

Mr. ROBERTSON. Yes, sir.

Senator BRICKER. Would you favor all those who are members of the Federal home loan bank having to also take out insurance?

Mr. ROBERTSON. That is a question that has been raised and discussed many times. I have no individual opinion. I would like to have Mr. Dixon or Mr. Hallahan comment on that.

Mr. DIXON. Personally, Senator, I would like to have them insured if they are a bank member. However, it might——

Senator BRICKER. That situation then would make it parallel to the bank situation?

Mr. DIXON. Yes, all bank members——

Senator BRICKER. Have to have insurance?

Dr. DIXON. All members of the bank system are insured. We operate just exactly opposite.

Senator BRICKER. Yes.

Mr. DIXON. We have members that are not insured. I think you have insured institutions that are not members.

Senator BRICKER. Yes.

Mr. DIXON. So it just reverses the process.

Senator BRICKER. What is the reason for that? Just an historical reason? The way it grew up?

Mr. DIXON. I think it is just historical, yes.

Mr. ROGERS. Mr. Dixon, then is not your present policy not to admit new members unless they are insured?

Mr. DIXON. No, it is not.

Mr. ROGERS. It is not? I'm sorry.

Mr. DIXON. No, we have admitted many members without insurance.

Mr. ROGERS. That clarifies it.

Mr. ROBERTSON. Should the committee, however, deem it inadvisable to make these provisions applicable to uninsured Federal home-loan bank members, it might desire to consider the language in amendment No. 2 in addendum A, which would have the effect of limiting the Board's proposal on this matter to institutions whose accounts are insured by the Federal Savings and Loan Insurance Corporation.

The sixth and last general recommendation of the Board, which appears at page 150 of the October 12 compilation, was likewise not adopted. That recommendation pointed out that the Board had under consideration the adoption of regulations laying down procedures and standards for cases in which Federal savings and loan associations undertake to convert into State-chartered nonmutual institutions, and pointed out that the same problems arise where the institution which is converting from mutual to nonmutual operation is a State-chartered institution. Accordingly, it suggested that the Board be given comparable power to regulate such conversions of State-chartered institutions the accounts of which are insured by the Federal Savings and Loan Insurance Corporation.

The advisory committee, at page 36 of its report, stated that it disapproved the requested extension of the power of the Board over insured State-chartered institutions "on the ground that control over such a conversion of a noninsured institution should lie with the authorities of the State concerned and not with Federal authorities." It would appear that the advisory committee report involves an inconsistency, in that while the Board's proposal pertains only to insured State institutions the reason given for its disapproval pertains to noninsured institutions.

Senator BRICKER. Of course, there would be no way you could have jurisdiction over the noninsured institutions.

Mr. ROBERTSON. No, sir. It may be, of course, that the word "noninsured" as used by the advisory committee is a typographical error, and that the committee meant to take the position that, even where the accounts of the institution are insured by an instrumentality of the United States, the Federal Government does not have a sufficient interest to warrant the conferring of this regulatory authority. The Board believes that, where these institutions have sought and obtained the protection of Federal insurance for their shareholders and have held out to the public that their investments are protected by such insurance, there is every reason to extend reasonable assurance that their rights and interests will not be left unprotected by the Federal Government in the case of such conversions.

Senator BRICKER. On the advisory committee there were practical savings and loan people; were there not?

Mr. ROBERTSON. Yes, sir.

Senator BRICKER. I wonder why they slipped up on it. Was there any dissent to it? Do you know?

Mr. ROBERTSON. I do not know, sir.

Senator BRICKER. Well, I will check on it.

Mr. ROBERTSON. To make completely clear the authority of the Board, we believe that amendment No. 3 in addendum A, which would carry into the committee print the original proposal of the Board, should be adopted. In any event, we are of the opinion that the right to protect the interests of the holders of savings accounts in such institutions involves matters concerning which the Congress may wish to give serious consideration.

Senator ROBERTSON. Mr. Robertson, I have taken the liberty of checking ahead of you the main items in your 22-page statement in which you renew your advocacy of proposals that you previously made and which were turned down by our advisory committee on the protest of the savings and loan representatives.

Are you aware of the fact that these recommendations of yours which you have already made and which you propose to make and which we left out are objectional to the savings and loan associations, that they do not want them? And if they do not want them, when we are trying to get a bill through to codify the law, very voluminous, rather technical, which does have some improvement with respect to this phase of credit, certainly a number of improvements in the Federal Reserve Act and the National Banking Act, are you recommending to us that we go out of our way to antagonize and cause opposition from all the savings and loan associations over some technical amendments that you think you ought to have?

Mr. ROBERTSON. We do not want to antagonize any group.

Senator ROBERTSON. You recognize they are against these amendments, and that is the reason we did not put them in. Is that not a fact?

Mr. ROBERTSON. I would assume that that was true.

Senator ROBERTSON. All right. You may proceed. I just wanted the record to show what we were up against from this side of the table.

Mr. ROBERTSON. Yes, sir.

We should now like to comment upon some of the provisions in titles IV, V, and VI of the committee print. For ease of reference we shall comment upon these provisions in the order in which they appear in the print.

Title IV deals with the Federal Home Loan Bank Act, and the first section on which we would like to comment is section 5A. This section deals with the liquidity which is required of member institutions in the Federal home-loan banks. Under existing law and the committee print, the liquidity is in the form of cash and obligations of the United States as fixed by the Board, but not less than 4 percent nor more than 8 percent of the institution's obligation on withdrawable accounts, or such base as the Board may determine to be comparable in the case of members which are insurance companies.

As pointed out in our testimony before the committee last November, it has been felt for some time that this provision does not adequately reflect the concept of liquidity as a net amount of cash and obligations of the United States over and above the association's current liabilities. In light of this fact, the Board proposed, in item 121, that the section be amended so as to provide that a member's liquidity be a net liquidity over and above the amount of specified liabilities, and specific language was submitted by the Board, which appears at page 339 of the printed hearings of November 9 and 10.

The advisory committee disapproved this item of the Board's recommendations but gave no reason for the disapproval. We feel that, for the protection of the Federal home-loan banks and the member institutions themselves, the proposal should be adopted. We are now undertaking to work out a formula which will achieve the desired result without being burdensome and are in the process of testing specific suggested formulas to that end. However, the Board's ability to deal with the situation will depend on the enactment of legislation giving it the necessary authority.

Next, the Board calls attention to section 13 of title IV of the committee print. First, we wish to withdraw the proposal in item 132 which resulted in adding to this section the sentence which appears as the last sentence of this section. This sentence relates to the exemption of obligations of the Federal home-loan banks from State and local taxation and would provide in effect that such exemption shall extend not only to taxation which in the technical legal sense is "imposed on" such obligations or the principal or interest thereof, but also to taxation which in the technical legal sense is merely "measured by" such obligations or such principal or interest. Representations have been made to the Board that this sentence would raise certain policy and legal questions with respect to the overall fiscal operations of the Government.

Mr. Chairman, there follow now some purely technical amendments.

Senator ROBERTSON. Without objection, they may appear in the record without your having to read them.

(The technical amendments referred to follow:)

In addition, and as a separate matter, it appears that the reenactment of existing exemption provisions of section 13 would raise legal questions as to the continued applicability of the Public Debt Act of 1941, as amended. In order to obviate such questions, the Board recommends that there be added to section 13 the following new sentence: "Nothing in this section shall affect the applicability of the Public Debt Act of 1941, as amended and in force immediately prior to the effective date of this sentence or as heretofore in force."

With respect to the provisions of section 14 as to the use of the Federal home-loan banks as depositaries of public money, a similar problem arises from the reenactment of provisions of section 15 of the Federal Reserve Act in subsection (b) of section 15 in title II of the committee print. The Board recommends that for the clarification of this matter the following new sentence be added to section 14, at page 196, of the committee print: "The provisions of this section shall not be affected by section 15 of the Federal Reserve Act or any other provision of law."

The next section in title IV, which is section 15 at page 196 of the committee print, would provide that obligations of the Federal home-loan banks issued with the approval of the Board shall be lawful investments and may be accepted as security for certain fiduciary, trust, and public or other funds. Request has been made to the Board that steps be taken to eliminate the possibility that this provision might be construed as authorizing the Federal Reserve banks to invest in such obligations, and to that end the Board recommends that the following amendment to the committee print be made: At page 197, line 3, strike the period and insert a colon and the following: "*Provided*, That nothing in this sentence shall authorize the investment of funds of any Federal Reserve bank in such obligations."

Mr. ROBERTSON. Section 17, at page 197, is the next section with respect to which the Board has comments. Subsections (a) and (b) are in satisfactory form as far as they go, but the Board again urges, as it urged in item 135 of the compilation of October 12, that the following sentence be added to subsection (a):

The Board may, from time to time, make such provisions as it may deem appropriate for the exercise of its functions through meetings or otherwise and such provisions as it may deem appropriate authorizing the performance by any officer or employee of the Board or of the Federal Savings and Loan Insurance Corporation of any function of the Board or authorizing the performance by any such officer or employee of any function of said Corporation.

As was noted in our testimony on November 10, the objectives of this provision are, first, to confer on the Board express authority to make provision for the exercise of its functions at times when it may not be possible to assemble a sufficient number of members to hold a formal meeting and, second, to permit the Board to make responsible and effective delegations of functions.

In connection with the first objective, the Board has in mind the possibility of the occurrence of national emergencies, as well as the fact that the authorities and responsibilities of the Board are at all times of such importance to the safety of savings and loan institutions and their investors that there should not be even brief periods when they could not be speedily and effectively exercised.

With regard to the second objective, the making of responsible and effective delegations, the advisory committee disapproved this recommendation on the ground that it fails to prohibit the delegation of judicial and legislative functions of the Board. The Board certainly has no intention of delegating its authority to make regulations or its authority to terminate membership or insurance or to appoint conservators or receivers, and would welcome such limitations as the committee might deem proper as to these matters.

The remaining portion of section 17 is subsection (c), which is designed to free the Board and the Federal Savings and Loan Insurance Corporation from the effects of restrictive statutes as to their powers with respect to their financial transactions, their personnel, and their property, funds, and receipts, and to give them the same freedom in this respect "as the Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation, respectively, now have." We have been advised by the Bureau of the Budget that the Civil Service Commission, the General Accounting Office, and said Bureau object to this provision, and that its enactment would not be in accord with the program of the President.

We have also been advised by the Bureau that the first sentence of section 19, which provides that the Board shall have power to select, employ, and fix the compensation of personnel without regard to the provisions of other laws applicable to the employment or compensation of officers, employees, attorneys, and agents of the United States, is objected to by the Civil Service Commission and said Bureau, and that its enactment would not be in accord with the program of the President.

Senator BRICKER. What has the President ever said about it?

Senator DOUGLAS. You presume the Budget Bureau speaks for the President?

Mr. ROBERTSON. That is right, sir.

Mr. ROGERS. Mr. Chairman, that confuses me because I think that is a reenactment of the present law.

Mr. ROBERTSON. We also have two further comments with respect to section 19. The first of these comments relates to the provision that the receipts of the Board, except from consolidated Federal home-loan bank bonds, and debentures, shall be deposited in the Treasury of the United States. While this would be a reenactment of language now appearing in section 19, the existing language has been affected by a provision of the Independent Offices Appropriation Act, 1944, providing for deposit of these funds with the Treasurer of the United States as therein provided, in lieu of deposit in the Treasury.

The object of this provision was to eliminate the delays and inconveniences arising from the covering of these funds into and out of the Treasury and from the necessity of treating them as appropriated funds.

Accordingly, we recommend that at page 200, lines 3 and 4, of the committee print, the language—

in the Treasury of the United States—

be deleted and the language—

with the Treasurer of the United States in a special deposit checking account or accounts

inserted in lieu thereof.

Second, we call attention to the provisions of subsection (b) of section 19, which provides that it shall not be lawful for any employee or former employee of the Board to accept employment with any member of a Federal home-loan bank except pursuant to the regulations prescribed by the Board, and which provides punishment by fine of not over $10,000 or imprisonment for not more than 5 years, or both, for violation of the subsection. The Board feels that this subsection should be amended, first, to limit the restriction on former employees to a period of 2 years after the termination of employment; second, to exclude former employees who are such only by reason of employment which terminated before the effective date of the new provision; and, third, to make the provision applicable to employees and former employees of the Federal Savings and Loan Insurance Corporation as well as those of the Board. Legislative language to accomplish these purposes is set forth in amendment No. 4 in addendum A.

In subsection (a) of section 21, which authorizes certain agencies to make reports and information available to the Board and to render certain other types of assistance to it, the Board feels that this subsection should be broadened to include the Federal Deposit Insurance Corporation among the agencies authorized to render this cooperation to the Board. Accordingly, the Board recommends that at page 200, line 33, of the committee print, after the language "Board of Governors of the Federal Reserve System" there be added a comma and the language "the Federal Deposit Insurance Corporation."

The Board has only one remaining comment as to title IV, and that is to suggest the elimination of section 23 at page 201 of the committee print. This section permits credit organizations composed exclusively of savings and loan associations and similar institutions or composed exclusively of savings banks, and including in either case a majority of those institutions organized within a State, to become Federal home-loan bank members under specified terms and conditions. This section has never been used, and the Board sees no good reason to retain it in the Federal Home Loan Bank Act.

We now have on title V the next two paragraphs which are purely technical matters.

(The technical amendments referred to follow:)

Coming now to title V, which would amend and rename the Home Owners' Loan Act of 1933, our first comment is to subdivision (b) of section 2, page 203.

This subsection defines two terms, "home mortgage" and "first mortgage," which were used in connection with the Home Owners' Loan Corporation but not in connection with Federal savings and loan associations. The Board suggests that this subsection be deleted as obsolete. However, the term "State" should be defined as including Puerto Rico, and the Board suggests therefore that a new subsection (b) be inserted as follows: "(b) The term 'State' includes Puerto Rico."

Also, section 3, repealing the provisions of the Federal Home Loan Bank Act for direct loans to homeowners, is long since obsolete and should be deleted. However, it would be undesirable to change the succeeding section numbers, particularly in the case of section 5, as there are references to that section by number in various State enabling acts. For this reason the Board recommends that section 8 at page 214, which relates to the territorial applicability of the act, be renumbered as section 3 and inserted in lieu of existing section 3. In making this change, section 8 (which would thus become sec. 3) should be amended by inserting after the language "District of Columbia" a comma and the language "Puerto Rico."

Mr. ROBERTSON. The next subject of comment is subsection (d) of Section 5, at page 205 of the committee print. This subsection deals with administrative and court proceedings for enforcement of the Board's powers, including the appointment of conservators, receivers, and supervisory representatives in charge, for Federal savings and loan associations.

In item 144 at page 178 of the committee compilation of October 12, we recommended a complete revision of this subsection. The objectives of the revision were to speed up judicial review; to provide that such review be on the basis set forth in the Administrative Procedure Act, that is, on the issue of substantial evidence, rather than on the weight of the evidence; to authorize the Board, subject to hearing and court review, to remove or suspend a director or officer of a Federal savings and loan association for violation of law or regulation, unsafe or unsound practices, or violation of duty to the association as a director or officer; and to deal with situations involving the termination of the Federal home-loan bank membership or the insured status of Federal savings and loan associations, which are required by law to have such membership and insurance.

The Advisory Committee, at page 39 of its report, disapproved the Board's proposed revision on the ground that the remedy sought seemed unduly stringent and severe and would result in too great a concentration of power in the Board without adequate safeguards.

The Board invites the committee to review the recommended revision in the light of the objectives sought, and is confident that it will conclude that the provisions are no more stringent or severe than is necessary for adequate protection of the investing public and the Federal Savings and Loan Insurance Corporation. In order that this adequate protection may not be lacking, the Board again urges the adoption of its proposal.

The Board wishes to call attention to the proposal by a previous witness to insert in subsection (d) the following language:

> No supervisory representative in charge, conservator, or receiver shall be appointed for a solvent and nonimpaired institution if the alleged wrongdoing can be corrected as provided in this section, or otherwise by law, without the seizure of private property.

This provision might compel the Board to sit idly by while the reserves and surplus of associations were being dissipated through self-dealing or mismanagement by directors or officials.

In any case, the Board feels that in no event should the authority of the Board to appoint a legal custodian for the protection of the association and its investors be clouded by such a provision as this.

The next two paragraphs are technical, and I would like to resume with the paragraph beginning "section 6."

Senator ROBERTSON. Without objection, you may skip that portion. It will appear in the record.

You may proceed.

(The technical amendments referred to follow:)

Subsection (g), at page 208 of the committee print, deals with the taxation of Federal savings and loan associations and of their shares and the income therefrom. Here again the reenactment might raise legal questions as to the continued applicability of the Public Debt Act of 1941, as amended. We recommend that there be added to this subsection the following new sentence: "Nothing in this subsection shall affect the applicability of the Public Debt Act of 1941 as amended and in force immediately prior to the effective date of this sentence or as heretofore in force." Also, the Board notes that the language "sections 1410 and 1600 of the Internal Revenue Code" appearing in this subsection should be changed to read "sections 1410 and 1600 of the Internal Revenue Code of 1939 or sections 3111 and 3301 of the Internal Revenue Code of 1954."

In subsection (j), at page 210, the language "including any having outstanding shares held by the Secretary of the Treasury or Home Owners' Loan Corporation" should be deleted as obsolete, and the language "Home Loan Bank Board" in the ninth line of the subsection should be changed to "Board."

Mr. ROBERTSON. Section 6, at page 211 of the committee print, deals with branches of Federal savings and loan associations. We are not in favor of this provision on the primary ground that it would forbid branches of Federal savings and loan associations in States which did not permit branches for their own financial institutions but at the same time exposed Federal savings and loan associations to the practical consequences of branch operations by permitting their banks to conduct chain, group, or affiliate operations. In some localities, notably in Florida, chain banking is in effect branch banking, and the only way in which Federal savings and loan associations can meet the impact of such an operation is through branches.

We are of the opinion that branching operations have a definite place in the savings and loan field. In some instances a branch may serve the needs of a particular area better than a new institution and may involve less risk to the Federal Savings and Loan Insurance Corporation, as in cases where the proposed location needs the services of a savings and loan association but does not have sufficient population to support an independent institution. On the other hand, branches should not be allowed to usurp the field.

Senator BRICKER. It would be mighty hard at the present time to get a new one started, would it not, either to get capital in the beginning or to get the return adequate to build up their reserves?

Mr. ROBERTSON. That may be true, although we are receiving a number of applications.

Senator BRICKER. Are you? At the present time? Any in my State?

Mr. DIXON. No.

Mr. ROBERTSON. The Board feels that in view of the risks to be assumed by the Federal Savings and Loan Insurance Corporation the establishment of branches by State-chartered insured institutions should require the prior approval of the Insurance Corporation. Amendment No. 5 in addendum A would accomplish this purpose and we recommend its adoption.

Senator BRICKER. At the present time the insurance on the parent institution would follow to the branch?

Mr. ROBERTSON. That is right.

Subsections (a) and (b) of section 7, at pages 212 and 213 of the committee print, would deal with the purchase or sale of property by a Federal savings and loan association from or to any of its directors or any firm of which any director was a member. Such transactions would be expressly permitted if in the regular course of business and on terms not less favorable to the association in the case of a purchase, or not more favorable to the director or firm in the case of a sale, than those offered to others. Even if these conditions were not met, such transactions would be expressly permitted if authorized by a majority of the directors, and the language of the provision would apparently permit even interested directors to form a part or all of such majority with the single exception that where the purchase was by the association a director interested in the sale would be excluded.

The Board does not favor the enactment of subsections (a) and (b) aforesaid for the reason that they would, it feels, effect a substantial weakening of the fiduciary duties and obligations applicable to the directors of these mutual institutions. As a longstanding matter of policy and regulation the Board has endeavored to prevent self-dealing by directors, officers, or employees with the association with which they are associated. Thus, by regulation, no Federal association may make a real-estate loan to a director, officer, or employee of the association, or to any attorney or firm of attorneys regularly serving the association, or to any partnership or corporation in which any such persons are interested, with only these two exceptions: (1) where the loan is made on the security of a first lien on the home or combination home and business property owned and occupied by such person, or (2) where such person does not own in excess of 15 percent of the stock in a corporation seeking a real-estate loan and all such persons do not own more than 25 percent of the total stock in such corporation.

Another regulation prohibits a Federal association from purchasing an office building or any part thereof, or land upon which to erect such a building, from an affiliated institution, officer, director, or employee of such association, or from a corporation or association in which an officer, director, or employee of the association is a stockholder, officer, director, or employee, or from a partnership in which any officer, director, or employee is a partner, without the prior approval of the Federal Home Loan Bank Board.

Senator BRICKER. I think those self-dealing provisions are maybe very desirable, and yet for the life of me I cannot see the reason for the stringency of rules for employment either in this field or in the banking field of former examiners or employees of the Government.

I would like somebody to tell me how general the practice has been or what you fear it would be.

I look upon most people as honest, and I think the building and loan industry is one of the most honest of all the financial institutions of the country. I have always felt that. It is organized for the benefit of the community. It handles the money of people whom most of us know in the institutions and loans it to people in the community whom most of the members of the various boards and the officers know.

Is it a prevalent thing? That you think that the employees of your board or of the Bank Board would favor an institution to get a job out of it and that there would be collusion among them to that end?

Mr. ROBERTSON. We made no such proposal.

Senator BRICKER. That runs through this whole situation. The advisory committee recommended it. I wonder what was back of it. I would like to have it cleared up in my own mind.

There have been 1 or 2 glaring examples, of course, in the past. We all know that.

Mr. HALLAHAN. Well, as the chairman said, we did not propose that amendment, Senator, and in our testimony we have asked that it be modified. We have had in our own experience no breaches that would warrant a severe restriction in that field.

With respect to other operations, we are not in a position to comment, but we have not experienced it.

Senator BRICKER. I think dealing with the institution's own officials is a very sound prohibition, but that is for the looks of it more than anything else. Those instances of collusion seem rather rare to me in the savings and loan field.

Mr. HALLAHAN. Yes.

Senator BRICKER. I just wondered if the Board has any record of any flagrant——

Mr. HALLAHAN. No; we have, on the other hand, requested that, if your committee is going to consider this, it be modified to be made more reasonable in its operations.

Senator ROBERTSON. The Chair wishes to say that those who investigated in Chicago with respect to two banks out there question the propriety of the quick and well-paid employment of some members of another agency that examined and did not find, presumably, what had been going on.

Senator DOUGLAS. That is right.

Senator ROBERTSON. They suggested to us, without accusing anybody of being crooked, that we put in here what amounted to "lead us not into temptation but deliver us from evil."

The other agencies say we have gone too far. We agree that we did in the criminal section. They do say it is not bad to put a 2-year limitation on employment and do it by regulation.

How would that appeal to the members of your Board?

Mr. ROBERTSON. We would concur.

Mr. Dixon would like to comment.

Mr. DIXON. I think that the answer that was just given was all that I had to offer.

Senator BRICKER. Well, then, this whole emphasis came from the Illinois bank situation, which was one institution and one default?

Senator DOUGLAS. Two institutions.

Senator BRICKER. But they were associated together? They were interrelated?

Senator DOUGLAS. Associated by Hodge, but two separate banks.

Senator ROBERTSON. That is correct as far as this part of the bill is concerned.

Senator BRICKER. That is what I am wondering. I think we ought to think pretty seriously whether to put a broad prohibition across the board because of the default in those institutions. Bad cases make bad law.

Senator BUSH. Have any of the commercial witnesses endorsed that?

Senator BRICKER. They have all said it is too stringent in drafting, as I remember.

Senator ROBERTSON. Repeatedly the chairman during the course of these hearings admitted that the witnesses were right, that we had put in a more drastic provision than appeared to be necessary, and the chairman said that when the committee marked up the bill he would recommend that it be modified.

The witnesses have said: "Just leave it to provision by regulation. We can prohibit them within 2 years if we think there is any too close connection between a big offer and their examination."

Senator DOUGLAS. Mr. Chairman?

Senator BRICKER. I remember within a few years when they came came to the Congress and asked us to pass a law to permit a Governor of the Federal Reserve Board to become president of a bank, and we passed it, and he did not get the job.

Senator ROBERTSON. Off the record.

(Remarks off the record.)

Senator ROBERTSON. The Senator from Illinois.

Senator DOUGLAS. I think the record ought to be a little bit more complete on this matter than it is up to date.

I do not know whether it emerged in the hearings in Chicago or not, but I think Mr. Rogers will bear me out when I say it developed that the chief examiner in Chicago of the FDIC was, in effect, running an employment agency and was getting his employees placed in banks which were being examined by the FDIC.

So that these cases which developed were merely the most notable part of the iceberg sticking above the surface of the sea, and down underneath there was much more than came to the surface.

Would Mr. Rogers correct me on that if I am wrong?

Mr. ROGERS. I think what we found was that when any large number of banks wanted new employees they would go to the Chicago office of the FDIC and ask if anyone was available that they knew of.

Senator DOUGLAS. Yes. Well, that, I think, bears out what I have said—that there was, in effect, an employment office.

May I say this: That I do not believe the people of Illinois are on the whole worse than the people of other States, and I think that if this showed up in Illinois it is quite possible that it exists in other States. Therefore, I think that the evil which was revealed is an evil against which we should move.

May I say that I personally think that while this prohibition against any future employment is too severe and I would like to see a 2-year period, I would like to see that done by statute rather than by regulation, but with the provision that if the administrative agency after due study thinks there is sufficient reason for a modification that it be permitted.

Very frankly—and this does not refer to the present group because I have been much impressed by the public spirit of their testimony—I think there are certain public agencies in which I would not have confidence that they would impose adequate restriction by regulation.

Senator BRICKER. Has the Senator any reason for assuming that these things are going on in other States just because it happened in Illinois?

Senator DOUGLAS. Well, as I say, I do not think the people of Illinois are any worse than the people of Ohio, Mr. Bricker.

Senator BRICKER. I think that that is a non sequitur. I think it is subject to argument. But then I——

Senator DOUGLAS. I do not think politics in Illinois is any worse than the condition of politics——

Senator BRICKER. After all, that was one incident and it could have happened in any State. I do not think it colors the whole banking situation in the country.

Senator DOUGLAS. I think what was revealed was a continuum of a long-established practice of bankers trying to influence political parties and political candidates, both political parties and both candidates on both tickets, by campaign contributions, and that in the case of the FDIC what we had was a very loose and noncritical relationship between this Federal agency and the banks which it presumably was inspecting.

You can say that is isolated, but to my mind it is a danger signal against which we should try to guard ourselves.

Senator MONRONEY. Is it not also a fact——

Senator DOUGLAS. If you want to, I will move we start an investigation of practices in Ohio.

Senator BRICKER. It is perfectly clean there I assure you. It will be a vain effort.

Senator MONRONEY. Is it not a fact we need some kind of statutory provision which would prohibit but allow the waiver as Senator Douglas has suggested, for one thing to prevent any tyrannical control of an examiner over a local bank who might be wanting to punish that bank or the financial institution to break down their resistance for the employment of some pal of his in that agency? There is the threat in that.

Senator BRICKER. I think there ought to be protection, but I am not one who approaches it from the standpoint of everybody examining in the banking system of the country being a crook or trying to force something on an institution.

Senator MONRONEY. Everybody is not going to commit murder, but I say we have to have laws against murder.

Senator BRICKER. I say I am for protection if there is any need for it, but I hate to approach this with an overall, across-the-board prohibition if we can do it otherwise. Maybe we cannot. I do not know.

Senator ROBERTSON. You may proceed.

Mr. DIXON. Might I make just this observation in connection with the discussion: We are faced—and I think probably any governmental agency is faced—with a very practical problem, and that is obtaining, recruiting examiners. And I think the suggestion of the Senator from Illinois, that a waiver be permitted after thorough study and examination, would solve the problem.

I think a flat prohibition would be very harmful to our operation as far as the savings and loan business is concerned. But I think with a provision that a waiver could be made after investigation that would satisfy me at least.

Mr. ROBERTSON. The basic concept of these regulations is to prohibit any traffic or business between persons in such fiduciary capacities and the associations which they serve. The transactions permitted by subsections (a) and (b) of section 7 would be inconsistent with these standards under which Federal associations have operated for many years, and would, in our opinion, not be in the best public interest.

Subsection (c), at page 213, would provide that no Federal savings and loan association shall pay a greater rate of return on the shares, deposits, or other accounts of any director, officer, attorney, or employee than that paid to other holders of similar accounts. This section is not needed, as the standard forms of charter for such associations all contain provisions under which a discrimination of this nature would be a violation of the charter itself. The Board therefore suggests that this provision be eliminated.

With respect to the sections of title 18 of the United States Code which are referred to in this subsection the Board notes that section 219 has no logical application to institutions insured by the Federal Savings and Loan Insurance Corporation and should be eliminated from this subsection.

The remainder of that paragraph is technical. The Board also notes that the reference to section 1005 should be changed to a reference to section 1006. Furthermore, sections 655, 1906, and 1909 do not in their existing wording apply to such insured institutions, but the Board recommends that they be extended to apply thereto. Amendment No. 6 in addendum A would accomplish such extension.

The remaining subsection of section 7, which is subsection (e) at page 213, is not needed in view of existing provisions of the Board's regulations which prohibit the making to any director, officer, or employee of any real-estate loan except on the security of a first lien on the home or combination home and business property owned and occupied by him, or any unsecured loan except for the alteration, repair, or improvement of such home or combination home and business property. The Board recommends that subsection (e) be therefore deleted. It is noted that subsection (e) would not permit the association to make a loan to an executive officer on the security of his shares in the association. The Board's regulations permit such share loans, and we see no reason why they should not be permitted.

Senator ROBERTSON. The Senator from Illinois.

Senator DOUGLAS. Would I be delaying matters if I asked the witness a question?

Senator ROBERTSON. No. no, because if we cannot finish up by 12 o'clock there are some matters in here he can just put in the record.

Senator DOUGLAS. Mr. Robertson, I would like to raise this question: If the first part of your paragraph, the matters referred to there. are already covered by regulation, what is the harm of covering them by statute? Why do we have the objection on the part of the administrative agencies against crystallizing in statute those provisions which have been found wise as a discretionary act of regulation?

As I say, I am greatly impressed with the public spirit of this Board, and I think the recommendations which they have made are in general in the public interest. But another Board may come along with lower standards and these regulations which you think wise may be repealed.

Should we not protect the future?

Mr. ROBERTSON. I can think of no reason, unless it might be a technical one, why if it is good by regulation it should not be——

Senator DOUGLAS. Then if these are wise, why not put them in statute form?

Mr. HALLAHAN. Actually, if I may answer that, Senator, our present regulations are broader in this respect and a little different than the one proposed in the committee print. I think the provision in the committee print would apply to the executive officer of the Association only and would put a $15,000 limit——

Senator DOUGLAS. No; I was speaking of the—go ahead.

Mr. HALLAHAN. Oh, with respect to——

Senator DOUGLAS. Directors, officers, or employees. The first sentence. It is not I think quite identical with the point which you make in the third sentence.

Mr. HALLAHAN. The paragraph starting "the remaining subsection of section 7"?

Senator DOUGLAS. That is right.

Mr. HALLAHAN. Currently the Board's regulations prohibit the making of a loan other than a share loan to a director, officer, or employee for any other purpose than a mortgage loan on the property in which he personally resides. I think——

Senator DOUGLAS. This merely refers to the executive?

Mr. HALLAHAN. Yes.

Senator DOUGLAS. So you want a broader prohibition?

Mr. HALLAHAN. Our present regulation is on a broader basis.

Senator DOUGLAS. And you are afraid if this goes into the final act that you will not have the power by administrative order to make this broader prohibition?

Mr. HALLAHAN. Partly that, except we see no—as I say, our regulation is broader, and it has been in effect I believe since the beginning of the Federal System, and we have experienced no difficulty with the section.

The only question in the proposal in the committee print is this: I believe there is a $15,000 limit on the home-mortgage loan for the executive officer. I do not know in all cases, considering current market conditions, whether such a limitation on one particular gentleman is a fair one in view of the fact that his board of directors has to approve——

Senator DOUGLAS. Is your criticism of this proposed draft that it is too restrictive or that it is not restrictive enough?

Mr. HALLAHAN. I think basically that we have had no trouble in that respect because of the regulations which have been in effect by the Board.

Senator DOUGLAS. Which are more restrictive?

Mr. HALLAHAN. Cover more people; yes, sir.

Senator DOUGLAS. So far as number of personnel is concerned?

Mr. HALLAHAN. Yes, sir. And it is limited to home mortgage loans. And, as I say, we have had no difficulty in that respect.

Mr. ROGERS. Senator, may I ask a question?

Senator DOUGLAS. Certainly.

Mr. ROGERS. I think that the reason this was put in is the fact that executive officers of banks are limited to $5,000 in their borrowing from their own institutions——

Senator BUSH. Executive officers what?

Mr. ROGERS. Are limited to——

Senator BUSH. Of what?

Mr. ROGERS. Of banks.

Senator BUSH. Of any——

Mr. ROGERS. Member bank.

Senator BUSH. Is that so?

Mr. ROGERS. The fact is we liberalized that by raising it from $2,500 to $5,000 in this bill. It was thought that there ought to be a comparable provision for comparable people in the savings and loan, and it was thought that $15,000 was much more liberal than the banks provided.

Mr. HALLAHAN. But there is this distinction I think which Mr. Rogers would recognize I am sure. A bank could make a loan to its executive officer for any purpose for which it could make loans.

Mr. ROGERS. Right.

Mr. HALLAHAN. Ours, as I say, have historically been limited just to home-mortgage loans.

Senator MONRONEY. For his own use?

Mr. HALLAHAN. The property in which he personally resides. So our institution's loaning authority is not the same as a bank's.

Mr. ROGERS. Oh, of course.

Senator DOUGLAS. The Senator from Connecticut.

Senator BUSH. Mr. Chairman, I was just going to ask Mr. Rogers: Is that a Federal Reserve Board regulation?

Mr. ROGERS. No; that is in the present law.

Senator BUSH. That is in the present law?

Mr. ROGERS. Yes.

Senator BUSH. That no member bank may lend more than $5,000 to any officer of it?

Mr. ROGERS. That is right.

Senator BUSH. I mean that shows that there is definitely a reservation in people's minds about the propriety of an officer borrowing from a bank which he serves. I feel myself that it is a very good reservation. I do not see why it is asking too much to ask an officer of a bank to go to another bank or an officer of a loan association to go to another association or to a bank to borrow money. I think it leaves his institution in a very strong position.

I would like to know what this section that they want to delete actually provides.

Mr. ROGERS. That is on page 213 of the bill. What it provides, Senator, is that an executive officer of a Federal savings and loan association could not borrow more than $15,000 from his own association. We thought that we were being liberal, in view of the fact that these would be home-mortgage loans, to increase it to $15,000.

Senator BUSH. When we mark this bill up, Mr. Chairman, I think we ought to consider whether we ought to permit it at all or not.

Senator BRICKER. I would go along with that. I do not think a man ought to be dealing with himself in any financial institution that involves fiduciary funds.

There might be some communities where there is only one building and loan where a man would be pretty much up against it if he wanted to buy a home. But, generally speaking, in cities I think that there would be no harm done and much protection given if a man were not permitted to deal with his own institution at all.

Let me ask you a further question about any unsecured loans by savings and loan associations.

Mr. HALLAHAN. That would likewise have to be on the property in which he resides, Senator.

Senator BRICKER. Are there any of those unsecured loans now given?

Mr. HALLAHAN. Just property improvement loans. Most of them are limited I believe to $3,500.

Senator BRICKER. Are those not generally secured by a mortgage?

Mr. HALLAHAN. No; the large ones, the ones which involve any sizable amount of money, would be secured by a mortgage loan, but generally up to $1,500 or $2,500 or $3,500 they can be on an unsecured basis similar to the FHA title I program.

Senator BUSH. Mr. Chairman, I again would have a considerable reservation about the propriety of an institution making that kind of a loan—an unsecured loan to an officer. I would question any loan, but an unsecured load to an officer for any purpose seems to me to be a very questionable proposition.

Mr. Chairman, I would like to ask counsel to be sure we focus on this when we come to mark up the bill, because this is a pretty important matter.

Mr. ROGERS. I wonder if we might have the regulation from the Board on hand so we will have it available.

Mr. ROBERTSON. We will see that you get it.

Mr. DIXON. Senator, I would like to ask you whether you think there should be any objection to making a loan to an executive officer on the security of his shares in the association.

Senator BUSH. That sounds like a pretty good loan as far as the quality of the loan is concerned, but it does not escape the point that I think is important here. Senator Bricker pointed it out. He says it is doing business with yourself. I think an officer of a savings and loan association, a savings bank, a commercial bank, or a trust company, ought to go some place else to do that kind of business just as a matter of excess caution, of propriety.

Senator BRICKER. It is hardly what we call in law an arm's-length deal.

Senator BUSH. That is right. I think the institution is in a much stronger position with the public if it is understood that the officers cannot borrow from it on any terms. If the shares are good, he will have no trouble getting a loan across the street at any bank.

Senator BRICKER. What loans are made on the security of shares in the association? I do not know of any such an operation myself.

Mr. ROBERTSON. Well, he simply deposits his—if he has $1,000 in his account, he would pledge his account and borrow $800 or $900 on it. Usually the reason for that is not to disturb the accrual of dividend over part of the dividend period.

Senator MONRONEY. Would not one of the reasons also be that disposing of the shares would be setting a bad precedent? Assuming a man had $100,000 in shares in the building and loan and he wanted to build himself a $50,000 house, rather than sell $50,000 worth of the stock, which he could readily do, he would hypothecate that amount of his shares, which is almost like an attachment to current bank account, for a $50,000 loan?

Mr. HALLAHAN. No, no; ordinarily he would sell it, Senator, because the return on his shares would be generally less than the interest that he would have to pay on his mortgage.

Generally, the association's share loans are not a large activity. Ordinarily, if you needed a little money, say, the month before the dividends were paid, it would be to the investor's benefit to take a small share loan on his account rather than withdraw it all and lose his entire dividend. And, generally, most share loans are the month preceding the dividend-payment period.

Senator BUSH. Mr. Chairman, I would like to make this one point.

Senator DOUGLAS. Certainly.

Senator BUSH. If an officer of such a bank or association is borrowing on his own account, even though well secured, up to $15,000, which I think this bill suggests is all right, his judgment on whether the bank should raise interest rates or lower interest rates or increase margins, whatever, is certainly not as objective as it would be if he were not borrowing from that bank.

I think that when he has that kind of a fiduciary responsibility to all these other depositors that he ought to go some place else and borrow his money.

Senator DOUGLAS. I personally find myself in agreement with the Senator from Connecticut, and, as a matter of fact, the same scruples which he has about dealings by executive officers I have also about dealings by directors, which I think you covered in your discussion of section 7 (a) on pages 212 and 213.

I would like to ask you your opinion on that, Mr. Robertson or Mr. Dixon.

Senator BUSH. Mr. Chairman, would you say that again? I did not hear.

Senator DOUGLAS. Yes. You have addressed yourself to the fact that you did not think that the executive officers of Federal savings and loan institutions should deal with themselves since their interests would be divided. I said that the same scruples which you had about these dealings by executive officers with themselves I also had in some measure about the question of the directors of a Federal savings and loan institution.

Senator BUSH. Oh, yes.

Mr. HALLAHAN. As I said, Senator, I think our regulations have been quite scrupulous in this area.

Senator DOUGLAS. Do you think they would be loosened by the provision in section 7 (a)?

Mr. HALLAHAN. Yes. Yes, sir.

Senator BUSH. Mr. Chairman, I certainly agree with you it should apply equally.

Senator DOUGLAS. I wonder if these gentlemen would care to make a statement for the record somewhat stronger, if they feel it, than that which they have made relative to section 7 (a). I do not want to have you say things you do not believe, and I am sure you would not do it anyway, but——

Mr. HALLAHAN. We are recommending that sections 7 (a) and (b) be deleted.

Senator DOUGLAS. On the ground that you have more stringent regulations?

Mr. HALLAHAN. Yes, sir.

Mr. DIXON. Much more.

Senator DOUGLAS. And that the passage of this provision would distinctly weaken the regulations which you now have?

Mr. HALLAHAN. Yes, sir.

Senator DOUGLAS. Could we see your regulations on this point? Would you have any objection?

Mr. HALLAHAN. Yes, sir; you may.

Senator DOUGLAS. Would you have any objection if the regulations were made statute?

Mr. HALLAHAN. No, sir.

Mr. ROBERTSON. No, sir.

Mr. DIXON. We would be glad to have them made statutory.

Senator DOUGLAS. Thank you. Would you continue?

Mr. ROBERTSON. Title VI of the committee print would amend title IV of the National Housing Act and would provide that said title IV may be cited as the Federal Savings and Loan Insurance Corporation Act.

Senator DOUGLAS. Mr. Robertson, may I ask if this discussion and a good deal that follows is technical in nature? Does it deal with matters of principle or policy?

Mr. ROBERTSON. There is one policy matter on holding companies. We marked the next paragraph as being technical, and practically all of page 16 is also technical.

Senator DOUGLAS. Counsel I know will study these suggestions scrupulously.

Mr. ROBERTSON. And practically all of page 17.

Senator DOUGLAS. At the bottom of page 17 you have certain policy suggestions. Would you read those?

(The balance of the technical amendments referred to follow:)

The last sentence of subdivision (b) of section 402, at page 215 of the committee print, is based on recommendation 166B of the advisory committee, at page 43 of its report. The stated purpose is to make certain that married savers in certain community-property States are provided insurance coverage on an equal basis with savers in other States. We believe that the language in amendment Nod. 7 in addendum A would more closely accomplish this purpose, and we recommend that said amendment be adopted.

In addition, there appears to be need for including in section 402 a definition of the term "State" as including Puerto Rico. This could be accomplished by adding to section 402 the following new subsection:

"(f) The term "State" includes Puerto Rico."

The Board also suggests several changes in the language of section 403 of the committee print.

In the first line of subdivision (5) of subsection (c), at page 216, the language "by its Board of Trustees," and the commas preceding and following that language, should be deleted, as there is no longer a board of trustees of the Federal Savings and Loan Insurance Corporation. Further, the language "Board of Trustees" in the first sentence of subsection (d), at page 217, should be changed to "Board."

The second sentence of subsection (d), likewise at page 217, provides that moneys of the Insurance Corporation not needed for current operations shall be deposited in the Treasury of the United States, or, upon the approval of the Secretary of the Treasury, in any Federal Reserve bank, or shall be invested as therein provided. While this sentence is in the exact language of the existing statute, that language has been affected by section 302 of the Government Corporation Control Act, which provides that the banking or checking accounts of all wholly owned or mixed-ownership Government corporations shall be kept "with the Treasurer of the United States" or, with the approval of the Secretary of the Treasury, with a Federal Reserve bank, or with a bank designated as depositary or fiscal agent of the United States. Section 302 further provides that the Secretary of the Treasury may waive the provisions of that section and that the section will not apply to the establishment and maintenance in any bank for a temporary period of banking and checking accounts not in excess of $50,000 in any one bank.

To guard against any contention that reenactment of the existing language might require that funds of the Insurance Corporation be covered into and out of the Treasury or might require that such funds be treated as subject to the requirement of appropriation, the Board recommends that the second sentence of subsection (d), at page 217, of the committee print, be amended to read as follows: "Moneys of the Corporation may be deposited in any depositary authorized or permitted by or under section 302 of the Government Corporation Control Act or may be invested in obligations of, or guaranteed as to principal and interest by, the United States."

The last sentence of subsection (d) of section 403 contains a provision that, when designated for that purpose by the Secretary of the Treasury, the Corporation shall be a depositary of public money. In order to make clear that this provision will not be affected by the reenactment of provisions of section 15 of the Federal Reserve Act as proposed in title II of the committee print, the Board recommends that the following sentence be added at page 217, line 29, of the committee print: "The provisions of the sentence next preceding shall not be affected by section 15 of the Federal Reserve Act or any other provision of law."

With respect to subsection (e), at page 217, the same questions as to the continued applicability of the Public Debt Act of 1941, as amended, might arise as in the case of section 13 of the Federal Home Loan Bank Act, and the Board recommends that there be added to subsection (e) the following new sentence: "Nothing in this subsection shall affect the applicability of the Public Debt Act of 1941, as amended."

In the third sentence of subsection (h), which sentence appears at page 219 of the committee print, the language beginning "and the Corporation shall also pay to the Secretary of the Treasury," and the comma preceding said language, should be deleted, as the payment referred to in said language has long since been made and the language is obsolete.

Two amendments should also be made to subsection (i), at page 219. First, the language "Home Loan Bank Board" beginning in the fourth line of the subsection should be changed to "Board." Second, the last proviso to the first sentence, and the colon preceding said proviso, should be deleted. This proviso, which relates to a method of insurance settlement that was repealed in 1950, is now obsolete.

Finally, in the second line of subsection (j), at page 219, the word "member" should be changed to read "Federal Home Loan Bank member."

Mr. ROBERTSON. The next section, which is section 404, does not include two of the recommendations which the Board made in item 158 of the compilation of October 12.

By the first of these two recommendations, the Board proposed that there be added to this section a provision that the Federal Savings and Loan Insurance Corporation have power to regulate retirement, pension, and deferred-compensation contracts and arrangements of insured institutions. We are still of the opinion that legislation along the lines suggested is desirable to protect the interests of the Federal Savings and Loan Insurance Corporation. We appreciate and are mindful of the fact that to attract and retain qualified personnel insured institutions may, and should, offer their employees retirement, pension, and deferred-compensation benefits. The Board is concerned, however, that some institutions may go so far as to jeopardize now, or in the future, the assets of such institutions to the point where the exposure of the Insurance Corporation would be the cause of serious concern. Therefore, we believe that legislation which would authorize the Insurance Corporation to have some regulatory control over such pension and related plans would be in the Government's best interests.

The second of these recommendations proposed that the Insurance Corporation be given power, by regulation, to define and limit the losses which may be charged to the reserves which insured institutions are required to provide. As pointed out in the Board's original recommendation in item 158, it is obvious that the making of allocations toward the building up of reserves may be defeated in a very simple manner if the reserves themselves are concurrently subject to improper or unwarranted charges. Accordingly, the Board recommends that the following new sentence, carrying out its original recommendation, be added at page 221, line 9, of the committee print:

The Corporation shall have power, by regulation, to define and limit the losses which may be charged to such reserves.

Section 406, at page 223, contains in subsection (b) a provision that where the Federal Savings and Loan Insurance Corporation makes settlement of its insurance obligation by making available a transferred insured account such account shall be an account "payable on demand." The Federal Home Loan Bank Board appreciates that this provision has been included because of a similar change in the language of the settlement provisions of the Federal Deposit Insurance Corporation.

Senator DOUGLAS. Mr. Robertson, may I ask this question: Are the Directors of the Federal Savings and Loan Insurance Corporation members of the Federal Home Loan Bank Board?

Mr. ROBERTSON. Yes, sir.

Senator DOUGLAS. So you wear two hats?

Mr. ROBERTSON. Yes, sir.

The Board believes, however, that our insured members should not be deprived, in all cases, of the opportunity of receiving, in settlement of their insurance, an account which earns income, and to that end the Board suggests the following amendment: At page 223, line 14, after the language "payable on demand", insert the language "or a savings account."

Senator BRICKER. To keep it in the same status as the original?

Mr. ROBERTSON. Yes, sir.

Senator BRICKER. In your second paragraph on page 18 where you mention improper charges against reserves, what would be the nature of those improper charges? How would they be made?

Mr. ROBERTSON. There are certain charges that should be made against current earnings, and what we would undertake to prevent would be an inflation of earnings at the expense of the reserves.

Senator BRICKER. What would be the nature of some of those charges? Give me an illustration.

Mr. HALLAHAN. Senator, we do not want this to be misunderstood, because it is not either widespread, nor I do not know that it is occurring at all. But we did not want institutions to sell loans from their portfolios at a loss and reinvest the proceeds currently in other mortgage loans and charge the loss on the sale against reserves, and take the income, for instance, if they were construction loans, of fees attendant to the construction loans into income currently in order to pay a dividend which maybe we think they should not pay.

Senator BRICKER. Would this same principle be applicable to the sale of bonds?

Mr. HALLAHAN. No, sir.

Senator BRICKER. They would be properly charged against the reserves?

Mr. HALLAHAN. Yes, sir. That is right.

Senator BRICKER. About the only place, then, it would be possible to mischarge, you might say, would be in the case of construction loans?

Mr. HALLAHAN. Yes, sir. We wanted to charge those losses against the income during that period, rather than against reserves.

Senator BRICKER. We wanted the Board to have the power to require that.

Mr. HALLAHAN. Yes, sir.

Senator BUSH. I think that is good.

Mr. ROBERTSON. At the top of page 19. In subsection (b) of section 407, at page 224, the Board's recommendation in item 162 of the compilation of October 12 to strike the language "and all valid credit obligations of such association" has not been adopted.

Senator BRICKER. Strike the language?

Mr. ROBERTSON. Strike that, yes. The advisory committee, at page 42 of its report, disapproved the recommendation on the ground that this provision should be retained in the law "in order to insure that creditor obligations shall have priority over shareholder obligations." The Board is convinced that the deletion of this provision could in no way affect the priority of creditor obligations, and urges that it be deleted on the grounds set forth in the Board's original recommendation.

Mr. ROGERS. Mr. Robertson, I wonder if you would clarify exactly what is meant by that phrase "all valid credit obligations"?

Mr. ROBERTSON. Mr. Hallahan, would you explain that?

Mr. HALLAHAN. Yes. An institution, of course, can have valid credit obligations. For instance, if it has a mortgage loan on the building which it occupies, if it occupies its premises under a leasehold, or it might have advertising contracts, or other contracts of that kind which are common to anyone doing business.

We merely maintain that those obligations, credit obligations of that nature, should be recovered from the general assets of the association. And they are a first claim on the total assets of the association. We believe that there is no basic reason why the insurance corporation should have to pay those obligations.

Mr. ROGERS. The crux of the matter is that you pay the insurance and then pay off all valid credit obligations. They should be taken out of the assets of the institutions?

Mr. HALLAHAN. Yes.

Mr. ROGERS. All right. Thank you.

Mr. HALLAHAN. Because there is no question of the priority of the credit obligation against the assets of the institution.

Senator BRICKER. There is no insurance on any liability of that kind at all, is there?

Mr. HALLAHAN. Under existing law, that provision is in there. We recommend that it be taken out, Senator.

Senator BRICKER. You mean at the present time if a savings and loan institution has a loan obligation on a mortgage on its building, that the Insurance Corporation insures that up to $10,000?

Mr. ROGERS. They have to pay it.

Senator BRICKER. They do?

Mr. ROBERTSON. Yes.

Senator BRICKER. That is clear beyond the intention of the insurance law.

Mr. HALLAHAN. Dr. Husband.

Dr. HUSBAND. The creditor obligations, Senator, are not insured, but if the institution gets in trouble, since the creditor obligations has a priority claim out of the shares, in order to get our money out of the shares we have to pay off the creditor obligations.

Senator BRICKER. I see. It is not very sound.

Mr. ROBERTSON. Section 408, at page 225, relates to the termination of the insured status of institutions insured by the Federal Savings and Loan Insurance Corporation. In item 163 of the committee compilation of October 12, the Board recommended a revision of the language of the section so as to provide a more speedy method of judicial review, substitute review on the question of substantial evidence (as provided in the Administraive Procedure Act) for the existing provision for review on the weight of the evidence, and authorize the Insurance Corporation to define the unsafe or unsound practices which are ground for termination of insurance. The Board again urges that this proposed revision be adopted as set forth in item 163.

The next paragraph is a technical one.

(The paragraph referred to follows:)

The Board also urges that the original numbering of the termination section as section 407 be retained, for the reason that expense-authorization language for the fiscal year 1958 which has already been transmitted by the Bureau of the Budget to the House Committee on Appropriations refers to the section by that number. This could easily be accomplished by renumbering section 407 of the committee print as section 408 and renumbering section 408 as section 407.

Mr. ROBERTSON. The next one; section 409 deals with savings and loan holding companies. The Board favors the enactment of legislation on this subject.

Subsection (b) of the section would provide that no application shall be approved for insurance by the Federal Saving and Loan Insurance Corporation of the accounts of any institution which is directly or indirectly controlled, or more than 10 percent of the stock of which is directly or indirectly held, with power to veto, by any company which also directly or indirectly controls, or directly or indirectly holds with power to vote more than 10 percent of the stock of, any insured institution or any other applicant for such insurance.

Senator BRICKER. Is that a prevalent practice in the field?

Mr. HALLAHAN. No; it is fairly new, Senator.

Senator BRICKER. It is gaining, you mean?

Mr. HALLAHAN. It is in its infancy.

Senator MONRONEY. There is one corporation now?

Mr. HALLAHAN. Two.

Senator BRICKER. Again, I know of no such practice in my State.

Mr. HALLAHAN. No. California and Utah—there is one in Utah.

Mr. ROGERS. That is a bank holding company.

Mr. HALLAHAN. It happens to be a bank holding company.

Mr. ROGERS. Also.

Mr. HALLAHAN. Yes.

Senator BRICKER. That is the one that has the power of advertising the interest rate?

Mr. HALLAHAN. Yes.

Mr. ROBERTSON. This subsection would also provide for the termination of insurance of any institution which should become insured under these circumstances.

Subsection (c) of section 409 would make it unlawful for any company, directly or indirectly, to acquire the control of, or acquire with power to vote more than 10 percent of the stock of, more than one insured institution, or to acquire the control of, or acquire with power to vote more than 10 percent of the stock of, any insured institution when it directly or indirectly holds the control of, or holds with power to vote more than 10 percent of the stock of, any other insured institution.

Senator BRICKER. That is to keep these institutions more or less the community affairs that they were supposed to be in the beginning?

Mr. ROBERTSON. Yes, sir.

Subsection (c) would permit shares of stock of savings and loan associations to be acquired by a lender pursuant to a pledge or hypothecation to secure a loan, or in liquidation of a loan, but would require divestment by the lender of such stock within a period of 1 year in any case where such acquisition would otherwise have been unlawful under the section.

Subsection (d) provides the procedure by which the Board may proceed to enforce divestment of ownership or control by any company which is in violation of the provisions of the section.

Subsection (e) provides a criminal penalty of $10,000 for any company which willfully violates any of the provisions of section 409.

Subsection (f) defines the term "stock" and authorizes the Board to define by regulation the terms "directly or indirectly," "stock of a similar nature," and other terms used in section 409, to the extent that it deems necessary to prevent evasion of the purposes or provisions of the section.

With respect to the provisions of section 409, the Board recommends that the committee give serious consideration to amendments which would (1) require the approval of the Board for control of one savings and loan association and (2) prohibit upstream loans to the holding company or any subsidiary owned or controlled by the holding company.

With regard to the first suggested amendment, the Board has had recent experience with a holding company which owns several banks and also two savings and loan associations. One of the savings and loan associations is insured by the Federal Savings and Loan Insurance Corporation and the other association is uninsured. This holding company advertised jointly its banking and savings and loan facilities in the newspapers, as well as its several bank offices, and accepted savings for at least one of its savings and loan associations in the lobby of one of its banking facilities.

Senator BRICKER. That is Utah?

Mr. ROBERTSON. Yes, sir.

Such intermingling of advertising in banking and savings and loan facilities is not only confusing to the public, but, in effect, permits the use of the banks as branches of savings and loan associations. Requiring the approval of the Board for a holding company to own or control or acquire a substantial interest in one savings and loan association would enable the Board to make sure that occurrences of this kind did not happen in the future.

In this connection, it might be advisable to amend section 409 to prohibit any holding company from acquiring or holding any interest in an insured savings and loan association if it already owns or subsequently acquires control or a substantial interest in an uninsured savings and loan association.

The second suggested amendment of the Board would prevent self-dealing by prohibiting upstream loans to the holding company or loans to any subsidiary owned or controlled by the holding company.

Senator BRICKER. You go on the theory, then, that it is well to hold these to local institutions, if you can do so?

Mr. ROBERTSON. Yes, sir.

Senator BRICKER. And this is a part of that program?

Mr. ROBERTSON. Yes, sir.

Senator BRICKER. I think it is very commendable.

Mr. ROBERTSON. The Board is of the opinion that one of the fundamental rules of sound lending is that the parties concerned deal at arm's length. The amendments suggested by the Board would preserve this sound and tested lending requirement with respect to institutions whose loanable funds are derived nearly 100 percent from the general public.

Mr. ROGERS. Mr. Chairman, may I speak?

Senator SPARKMAN. Mr. Rogers.

Mr. ROGERS. Have you any idea how many situations there are when a corporation owns just one? Before this we were talking about more than one.

Mr. ROBERTSON. I am aware of only two situations which we have had under consideration. There may be some others.

Mr. HALLAHAN. No; I don't know how it stands with one. I think those are basically family and local holdings anyway. But those have not given us any concern.

Mr. ROGERS. I understood there were any number set up for tax purposes in that manner.

Mr. HALLAHAN. I think so.

Mr. ROGERS. Thank you.

Mr. Robertson. The remaining comments of the Board relate to section 803 of title VIII, which would amend certain sections of title 18 of the United States Code.

In subsection (a), the Board recommends that the material in subdivisions (ii) and (iii) at page 248 be eliminated. The Board feels that the matter of employment within the savings and loan industry of employees or former employees of the Board or the Federal Savings and Loan Insurance Corporation would be adequately covered by the proposed subsection (b) of section 19 of the Federal Home Loan Bank Act, at page 200 of the committee print, with the amendments which the Board has proposed. It believes that the drastic provisions of section 803 might seriously impair its ability to obtain competent personnel, especially in the examining and supervisory fields. The Board suggests that the matter of loans be dealt with by providing that no examiner or assistant examiner who is indebted to an institution on a loan other than a loan on shares or deposits in the institution shall take part in any examination of such institution. In addition, the Board suggests that, at page 248, line 4, after the language "officer or employee," the language "or any member" be added.

The next two paragraphs are entirely technical.

(The paragraphs referred to are as follows:)

Likewise, and for the same reasons, the Board suggests that in subsection (b), at page 249, the material in subdivisions (ii) and (iii) be deleted. It further suggests that in line 10 on page 249, after the language "the Federal Home Loan Bank Board," there be added a comma and the language "of the Federal Savings and Loan Insurance Corporation."

In subsection (c), we note that at page 250, line 16, the language "bank or corporation" should be deleted and the language "bank, corporation, member, or institution" inserted. Finally, in connection with subsection (h), at page 251, we note that the existing language of subsection (h) of section 2113 of title 18 of the United States Code has a reference to section 401 of the National Housing Act, which would be renumbered as section 402 by the present measure. Amendment No. 8 in addendum A is recommended for the purpose of changing this reference.

Mr. Robertson. The Board also submits herewith, as addendum B, a few purely technical amendments to the committee print.

We are advised by the Bureau of the Budget that, subject to the foregoing, there is no objection to the submission of the testimony which I have just presented.

I should like to thank you, Mr. Chairman, and the other members, for giving us this opportunity to express our views, and to again thank you, the committee and your staff, for having done a splendid job.

If the committee so desires, the Board and its staff will be very happy to give any assistance that may be requested by your committee in its further consideration of this legisaltion.

Thank you very much.

Senator Bricker. There are a few things I would like to clear up just for the purposes of the record and my own mind. How many boards of regional Federal home-loan banks are there?

Mr. Robertson. Eleven.

Senator Bricker. Eleven. And how many directors are there on each board?

Mr. Robertson. They vary in number.

Mr. Hallahan. There are 12 on 10 of them and 15 on 1.

Senator Bricker. Those are in the more populous areas?

Mr. Hallahan. Yes.

Senator BRICKER. That is where; in San Francisco?

Mr. HALLAHAN. Yes, sir.

Senator BRICKER. How are they chosen?

Mr. ROBERTSON. Mr. Hallahan will answer that.

Mr. HALLAHAN. Eight of the members are chosen by the member institutions themselves, and four are appointed by the Board.

Senator BRICKER. Appointed by your Board?

Mr. HALLAHAN. By our Board; yes, sir.

Senator BRICKER. What are the qualifications of those four that are appointed by your Board? The eight, I presume, are all picked from the industry itself?

Mr. HALLAHAN. Yes, sir.

Senator BRICKER. They are nominated by the industry and voted on by the industry and really represent the industry itself?

Mr. HALLAHAN. That is true.

Senator BRICKER. What about the four that are picked by your Board?

Mr. HALLAHAN. The four that are chosen by the Board are what we refer to as "public-interest directors" to represent the public on our regional bank. And the Board selects the chairman and vice chairman of our regional boards of directors.

Seantor BRICKER. You mean your Board?

Mr. HALLAHAN. Our Board; yes, sir.

Senator BRICKER. Selects the chairman and vice chairman of the regional banks?

Mr. HALLAHAN. The chairman is always a member who is appointed by the Board.

Senator BRICKER. Are those four always outside of the industry itself, from other interests than the savings and loan institutions?

Mr. HALLAHAN. Generally, they are. But we do have a few cases, Senator, where those appointive directors are actually operating industry personnel.

Senator BRICKER. Do you not think they ought to be from the public, if it is at all possible to get them?

Mr. HALLAHAN. Yes; I think it would be hard to argue—they are public-interest directors and should represent the public.

Senator BRICKER. The compensation is not high; it really does not pay for their time. It is really a public-service job, is it not?

Mr. HALLAHAN. Yes, sir.

Senator BRICKER. That is what it amounts to?

Mr. HALLAHAN. Yes, sir.

Senator BRICKER. I refer to that because I remember Charles Dever served as the chairman of our regional board.

Mr. HALLAHAN. He still does, and renders distinguished service to our system.

Senator BRICKER. Purely from a public-interest motive, because he had a full-time job as president of a university.

Mr. HALLAHAN. Yes, sir.

Senator Bricker, there is no difference in the interest as I can see that the public members would represent as contrasted to the others, but I do think that it is desirable, if at all possible, to get people from outside of the industry in those four jobs. I think it is better for the industry if we can get them.

Senator BRICKER. It brings a point of view that I think would be very helpful to the industry as a whole.
Senator BUSH. Mr. Chairman?
Senator BRICKER. I would just like to ask one more question. You have 11 boards; that would be 44 public representatives appointed by your Board?
Mr. HALLAHAN. Yes, sir.
Senator BRICKER. How many of them are from the industry?
Mr. HALLAHAN. I think currently there are three.
Senator BRICKER. That is only 3 of the total of 44?
Mr. HALLAHAN. Yes, sir. Is that not correct?
Mr. DIXON. I think that is correct.
Mr. HALLAHAN. Yes.
Senator BRICKER. I just wanted the record to show that. It is kind of hard to keep track of it in the appointment of members, and so on.
Mr. HALLAHAN. Yes, sir.
Senator BRICKER. If it is not a matter explicitly stated, expressly stated in the record.
Mr. HALLAHAN. It would be rather difficult for us to say that all of those members should not be public-interest directors because that, I am sure, is what was intended.
Senator BRICKER. You would not want any provision?
Mr. HALLAHAN. No, sir.
Senator BRICKER. You do get as many public-interest directors as you can?
Mr. HALLAHAN. Yes. As I say, I think it would be hard for us to argue that it should not be 100 percent.
Senator SPARKMAN. Senator Bush.
Senator BUSH. Mr. Chairman, I would like to get a little clearer picture about the relationships between the bank and the associations. Are these associations members of the bank like, say, the members of the Federal Reserve System? Is there a similar relationship?
Mr. ROBERTSON. Yes, sir.
Senator BUSH. They are. What do they do, pay a fee or own stock in the bank?
Mr. ROBERTSON. They own stock.
Senator BUSH. They own stock?
Mr. ROBERTSON. Yes, sir.
Senator BRICKER. Senator, will you yield on that point?
Senator BUSH. Yes.
Senator BRICKER. They are required to own a percentage of stock in relation to their——
Mr. ROBERTSON. Home mortgage loans.
Senator BRICKER. That is right.
Senator BUSH. How does the bank get its funds outside of this procedure that you have just mentioned?
Mr. ROBERTSON. About once a month the Federal home-loan banks sell joint and several obligations to the public.
Senator BUSH. Yes. What is the principal markup for those securities; what are those, debentures? What are they, long-term?
Mr. ROBERTSON. They are, ordinarily, short-term, running from 12 to 18 months.
Senator BUSH. Yes. And they keep issuing these——
Mr. ROBERTSON. Mr. Hallahan corrects me—6 to 8 months.

Senator BUSH. I beg your pardon?
Mr. ROBERTSON. It is 6 to 8 months.
Senator BUSH. Six to eight months?
Mr. ROBERTSON. Yes, sir.
Senator BUSH. And they keep turning these over all the time?
Mr. ROBERTSON. Yes, sir.
Senator BUSH. As they need money?
Mr. HALLAHAN. Yes, sir.

Senator, I believe it would be better to give you a little more of the background; the member institutions themselves currently own over some $600 million of stock in the banks. In addition to that, the banks have an earned surplus of some $50 million. So that the member institutions have contributed somewhere around $660 million or $670 million.

In addition to that, the member banks accept deposits from their member institutions. And currently those deposits amount to approximately $680 million.

So the bank systems have currently from its own members somewhere in the approximate amount of about $1,350 million.

Senator BUSH. Before they sell any note? Without selling any notes at all?
Mr. HALLAHAN. Yes, sir.
Senator BUSH. What is the incentive for a member institution to deposit with the home-loan bank?
Mr. HALLAHAN. It is a liquidity reserve, in a way, Senator.
Senator BUSH. Are they obliged to use that as a bank of deposit, rather——
Mr. HALLAHAN. No, sir. It is purely voluntary.
Senator BUSH. Why do they choose it, for instance, rather than a commercial bank in the same city?
Mr. HALLAHAN. I think on the whole more of their deposits, more of their cash is in commercial banks than it is in our system.
Senator BUSH. I just cannot quite see what is the incentive to deposit with the home-loan bank if you are a member institution.
Mr. HALLAHAN. There are many services which our banks can and do render to their member institutions. This is one of the services.
Senator BUSH. But the relationship of a depositor is purely a voluntary one by the member institution, is that right?
Mr. HALLAHAN. Yes, sir.
Senator BUSH. One of the criticisms that one hears from time to time about this arrangement is that your member institutions have an advantage over the ordinary savings bank, mutual savings bank, because they may borrow from the home-loan bank and thus put themselves in a position to lend more money than the total deposits which they have, or share capital which they have from the public.
Mr. HALLAHAN. Yes.
Senator BUSH. Is it a fact, in your opinion, that this does give the member institutions an advantage over the mutual savings banks?
Mr. HALLAHAN. Well, Senator, mutual savings banks are eligible for membership in our system, and we do have some 26 or 27 of them currently.
Senator BUSH. May I ask you why more do not join then? Do you have any opinion?

Mr. HALLAHAN. No. I assume if they are prohibited by the laws of their State from borrowing money, there would be no reason for them to join our system.

Senator BUSH. That is the case in most States, is it?

Mr. HALLAHAN. I really could not say, Senator, whether it is or not. But one of the purposes of the bank system is to provide liquidity for its member institutions, and that is exactly what it does.

Senator BUSH. I can see that, and I thought that was the original purpose of the bank system.

Mr. HALLAHAN. Yes, sir.

Senator BUSH. It was to provide liquidity when liquidity was needed. But what I am trying to find out is whether there is any justice in the claim that this gives these savings and loan associations an unwarranted advantage over savings banks by having this governmental institution available to lend them money in excess of their deposited capital or share capital so that they can actually lend out more money than they have acquired in their thrift-gathering efforts.

Mr. HALLAHAN. It certainly is an advantage, Senator, and, as I say, mutual savings banks are offered membership in our system.

Senator BUSH. Is this taken advantage of right along by members of the bank?

Mr. HALLAHAN. Oh, yes, sir. The building season normally runs from the good weather of March through September or October. The institutions are receiving savings on a 12-month basis. Their disbursements are predominantly concentrated during the building season.

Senator BUSH. Yes.

Mr. HALLAHAN. The system furnishes a source of seasonal funds for its members to meet their needs.

Senator BUSH. Do you think using the bank's resources by the member institutions is largely seasonal?

Mr. HALLAHAN. It is about, I would say 40 percent. And it also serves as an additional source of long-term funds for institutions in those localities where there is not sufficient capital formation to meet the home financing needs of the community.

Senator BUSH. What determines the amount that a member institution can borow from one of the banks?

Mr. HALLAHAN. The Board currently is setting a maximum—sets a maximum limit.

Senator BUSH. This Board?

Mr. HALLAHAN. This Board; yes, sir.

Senator BUSH. And what is the regulation that is in force now?

Mr. HALLAHAN. For other than meeting withdrawals, 12½ percent of their savings capital.

Senator BUSH. That is the limit of their borrowing ability from the bank?

Mr. HALLAHAN. Yes, sir.

Senator BUSH. Has it been larger than that at any time?

Mr. HALLAHAN. Yes, it has been in the past.

Senator BUSH. How high do you recall that it has been?

Mr. HALLAHAN. It has, I believe, been up to 25 percent, has it not?

Mr. DIXON. Twenty-five percent, I believe, would be as accurate an answer as we could give without——

Senator BUSH. I presume you think it is a sound setup?

Mr. HALLAHAN. Very, very sound, Senator.

Senator BUSH. I thank you.

Senator MONRONEY. Mr. Chairman.

Senator SPARKMAN. May I ask 1 or 2 questions? I have an appointment that I am late for already.

You are going to put in this record, as I understand, the answers to Senator Bush's question. I think perhaps he touched on one, though, that I do not ask you to answer now, but I wish you would put it in.

We had a good many letters from the commercial banks claiming that there is some kind of unfair competition from the savings and loan associations with reference to the savings or the dividends or interest or whatever you want to call it that is paid out. You know what I am talking about?

Mr. HALLAHAN. Yes.

Senator SPARKMAN. If you care to produce it, I will be glad if you will come in one that when you furnish the answer to Senator Bush's question. Because from time to time I know I do have letters from commercial banks.

There are one or two things I want to ask you about, quite hurriedly, because I do have to go. One thing that has been called to my attention recently with some degree of criticism, or perhaps I should say "questioning," is the amount, the high percentage of the funds of our savings and loan associations that are tied up in construction loans rather than in the actual long-term home mortgages.

Would you care to comment very briefly on that?

Mr. ROBERTSON. Could you comment on that, Mr. Dixon?

Senator SPARKMAN. Do you know offhand how it would run?

Mr. DIXON. I would not know, Senator, but——

Senator SPARKMAN. I wonder if you would look that up and give it to us in writing?

Mr. DIXON. Yes, sir. We would like to furnish that.

Senator SPARKMAN. I know nothing about it, but I just heard that there was a very high percentage that went into construction loans.

Senator BRICKER. A great share of those loans are financed in the same institution.

Senator SPARKMAN. Of course, in treating that, I would like to know if it is in connection with housing upon which they subsequently take the mortgages. It seems to be logical and conceivable.

Mr. DIXON. We would like to give you a complete story on that.

Senator SPARKMAN. I would like to have it.

Here is something I do want to ask you about. You will recall about 3 weeks ago, Mr. Chairman, you had a letter from Jack Carter, the staff director from the Housing Committee, with reference to the construction that the Home Loan Bank Board has put on an amendment that we passed last year, permitting the increase from 15 percent to 20 percent of funds that could be invested beyond the $50 million limit.

Mr. ROBERTSON. Yes, sir.

Senator SPARKMAN. Do you recall that?

Mr. ROBERTSON. Yes; I do.

Senator SPARKMAN. It seems to me, in all frankness, that the construction is not in accord with the intent of Congress in writing the amendment. It may be that the wording was bad. I have just been checking the wording, and it may very well be that the wording in the provision was such as to justify your construction.

But I have gone back and even gone over the transcript of the discussion in the subcommittee at the time that it was being agreed upon, and I know that the subcommittee intended—and it originated here, by the way—I know that the subcommittee intended that there would be no difference as between home mortgages and loans on other types of property.

Unfortunately, I think that word "other" was used. But I know it was not our intention. We simply thought we were increasing the amount that could be used just as it had been used previously. I notice Senator Douglas took part in the discussion, Senator Capehart did, I did, and there may have been 1 or 2 others. It is very clear from that discussion that we thought we were simply extending, increasing the amount from 15 to 20 percent, and did not intend to make any limitation on the type of the loan. Although it is my understanding that your regulation, your construction has been——

Senator BRICKER. I think, Senator, that was worked out in conference, was it not, the final wording of it?

Senator SPARKMAN. Was it?

Mr. ROGERS. Yes.

Senator SPARKMAN. It may have been. But anyhow, the word "other" got into it, and I do not think it was intended to be limited.

Mr. ROBERTSON. We shall be glad to review the regulation.

Senator SPARKMAN. I would be very glad. It was called to your attention by letter.

Mr. ROBERTSON. Yes, sir.

Senator SPARKMAN. I asked Jack Carter to write you a few weeks ago.

Mr. ROBERTSON. Yes, sir. I recall the letter.

Senator SPARKMAN. If you would do that, I would appreciate it. I wish I had time to stay further and ask you some more questions, because I think all this discussion has been quite helpful and quite interesting, but, unfortunately, I have an appointment to which I have to go.

Mr. ROBERTSON. Thank you, Mr. Chairman, for hearing us.

Senator BRICKER. Mr. Chairman, may I ask just a couple of questions?

Senator DOUGLAS. Yes, sir.

Senator BRICKER. In relation to the examination of Senator Bush, what is this rate you are paid by your regional banks to the members for deposits?

Mr. HALLAHAN. It varies between 2 and 2½ percent currently, Senator.

Senator BRICKER. And that is determined where?

Mr. HALLAHAN. By the regional board.

Senator BRICKER. By the regional board itself?

Mr. HALLAHAN. Within maximums which we set.

Senator BRICKER. That is a little more than they could get then in the local commercial banks?

Mr. HALLAHAN. Yes, sir.

Senator BRICKER. Is it not one of the reasons for that deposit that it creates a very good relationship between the regional board and the banks so they can go there for loans when the times comes they need money, as everyone of them does at certain periods during the year?

Mr. HALLAHAN. Yes, sir.

Senator BRICKER. Mention was made about savings banks. I do not know how it is in New England, Senator, but in our State, savings banks operate more like banks than they do savings and loan associations. I do not think any of ours—we have only three—I do not think any of them is a member of the regional board that I know of.

Mr. HALLAHAN. I do not believe they are, Senator.

Senator BRICKER. Two small ones and one very large one, and it has been largely in competition with regular banks, rather than savings and loan associations.

Senator BUSH. I might say to the Senator that I think that is true, they do operate more like banks, but where they feel the competition or where one hears criticism of the competition, they compete for thrift savings; they compete for the savings of the people.

Senator BRICKER. They compete for the savings of the people, that is true, rather than the use of the money after they get it.

Senator BUSH. That is right. It is the competition for the savings that bothers these people, apparently. I have not heard anything about this lately, but I have heard it over the years. The banks feel that with this borrowing authority which the savings and loan association has which they do not enjoy, the savings and loan association can pay a higher interest rate on deposits, and that they do not have that advantage. I guess, as a matter of fact, it is true, is it not? I mean they do have that advantage, the associations, do they not?

Mr. HALLAHAN. We think the mutual savings banks are fine institutions, Senator, and we welcome with open arms for them to join our system.

Senator MONRONEY. They can join freely, can they not?

Mr. HALLAHAN. Yes, sir.

Senator BRICKER. They can also, mutual savings banks can also accept deposits with you, can they not?

Mr. HALLAHAN. Yes, sir.

Senator MONRONEY. If they can get in, they have the same advantage.

Senator BUSH. The State laws would prohibit them not from joining but from borrowing; is that not it?

Mr. HALLAHAN. That may be true in some States.

Senator BRICKER. If they become members, they can borrow just the same as the savings banks, can they not?

Mr. HALLAHAN. That is right.

Senator BUSH. Not if the State law prevents them.

Senator BRICKER. I do not know of any State law preventing them.

Mr. HALLAHAN. I think there may be some States which prevent them from borrowing.

Senator BUSH. That is what he said. I assume there are a lot of them.

Senator DOUGLAS. There is more to this than meets the eye.

Senator BUSH. Mr. Chairman, may I ask that question? Do you know how many States prevent the borrowing of savings banks?

Mr. HALLAHAN. No, sir.

Senator BUSH. Can you supply us with that information conveniently?

Mr. HALLAHAN. Yes, sir.

Senator BUSH. I think we ought to have that.

Mr. HALLAHAN. Most of our savings bank members are from New England, Senator.

Senator BUSH. Yes. I know it is a good business in our State.

Mr. ROBERTSON. There are relatively few States that have mutual savings banks.

Mr. HALLAHAN. Seventeen States that have them.

Senator BUSH. Yes. Well, we have a lot of them. We have both, of course.

Senator DOUGLAS. Senator Monroney.

Senator MONRONEY. First I would like to express my appreciation along with the other members of the committee for this splendid testimony, and may I say it is wonderful to see Mr. Hallahan sitting in the witness seat after so many years as an expert, and a very able expert, with the staff of the House Banking and Currency Committee.

Mr. HALLAHAN. Thank you, Senator.

Senator MONRONEY. Having served on that committee for so many years, we were all gratified, as those who served with him, on his promotion to the Bank Board.

Senator BRICKER. Mr. Dixon came from this committee.

Senator MONRONEY. Could I ask how the directors and officers of the building and loan associations are chosen?

Mr. ROBERTSON. Do you want to answer that, Mr. Dixon?

Mr. DIXON. The directors and officers? The directors are chosen at an election held by shareholders, an annual election held by shareholders.

Senator MONRONEY. How are the votes apportioned, does the amount of stock that the members——

Mr. DIXON. Except there is a limt; there cannot be in excess of 1 vote for every $50 share. Is that not right, doctor?

Dr. HUSBAND. For the Federals, the maximum votes for any institution, irrespective of shares, is 50 votes; where some State associations have only vote.

Senator MONRONEY. It only goes up to the maximum of 50 votes?

Dr. HUSBAND. If you had only a $10,000 account, you would have 50 votes; if you had $3,000, you would have 30 votes.

Senator BUSH. Mr. Chairman, I am very much interested, but I cannot hear this private conversation.

Senator MONRONEY. I am trying to find out how the elections occur.

Senator BUSH. I know, but I cannot hear this gentleman at all.

Dr. HUSBAND. For Federals, you have 1 vote for each $100 par value with a maximum number of votes to be cast by any 1 member of 50. In other words, if you have a $10,000 account you have 50 votes; if you have a $3,000 account, you have 30 votes.

Then you asked the question whether the votes are cast by ballot, I think. The answer to that is, to the best of my knowledge, no.

Senator MONRONEY. At a stockholders meeting at which proxies are available; is that correct?

Dr. HUSBAND. Yes, sir.

Senator MONRONEY. That brings up the point I raised in the banking section law. There is no provision of law requiring or making it eligible to hold stock in phoney names or through dummies; is that correct?

Mr. HALLAHAN. I do not think there is any provision, but it would not serve much of a useful purpose, Senator, because of the large number of eligible voters in our institutions.

Senator MONRONEY. But still it presents a point that I raised in banking, and I think the same rules should apply. Certainly we do not wish racketeers under assumed names to get control of our financial institutions, and I certainly hope that when this bill is finally put in its final form that we will have in all of our financial institutions a requirement that ownership must be in the true name of the owner so that the public will have knowledge of the power that anyone might have in the institutions.

Senator BRICKER. That is true of all corporations too.

Mr. HALLAHAN. We would have no objections to that, certainly.

Senator MONRONEY. I know of no such cases; I am quick to say that there is only a chance that those things could occur.

Senator BRICKER. I think if we could get that provision in all corporations of the country we would solve a very difficult problem.

Senator MONRONEY. Of course, we do not have control of anything excepting the Federal banking and financial structures.

Senator BRICKER. I know that is a source of great trouble in business at the present time; yes.

Senator MONRONEY. Business is more and more being subjected to raids by illegal money and money that is not identified as to its source. You would have no objection, if we write such a provision in the other institutions, that it be incorporated in yours?

Mr. HALLAHAN. No, sir.

Senator MONRONEY. We heard a great deal during the taking of testimony of the suggestion that audits that are made by the institutions themselves, in addition to the inspections by your examiners, be a CPA type of audit. I missed part of your earlier testimony. Did you mention that in your testimony?

Mr. ROBERTSON. No; I did not. But Mr. Bonesteel, our Director of the Division of Examinations, is here, and he has been working on that program, and I would like him to speak on that.

Mr. BONESTEEL. We require every insured institution to have an audit as well as an examination every year. We give them three options on that audit: They can have the audit combined with the Federal examination; they can have a CPA make an audit separate from the examination; and now, under certain conditions which are very strict, we permit an internal audit.

Senator MONRONEY. The defalcation in the Virginia bank evidently indicated a need for additional CPA type of audit. I just wondered——

Mr. BONESTEEL. Well, of course, there it was not so much the audit, Senator, as the utter lack of internal control.

Senator MONRONEY. But would that not be revealed quickly in a CPA type of audit?

Mr. BONESTEEL. It is a very complicated question and a very complicated answer we had to give. We knew, of course, that there was a lot of concentration of conflicting duties in this one person. But that was a State-chartered association, and we really could not control and supervise it as we could a Federal.

We think now that we have tightened up those loopholes, if that is what you refer to, in our relationships with the State departments.

Senator MONRONEY. But in an internal type of audit which you still say you permit, you do not have the outside inspection and investigation of the assets and the records and spot checks on the deposits that a CPA audit would give you?

Mr. BONESTEEL. Yes; we would require verifications by direct correspondence; we would require that the internal audit be absolutely independent of any operating functions.

Of course, what we would like to see is an outside audit plus this internal audit.

Senator MONRONEY. That is just what I am getting at. Would it be too costly or too cumbersome if the same provisions we are talking about on banking institutions be extended to audits of your home loan banking members?

Mr. HALLAHAN. Well, I think what Mr. Bonesteel is saying is that we have always required an audit with respect to our examinations. In many of the cases our examiners perform that audit themselves. We already will accept CPA audits.

Senator MONRONEY. But it is not accepting, it is requiring that I am interested in. You have a great many institutions in which your hard pressed staff has to go in. They examine the books and the records as they come to them. Very few have the time that it takes, such as an independent auditor would have.

Mr. BONESTEEL. May I say that there are a number of reasons why we would not want to—in my opinion, I think the Board would agree—require that they have an audit by a CPA. In the first place, while we like to see it, there are just hundreds of associations that do not have available, without going to a distant city, a CPA. And there are very few CPA's now who specialize in the audits of savings and loan associations. There are a few. But 70 percent of them have only one client in the savings and loan associations. We think it is a good thing, but we think it would be entirely arbitrary and unnecessary to require them to have a CPA audit. We recommend that, and we make the audit. They do have to have an audit, either by ourselves or by a CPA, or now, if they meet these very stringent conditions, they can have an internal audit which we review very carefully.

Senator MONRONEY. And verify the accounts?

Mr. BONESTEEL. The accounts by direct correspondence.

Senator MONRONEY. That is all.

Senator DOUGLAS. I would like to call up a very interesting question that Senator Bush started, namely, the way in which the regional banks get their funds. You say that they get $1,350 million from the purchase of shares by member banks and by deposits from those banks. But they also get some funds from the sale of short-time obligations by those banks. The question I would like to ask is how much of the funds is obtained by the sale of these short-time 6- to 9-month obligations?

Mr. HALLAHAN. I think currently we have somewhere in the neighborhood of $950 million of our——

Senator DOUGLAS. So that roughly 40 percent of the funds is derived from the sale of the short-time obligations?

Mr. HALLAHAN. Currently, yes, sir.

Senator DOUGLAS. Who will buy these short-time obligations?

Mr. HALLAHAN. I think the distribution of purchases is pretty widespread at the moment, Senator. I do not know what the exact figures are currently, but I think probably the commercial banks hold at the present time somewhere in the neighborhood of maybe 20 percent of the total that we have outstanding.

Senator DOUGLAS. But may they not hold indirectly an additional amount, that is, short-time loans to others which permit these other groups to buy the obligations?

Mr. HALLAHAN. Our surveys do not reveal that.

Senator DOUGLAS. It is quite possible that that exists?

Mr. HALLAHAN. It could happen, but I would doubt very seriously whether it was true at the moment. Our other holders are corporations, pension funds.

Senator DOUGLAS. But to the degree that the funds are derived from commercial banks, does that not mean, in effect, that the commercial banks are creating monetary purchasing power which is then used for investment purposes, to the degree to which it does exist?

Mr. HALLAHAN. I do not believe that our obligations are eligible for rediscount by the Federal Reserve System.

Senator DOUGLAS. I am not questioning the rediscount. But the ordinary process in a commercial bank is that the loan comes first. The loan is made in the form of a credit which is then set up in a checking account of the borrower. And, therefore, in commercial banking the banks create the deposit. That constitutes, in effect, the creation of monetary purchasing power.

This is sharply different from investment banking where the bank merely serves as an intermediary between the savings of the individual of current income and the investment in the productive enterprises, normally for long-time purposes.

But I think one of the most serious problems which arises in banking is the use of commercial banks designed usually for short-time purposes and to finance the movement and fabrication of commodities into investment purposes.

I think it is this which is largely responsible for the inflation in the prices of capital goods at the present day. An injection of monetary purchasing power for the purposes of investment in capital goods, rather than a financing of capital goods through diversion of income from consumers' expenditures—and that, therefore, the injection of this additional purchasing power, wherever it occurs, and to the degree that it does occur, creates inflation.

Mr. HALLAHAN. Senator, on that point, I think if we would take the last 5 years and trace the holdings of our securities by the nature of the holder—and I am sure we can supply this for the record—I think we would find that the commercial-banking system has decreased their holdings of our obligations at least from 50 percent to the present 20 percent, or substantially. So although what you say may be true, our experience is the other way.

Senator DOUGLAS. You say it is true, but it is not as bad as it was before, Doctor?

Dr. HUSBAND. Senator, may not the money come from the time deposits and the trust funds of commercial banks instead of the demand deposits?

Senator DOUGLAS. Yes; that is true. But you cannot get around the fact fundamentally that what the commercial banks do so far as their bank function is concerned is to create monetary purchasing power which is placed at the disposal of the borrower. The historic function of commercial banking has been to absorb the time lag in the movement and fabrication of commodities to be repaid out of the successive sales of the articles as they move on toward final consumption. But when you have commercial banking used to finance investment, then you get into a most serious situation, because it is one of the contributing causes to inflation and hence to the recession or depression which is to be compared with the last depression. To distinguish between these two types of banking and to try to have investment banking from savings rather than from the creation of credit is, I think, vitally necessary at the present time.

Mr. HALLAHAN. Senator, in that respect, I think without question at the present time the amount of our obligations which the commercial banks hold would certainly fall into the seasonal cash requirements that are business needs and not necessarily into the investment side of our operation.

Senator DOUGLAS. Would you submit the figures on this matter?

Mr. HALLAHAN. Yes, sir.

(The information referred to follows:)

U. S. Treasury survey of ownership of Federal home loan bank obligations as of dates indicated

Dec. 31	Total amount outstanding (millions)	Percentage distribution		
		Commercial banks	Mutual savings banks	All other investors
1950	$561	81.5	1.3	17.2
1951	529	54.3	1.7	44.0
1952	448	56.9	1.8	41.3
1953	414	47.1	3.9	49.0
1954	273	53.9	.7	45.4
1955	975	26.8	4.8	68.4
1956	963	18.0	4.5	77.5

Source: Federal Home Loan Bank Board, Division FHLB operations, Feb. 15, 1957.

Senator DOUGLAS. Now, 1 or 2 questions which I want to ask for my own information and enlightenment. One question I would like to ask is whether the Board now controls the interest rates which the associations may charge on loans.

Mr. ROBERTSON. No, sir.

Senator DOUGLAS. It does not.

Mr. ROBERTSON. You mean that the savings and loan associations charge?

Senator DOUGLAS. Yes.

Mr. ROBERTSON. They are subject to the interest laws of the States in which they operate. Where there is no limitation. One statute has fixed a maximum rate of 8 percent.

Mr. HALLAHAN. They are required to operate under the laws of the State in which they are located.

Senator DOUGLAS. So that if the State laws prohibit a rate of interest in excess of 6 percent, that becomes the maximum rate for that State.

Mr. ROBERTSON. Yes.

Senator DOUGLAS. Where there are no usury laws in a State, you permit up to 8 percent.

Mr. ROBERTSON. Yes, sir.

Senator DOUGLAS. Do you think there should be some change in this present practice?

Mr. HALLAHAN. No. I believe that the institutions should be subject to the usury laws of the State in which they are located.

Senator DOUGLAS. There has been some proposal that this requirement be removed. I remember hearing some witness testify to that. At least I so understood him.

Mr. ROBERTSON. We would not be in favor of the removal of such requirements, Senator.

Senator MONRONEY. Those usury laws, under your regulations, would they apply to discounts?

Mr. HALLAHAN. It's under the statute.

Senator MONRONEY. You mean the statute?

Mr. HALLAHAN. No, the Federal home loan bank statute itself says the State laws shall prevail.

Senator MONRONEY. They are up and down, I mean, and some of them do not include the earnings if the paper is bought at a discount. In other words, take a home mortgage today that you would buy for 90 and if you are charging 8 percent you would be getting better than 10 percent return.

Mr. HALLAHAN. I think that might be theoretically true, but when you are speaking of an interest rate, such as a 6 percent interest rate, that would be on conventional loans, and most conventional loans are not discounted. The discounts are experienced on the FHA and—well, the GI loans principally.

Senator MONRONEY. But you are allowed to buy any loans, whether they are conventional or not, aren't you?

Mr. HALLAHAN. Yes, sir.

Senator MONRONEY. I mean if they are requesting mortgage loans.

Mr. HALLAHAN. Yes, sir.

Senator MONRONEY. A mortgage loan does not necessarily have to be 50 percent cash.

Mr. HALLAHAN. No, sir. I was merely saying that most conventional loans are not discounted.

Senator MONRONEY. They could be, though, if they are made by a builder, for example, and at, say, a 20 percent downpayment they would be subject probably to a discount even less than FHA's or GI's, so that you would be able to earn better than the legal rate of interest as it applies to the discounted amount of the mortgage. I just wondered if there is any pattern that your organization has, whether it includes the paper bought at discount or whether it is just subject to whatever the State law happens to be as to usury.

Mr. HALLAHAN. It is subject to the State law.

Senator MONRONEY. Do you think it might be wise to have a figure written in or a policy written in to be uniform as to what the interest rate, maximum interest rate, could yield, including the paper that is bought at discount?

Mr. HALLAHAN. Well, Senator, with respect to purchases of mortgages, if they are purchased at a discount, our regulations prohibit taking those discounts into earnings, as do the Internal Revenue regulations. In other words, the amount of the discount has to be amortized over the average life of your mortgage portfolio. So it does not come into your earnings picture immediately, anyway.

I think if you are dealing with the subject of interest rates, you would have to have something that was applicable to all lenders in any area. And I think that is undoubtedly the reason that the provision with respect to interest which Federal home-loan bank members may charge is written the way it is.

Senator MONRONEY. Thank you.

Senator DOUGLAS. There is one question that has puzzled me during the last few years very much, and that is the problem of the conversion. In some localities in States there are mutual savings and loan associations converting into stock associations. This has puzzled me, first, from the standpoint of general policy, and it also puzzles me in the complexities between Federal and State loan associations, between insured and uninsured, and so forth. So that at times I must admit that I seem to be in a wilderness of crosscurrents. But I would like to start, if I may, and see if we can find some path through the wilderness.

What is the present situation? Do you permit the conversion of Federal savings and loan associations, previously organized on a mutual basis, into stock companies?

Mr. ROBERTSON. We have prepared and have published in the Federal Register a regulation which we think will take care of that situation——

Senator DOUGLAS. Now, just a moment. I know the importance of the Federal Register. But in view of the reading matter which I have to cover, it is not possible for me to read that, and, therefore, I do not regard that as a responsive answer. I would like to have you tell the committee what you do, rather than referring me to the Federal Register. It is not addressed to you, but to the common practice of the administrative agencies avoiding answering questions before legislative committees.

Mr. ROBERTSON. I am sorry. I said that only by way of introduction——

Senator DOUGLAS. I am just indicting you for a general sin which you are practicing. Go ahead. What are your regulations?

Mr. HALLAHAN. I think that the answer to your question at the moment is we do not now permit Federal associations to convert to stock companies. We have published, if the Senator will bear with me, a proposed regulation appeared in the Federal Register. It is not effective at the present time.

Senator DOUGLAS. When will it be effective?

Mr. HALLAHAN. I think this is the second publication. And there were changes from the first one—and it could not become effective for at least, I think, another month. The reason the Board published it is to get comments from everybody concerned, anyone desiring to make comments, and we will review and evaluate those.

Senator DOUGLAS. What is the practice over the country so far as the State associations are concerned? How many States permit this, how many States forbid it, how many States do not deal with it?

Mr. HALLAHAN. Dr. Husband informs me that 11 States permit conversions.

Senator DOUGLAS. What are those States, Dr. Husband?

Dr. HUSBAND. California, Illinois, Ohio, Utah, the State of Washington, Virginia, Texas—I happen to have the exact names here, Senator. It will just take me a moment to put my finger on it and give it to you. California, Virginia, Ohio—permitted in Indiana, but it is practically nonexistent—Texas, Colorado, Kansas, Arizona, Idaho, Utah and Guam.

Senator DOUGLAS. And Illinois?

Dr. HUSBAND. And Illinois; that is right. Illinois was added since I——

Senator DOUGLAS. Those are the States in the historical order in which this permission has been added?

Dr. HUSBAND. No, sir, I don't think so. I may add that you now have 339 stock companies, insured stock companies, in existence, with assets of between $4 billion and $4.5 billion.

Senator DOUGLAS. What percentage of the business is now in the hands of the stock companies?

Mr. HALLAHAN. Ten percent.

Dr. HUSBAND. About 10 percent.

Senator DOUGLAS. Have you previously had this provision against Federal savings and loan institutions converting from a mutual to a stock basis, or is this a new regulation, Doctor?

Dr. HUSBAND. There have been 28 conversions in total from the time the corporations were organized in 1944, 7 being Federal, direct Federal-stock, 9 going from Federal to State mutual and stock, and the remaining 12 going direct from State mutual to State stock. The other stock companies, in other words, were started new as stock companies, and we have had an accumulative total of 28 conversions.

Senator DOUGLAS. What volume of business is that in the conversions?

Dr. HUSBAND. Their assets?

Senator DOUGLAS. Yes, sir.

Dr. HUSBAND. As of the date of conversion, I presume.

Senator DOUGLAS. Will you supply that, Doctor?

Dr. HUSBAND. I would be very happy to supply that, sir.

Senator DOUGLAS. May I ask about savings and loan institutions which are controlled by one of your sister corporations. I guess you wear three hats, do you not?

Mr. HALLAHAN. Only two.

Senator DOUGLAS. Only two. What is the practice on insurance? Will you insure State savings and loan associations which convert from mutual to stock?

Dr. HUSBAND. That is assuming that the conversion has already taken place. Is that the question?

Senator DOUGLAS. Well, let's ask first—what about conversions which are going to take place?

Dr. HUSBAND. If the applications for insurance came in during that period?

Mr. HALLAHAN. The insured mutual——

Senato rDOUGLAS. Now we are really getting into the difficulties. Let us say that they have already been insured but now want to convert from mutual to stock.

Dr. HUSBAND. As of this date, as of this time, and for the last year-and-a-half the Board has approved no such conversions of an existing insured mutual over to a stock basis. There is some question, however, as to the point of authority.

Senator DOUGLAS. Has it done this on a case-by-case handling, or has it promulgated general rules?

Dr. HUSBAND. It has been on a general policy basis.

Senator DOUGLAS. Has this policy been crystallized in a regulation?

Dr. HUSBAND. No, sir.

Senator DOUGLAS. In other words, this is something which exists in the minds of these gentlemen but which has not yet been put on paper.

Dr. HUSBAND. It exists in the minds of the Board as a declared resolution of policy that will be applied to all cases of that type.

Senator DOUGLAS. I would like to have a comment from the Board in this matter. Why don't you put it in the form of a regulation?

Mr. HALLAHAN. Senator, I think all of the institutions in the industry are aware of the Board policy of which Dr. Husband spoke. The Board in its testimony stated that it is not crystal clear whether we have the authority to approve the conversions of State insured mutuals to State stock companies. The Board, in its testimony this morning, has asked the Congress to clarify this matter for us.

Senator DOUGLAS. Which way do you want to clarify it?

Mr. HALLAHAN. We have recommended, I believe, that the Board be given this authority, clearly, and a proposed amendment which would carry out that recommendation.

Senator DOUGLAS. Now, does the——

Mr. HALLAHAN. But we think it is something the Congress should decide.

Senator DOUGLAS. Does the proposed codification increase your powers, diminish your powers, or leave them unaffected?

Mr. HALLAHAN. They leave them unaffected.

Senator DOUGLAS. I imagine I did not cover all the possibilities of these State associations. What about State associations which are not yet insured but wish to become insured? Must they be mutuals before they can be insured?

Mr. HALLAHAN. No, they can be either mutual or stock companies, Senator.

Senator DOUGLAS. That means you will not refuse insurance because they are stock companies.

Mr. HALLAHAN. No, sir, there are several States which have long permitted stock savings and loan associations, and we draw no distinction between them.

Senator DOUGLAS. In other words, if they are a stock company, you make no objection to their being insured.

Mr. HALLAHAN. No, sir.

Senator DOUGLAS. It is only if they have been a mutual enterprise that you restrict conversion into a stock company.

Mr. HALLAHAN. Yes, sir, and that is the area in which we are asking for a clear expression of congressional policy.

Senator DOUGLAS. Mr. Rogers has another problem for you, which I had better let him present to you.

Mr. ROGERS. What about the situation where you have a Federal that converts into a State mutual and then into a State stock company?

Senator DOUGLAS. And still wants to keep its insurance.

Mr. ROGERS. Yes.

Dr. HUSBAND. There were nine of those cases that I mentioned.

Mr. ROGERS. Those were the nine that you mentioned?

Dr. HUSBAND. Yes, sir.

Mr. HALLAHAN. The Board, I believe, this past summer, the summer of last year, adopted a policy based upon the opinion of its general counsel that such conversions could not take place without the approval of the Board; that our construction of the statute which the Congress passed would not permit what is referred to as a two-step conversion without the Board's approval.

Mr. ROGERS. In other words, what you prohibit directly they could not do indirectly.

Mr. HALLAHAN. That is it, exactly.

Senator DOUGLAS. Then do I gather this—that while you do not propose to override State laws, that your general feeling is that it is unwise for mutuals in the building and loan field to convert into stock companies? It is not in the public interest.

Mr. HALLAHAN. We believe, Senator, that if the Congress desired to permit such conversions, that the public interest requires that the interest of the shareholders be fully protected.

Senator DOUGLAS. I see that you have taken good lessons from hearing for many years administrative officials testify before congressional committees, and you have become as artful as the most artful administrative officials.

Mr. HALLAHAN. I did not intend to leave that impression, Mr. Chairman.

Senator DOUGLAS. Is it true or is it not true that some of the tax provisions which have been granted to savings and loan associations have been given on the assumption that they are mutuals and cooperatives and that therefore they did not make profits but shared in savings?

Mr. HALLAHAN. Well, I believe the Senator is better acquainted with that subject than I.

Senator DOUGLAS. No; I am an inexperienced city boy lost in the woods.

Mr. HALLAHAN. Well, I wouldn't subscribe to that statement, Senator. But there is no question about the fact that any institution which is investing principally in long-term investments of the home-mortgage type must be able to accumulate reserves against the losses which it might expect. And I think that the tax treatment which has been applied to savings and loan associations, both stock associations and mutuals, takes into recognition the fact that they are accepting the savings of the public, and taking those savings and investing them in long-term investments, and that some tax-free loss reserve must be provided for the protection of those long-term investments. The same, of course, is true of savings banks. They are on a similar pattern. How much of the tax treatment is weighted because they are mutual institutions and how much of that tax treatment depends solely upon the nature of the investment I would be hesitant to say.

Senator DOUGLAS. Well, of course, when an association which aimed to remove what it said was the unjust favoritism granted to cooperatives started its propaganda, it was originally designed to curb consumer cooperatives.

Mr. HALLAHAN. Yes, sir.

Senator DOUGLAS. Then it was discovered that there were not many consumer cooperatives and that this proposal was primarily aimed at the cooperatives and building and loan associations and mutual savings banks. I think it is true that those interested savings banks, mutual savings and loan associations, and with the backing those groups have, have urged separate tax treatment as justified in that they are merely institutions whereby economies and savings can be passed on to members in proportion to use, and that therefore they are not profits in the ordinary sense, and that separate tax treatment is justified.

This is a very vital question. I wondered if the Board had given any thought to it.

Mr. HALLAHAN. Well, speaking as one member, we, as supervisors, which we are, of these institutions, have a very fundamental and deep-seated feeling about the reserves which the institutions should maintain. And in a regulation which the Board published only this last year, which is currently effective, we have strengthened the requirements with respect to reserves. We would not want to see the tax treatment, whether for stock or mutuals, dissipated below the present level, because as supervisors, recognizing the fact that they are long-term investors, we would like them to be able to accumulate a reserve which experience has shown is necessary for this type of financial institution.

Senator DOUGLAS. Just one final question. This was suggested by Mr. Rogers. Do savings and loan associations organized on a stock basis now have the same tax rates and privileges as savings and loan associations organized on a mutual basis?

Mr. HALLAHAN. With respect to the accumulation of loss reserves only, Senator. With respect to the dividends which are paid on that stock, they are treated the same as dividends paid on any other corporate enterprise.

Senator DOUGLAS. Yes—treated as income to the recipient.

Mr. HALLAHAN. Yes, sir.

Senator DOUGLAS. So patronage dividends of cooperatives are treated as income to the recipient.

Mr. HALLAHAN. It is treated the same as a bank in that respect. In other words, that income out of which the dividends are paid is subject to the corporate income taxes, the same as any other corporation.

Mr. ROGERS. But do they still have the 12-percent reserves?

Mr. HALLAHAN. With respect to reserves; yes.

Mr. ROGERS. The income out of it is taxable.

Mr. HALLAHAN. Yes, sir.

Senator DOUGLAS. Whereas in a mutual the income to the member is taxed as individual income and does not have a prior deduction.

Mr. HALLAHAN. Yes, sir.

Senator DOUGLAS. Or a corporate deduction.

Mr. HALLAHAN. Yes, sir.

Senator DOUGLAS. Well, thank you very much. In general I want to congratulate the Board. I am much impressed with both the quality of your testimony and the spirit in which you presented it.

I urge you to consider that Members of Congress are not the ogres which they are considered to be and more frankness in dealing with the Members of Congress is most appropriate.

Mr. HALLAHAN. Thank you, sir.

(The addenda A and B referred to follows:)

ADDENDUM A TO STATEMENT OF ALBERT J. ROBERTSON, CHAIRMAN, FEDERAL HOME LOAN BANK BOARD

AMENDMENT NO. 1

At page 184, after line 4, insert the following new subsection:

"(e) No member shall carry on any sales plan or practice, or any advertising, in violation of regulations of the Board: *Provided*, That this subsection shall not authorize the Board to impose any greater limitations or restrictions on members than the Board or the Federal Savings and Loan Insurance Corporation may from time to time impose on insured institutions under title IV of the National Housing Act as now or hereafter in force (including agreements therein provided for) or otherwise."

AMENDMENT NO. 2

At page 227, after line 3, add to section 408 a new subsection to be appropriately lettered and to read as follows:

"As used in this subsection, the term 'institution' means an insured institution other than a Federal savings and loan association. Whenever in the opinion of the Board any director or officer of an institution has violated or is violating any law or regulation relating to such institution or has engaged or is engaging in unsafe or unsound practices in conducting the business of such institution or has violated his duty to such institution as a director or officer, the Board may notify the board of directors of such institution to remove such director or officer from office. If, within thirty days from the date of the notification to it by the Board, the board of directors of such institution shall have failed or refused to remove such director or officer as hereinbefore provided, the Board may cause notice to be served upon such director or officer to appear at a hearing before the Board, a member thereof, or a person designated by the Board and show cause why an order of removal should not be issued against him. The notice shall state the ground or grounds upon which it is based. A copy of such notice shall be sent to each director of the institution affected by registered mail. The Board may issue an order of suspension against such director or officer pending final determination upon the question of the issuance of an order of removal against him. If, after hearing, the Board finds that such director or officer has violated or is violating any law or regulation relating to such institution or has engaged or is engaging in unsafe or unsound practices in conducting the business of such institution or has violated his duty to such institution as a director or officer, the Board may issue an order of removal against such director or officer. A copy of such order shall also be served upon the institution of which he is a director or officer. Any such director or officer against whom an order of removal has been issued as herein provided who thereafter participates in any manner in the management of such institution, or any such director or officer who participates in any manner in the management of such institution while such an order of suspension against him is in effect, shall be fined not more than $5,000 or imprisoned for not more than 5 years, or both, in the discretion of the court. As used in this subsection, the term 'order of removal' means an order directing a person to resign or otherwise cease to hold office, and the term 'order of suspension' means an order directing a person to refrain from participating in the management of an institution pending determination upon the question of the issuance of an order of removal against him. If at the expiration of thirty days from the date on which such an order of removal becomes conclusive as against further proceedings by way of review as provided for in this subsection, such director or officer shall not have ceased to hold office, the Board, without any requirement of notice or hearing, may, by order, terminate the status of such institution as an insured institution or its membership in any Federal home-loan bank, or both, and the action of the Board shall be final. In case of such termination of insured status, the provisions of this title with respect to continuance of insurance, examination, payment of final premium, and notice to insured members in cases of termination of insured status shall be applicable, and in case of such termination of membership the provisions of the Federal Home Loan Bank Act as now or hereafter in force with respect to liquidation of indebtedness, surrender and cancellation of capital stock, and payment for capital stock surrendered in cases of termination of membership shall be applicable. The provisions of this title with respect to hearings and court review in cases of termination of insured status shall be applicable with respect to proceedings under this subsection for the removal of a director or officer."

AMENDMENT NO. 3

At page 220, after line 5, insert the following new subsection:

"(k) No insured institution shall, in violation of regulations of the Corporation, (1) issue any security (i) not having the same characteristics as a security of such institution previously issued and currently outstanding or (ii) the issue of which is contrary to any agreement entered into with the Corporation or any condition imposed by the Corporation in connection with the insurance of the accounts of such institution or otherwise; (2) enter into, become a party to, or consent to any contract, agreement, or arrangement, or take any other action for modification of, or which has the effect of modifying, any of the characteristics of any security of such institution which is currently outstanding or which it is authorized to issue; or (3) enter into any management contract, agreement, or arrangement, or any contract, agreement, or arrangement for the rendering to such institution of management or similar services. As used in this subsection, the term 'security' means any share, stock, note, bond, or debenture, or any right or interest in or with respect to, or obligation of or with respect to, an insured institution or a security thereof, or any other right, interest, or obligation defined by regulations of the Corporation to be a security for the purposes of this subsection, whether or not any of the same be evidenced by a writing."

AMENDMENT NO. 4

At page 200, line 13, amend subsection (b) to read as follows:

"(b) It shall not be lawful for any employee of the Board (or of the Federal Savings and Loan Insurance Corporation) to accept, or for any former employee of the Board (or of said Corporation) to accept within two years after the termination of his employment as such employee, employment with any member of a Federal Home Loan Bank except pursuant to regulations prescribed by the Board or pursuant to prior written consent of the Board. Any person convicted of any violation of any provision of this subsection shall be fined not more than $10,000 or imprisoned not more than five years, or both. The provisions of this subsection shall not apply to any former employee of the Board (or of said Corporation) who is such a former employee solely by reason of employment which terminated prior to the effective date of this subsection."

AMENDMENT NO. 5

At page 221, line 31, after the period, insert the following new sentences:

"No insured institution shall establish any branch unless it shall have the prior written approval of the Corporation by regulations or otherwise, and no insured institution shall move its principal office or any branch without such prior written approval. As used in this subsection, the term 'branch' means any office (other than the principal office) of an insured institution at which accounts of an insurable type are opened or payments thereon are received or withdrawals therefrom are paid, or any other office (other than the principal office) of an insured institution which is defined by regulations of the Corporation as a branch."

AMENDMENT NO. 6

At page 251, after subsection (h), insert the following new subsections:

"(i) Section 655 of title 18 of the United States Code is hereby amended (1) by striking in the first sentence the word 'bank' in the language 'bank examiner'; (2) by striking in the first sentence the language 'or from any safe deposit box in or adjacent to the premises of such bank' and inserting in lieu thereof the language 'or in the possession of an institution the accounts of which are insured by the Federal Savings and Loan Insurance Corporation, or from any safe deposit box in or adjacent to the premises of any such bank or institution'; (3) by striking in the second sentence the language 'or banks the deposits of which are insured by the Federal Deposit Insurance Corporation, whether appointed by the Comptroller of the Currency, by the Board of Governors of the Federal Reserve System, by a Federal Reserve agent, by a Federal Reserve bank, or by the Federal Deposit Insurance Corporation' and inserting in lieu thereof the language ', banks the deposits of which are insured by the Federal Deposit Insurance Corporation, or institutions the accounts of which are insured by the Federal Savings and Loan Insurance Corporation, whether appointed by the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, a Federal Reserve agent, a Federal Reserve bank, the

Federal Deposit Insurance Corporation, the Federal Home Loan Bank Board, or the Federal Savings and Loan Insurance Corporation'; and (4) by inserting in the second sentence, immediately before the period, the language 'or of an institution the accounts of which are insured by the Federal Savings and Loan Insurance Corporation'.

"(j) Section 1906 of title 18 of the United States Code is hereby amended (1) by striking the language 'or bank insured by the Federal Deposit Insurance Corporation' and inserting in lieu thereof the language', bank insured by the Federal Deposit Insurance Corporation, or institution the accounts of which are insured by the Federal Savings and Loan Insurance Corporation'; (2) by inserting after the language 'the proper officers of such bank' the language 'or institution'; and (3) by striking the language 'or the Federal Deposit Insurance Corporation as to any other insured bank, or from the board of directors of such bank' and inserting in lieu thereof the language', the Federal Deposit Insurance Corporation as to any other insured bank, or the Federal Savings and Loan Insurance Corporation as to any institution the accounts of which are insured by the Federal Savings and Loan Insurance Corporation, or from the board of directors of such bank or institution'.

"(k) Section 1909 of title 18 of the United States Code is hereby amended by inserting therein. immediately after the comma following the language 'in any capacity', the language 'or whoever, being an examiner or assistant examiner of institutions the accounts of which are insured by the Federal Savings and Loan Insurance Corporation, performs any other service, for compensation, for any Federal or other savings and loan association, building and loan association, cooperative bank, or homestead association, or for any officer, director, or employee thereof, or for any person connected therewith in any capacity,'."

AMENDMENT NO. 7

At page 215, line 18, strike the sentence beginning at this line and in lieu thereof insert the following: "For the purpose of determining the amount of insurance under this title, any account which is in the sole names of two persons who are husband and wife and which under applicable law is community property of such husband and wife shall be treated as if it were an account held by said persons in joint tenancy, and any account which is in the sole name of a husband or wife and which under applicable law is community property of such husband or wife and the spouse of such husband or wife shall be treated as if it were an account held by said husband or wife and such spouse as tenants in common in equal amounts."

AMENDMENT NO. 8

At page 251, line 25, strike "and (2)" and insert in lieu thereof "(2) by striking 'section 401' and inserting in lieu thereof 'section 402'; and (3)".

ADDENDUM B TO STATEMENT OF ALBERT J. ROBERTSON, CHAIRMAN, FEDERAL HOME LOAN BANK BOARD

TECHNICAL AMENDMENTS

Page 184, line 22, strike "Home Loan Bank".
Page 185, line 35, strike "board" and insert "Board".
Page 186, line 15, strike "board" and insert "Board".
Page 186, line 18, strike "board" and insert "Board".
Page 187, line 20, strike "board" and insert "Board".
Page 187, line 28, strike "board" and insert "Board".
Page 188, line 25, strike "board" and insert "Board".
Page 189, line 6, strike "board" and insert "Board".
Page 191, line 4, strike "purpose" and insert "purposes".
Page 192, line 16, at end of line, insert a period.
Page 193, line 8, strike "board" and insert "Board".
Page 193, line 17, strike "banks" and insert "bank".
Page 194, line 3, strike "(g)" and insert "(g))".
Page 194, line 8, strike "board" and insert "Board".
Page 194, line 24, strike "public debt" and insert "public-debt".
Page 203, line 25, strike "by the Board".
Page 204, line 28, strike "Federal home-loan bank" and insert "Federal Home Loan Bank".
Page 208, line 33, strike "Federal home-loan bank" and insert "Federal Home Loan Bank".
Page 208, line 35, strike "Federal home-loan bank" and insert "Federal Home Loan Bank".
Page 209, line 13, strike "Federal home-loan bank" and insert "Federal Home Loan Bank".
Page 210, line 30, strike "Home Loan Bank".
Page 210, line 37, strike "Federal home-loan bank" and insert "Federal Home Loan Bank".
Page 210, last line, strike "Federal home-loan bank" and insert "Federal Home Loan Bank".
Page 216, next to last line, strike "service" and insert "services".
Page 219, lines 17 and 18, strike "Home Loan Bank".
Page 219, line 31, strike "herafter" and insert "hereafter".
Page 221, line 20, strike "404" and insert "405".
Page 222, line 14, strike "403" and insert "404".
Page 224, line 10, strike "which ever" and insert "whichever".
Page 250, line 6, strike "Federal home-loan bank" and insert "Federal Home Loan Bank".
Page 251, lines 1 and 2, strike "Federal home-loan bank" and insert "Federal Home Loan Bank".

Senator DOUGLAS. The committee is recessed until Monday at 10 o'clock.

(Whereupon, at 12:35 p. m. the subcommittee was recessed until 10 a. m., Monday, February 18, 1957.)

×

STUDY OF BANKING LAWS

Financial Institutions Act of 1957

MONDAY, FEBRUARY 18, 1957

United States Senate,
Committee on Banking and Currency,
Subcommittee on Banking,
Washington, D. C.

The subcommittee met in Room 301, Senate Office Building, at 10 a. m., Senator A. Willis Robertson, chairman of the subcommittee, presiding.

Present: Senators Robertson, Sparkman, Douglas, Monroney, Clark, Bricker and Bush.

Also present: L. A. Jennings, Deputy Comptroller of the Currency.

Senator Robertson. The subcommittee will please come to order. We have with us this morning the Attorney General of the United States, who will speak for the Justice Department on a phase of the proposed bill in which the Justice Department is primarily interested.

You may proceed.

STATEMENT OF HERBERT BROWNELL, JR., ATTORNEY GENERAL OF THE UNITED STATES; ACCOMPANIED BY ROBERT BICKS, ACTING FIRST ASSISTANT, ANTITRUST DIVISION, DEPARTMENT OF JUSTICE

Mr. Brownell. Mr. Chairman. Mr. Robert Bicks of the Department of Justice is here with me this morning, and if it is agreeable to you I will have a short prepared statement that I would like to read, and with your permission, insert in the record.

I appreciate this opportunity to come before the committee to present the Jsutice Department's views on certain legal aspects of the pending committee print "to amend and revise the statutes governing financial institutions and credit." As you undoubtedly know, the great bulk of this bill treats matters beyond this Department's direct concern. Only a few of its provisions cover problems on which we might helpfully comment. Of these, I plan today to focus primarily on section 23, chapter 5, of title 3—covering bank mergers and consolidations.

That provision would, first, require premerger consent to most banking mergers by the appropriate banking agencies. "In granting or withholding consent," that proposal specifies, "the appropriate agency shall also take into consideration whether the effect thereof may be to lessen competition unduly or to tend unduly to create a monopoly."

Finally, according to proposed section 23, "the appropriate agency may also (and let me emphasize the word 'may') request the opinion of the Attorney General with respect to such question."

Treating this provision, my plan is, first, to emphasize need for more effective curbs on certain bank mergers, a need recognized by the President of the United States, this Department, and interested banking agencies alike, but which we believe is not adequately met in this bill. Secondly, I would like briefly to show why, in our opinion, proposed section 23 runs afoul of basic—governmentwide—principles of comity between prosecuting and supervisory agencies. Third, to meet these objections, I shall offer alternatives to presently proposed section 23.

First, the need for reasonable curbs on bank mergers. This need stems from present section 7 of the Clayton Act's failure to cover asset acquisitions by banks, as distinguished from stock acquisitions. The section provides, as to stock acquisitions, that it applies to all corporations, "engaged in commerce." Section 7's asset acquisition portion, in sharp contrast, covers only corporations "subject to the jurisdiction of the Federal Trade Commission." Further, section 11 of the Clayton Act exempts banks from Federal Trade Commission jurisdiction by specifying that "authority to enforce compliance" with section 7 "is hereby vested * * * in the Federal Reserve Board where applicable to banks, banking associations, and trust companies." On the basis of these provisions the Department of Justice has concluded, and all apparently agree, that asset acquisitions by banks are not now covered by section 7 as amended in 1950.

As a result, section 7 is for practical purposes useless to cope with what the Comptroller of the Currency has described as "this recent trend of (bank) mergers, consolidations, and sales." Corroborating the rise in bank mergers, the Chairman of the Board of Governors of the Federal Reserve Board concluded that bank mergers "have gone up steadily." In 1952 his testimony—I believe before this committee—reveals there were 100 bank mergers. This number jumped to 116 in 1953 and more than double to 202 in 1954, and reached 232 by the end of 1955. Most important, the Federal Reserve Board Chairman concluded in mid-1955, this number is "still rising." As a result, the Board Chairman has stated:

> The current trend in bank mergers and consolidations is a matter which deserves careful consideration and one to which the Board of Governors has given a great deal of thought * * *

This bank merger trend must be viewed against the background of present commercial bank asset concentration. In 9 of 16 of America's principal financial centers, 2 banks owned more than 60 percent of all commercial bank assets. And in each of these 16 centers, the first 2 banks owned more than 40 percent of all commercial bank assets. From these figures, it seems clear, emerges a picture of a steadily increasing bank asset concentration.

It is true that we may still move against this tide of bank mergers to a limited extent under Sherman Act section 1. But mergers may meet Sherman Act standards yet fall before the Clayton Act's more stringent bans. Congress' clear object in its 1950 amendment of section 7 was to strike some mergers beyond the reach of the Sherman Act. Thus the Senate report explains that the—

* * * bill is not intended to revert to the Sherman Act test. The intent here * * * is to cope with monopolistic tendencies in their incipiency and well before they have attained such effects as would justify a Sherman Act proceeding.

The report further states that the act's intent is to have—

* * * broad application to acquisitions that are economically significant * * * (The) various additions and deletions, some strengthening and others weakening the bill, are not conflicting in purpose or effect. They are merely different steps toward the same objective—namely, that of framing a bill which, although dropping portions of the so-called Clayton Act test that have no economic significance, reaches far beyond the Sherman Act.

To apply such a competitive standard to bank asset acquisitions, as it now does to bank stock mergers, is our clear aim. And this general broad aim, apart from disagreements over means, is endorsed—in principle—by the President of the United States, the Department of Justice, the Federal Trade Commission, and appropriate banking agencies.

To detail this point, the President, in his Economic Report sent to Congress within the month, has reiterated the need for, as he put it, "extension of Federal reglation to cover bank mergers by asset as well as by stock acquisition." Similarly, Gov. J. L. Robertson of the Board of Governors of the Federal Reserve System stated last session before the House Antitrust Subcommittee considering like legislation: "The Board favors the objective of this legislation."

Senator Robertson. Will the witness yield at that point?

Governor Robertson testified before this committee this year also.

Mr. Brownell. Did he?

Senator Robertson. Yes; he said that he not only favored the objective, but he favored the plan.

Mr. Brownell. As outlined in section 23?

Senator Robertson. As written in the tentative bill. The Federal Reserve Board gave it emphatic endorsement, and so did the Comptroller General. So the administration seems to be just a little bit at cross-purposes on this proposal. The provision in the bill was endorsed by a fine group, which I call my advisory group, of 27 men—bankers and credit men. It was endorsed by the American Bankers Association. It was endorsed last year by this committee, and it passed the Senate.

So we have all the testimony so far, except yours, in favor of the bill, and we have all of the Federal agencies, except yours, in favor of the bill.

We have the record here. We have all of the big banking associations and credit associations in favor of the bill. We have it a matter of record that the Senate voted last year and passed it, but I still say you have the right to renew your objections to it.

Mr. Brownell. I deeply appreciate that, and I am not only in accord with the objective of the bill, but I am going to submit to you as the last part of my statement this morning a new method of implementing the objective which I think will meet the broader law enforcement objectives I shall treat and still carry out the intent that you have in mind. It is the third part of my statement today, which I think is the most important.

I think it will, or I hope it will, convince you that you can accomplish everything you have in mind in section 23 and still not jeopardize the antitrust work of the Department of Justice. That is at least what I am going to try to convince you.

Senator ROBERTSON. I am not denying your suggestions and we will hear them all. They will all be made a part of the record. If you get the civil rights legislation in which you are so much interested you are going to have your hands pretty full without taking on any additional bank merger program.

Mr. BROWNELL. We are not going to divert any of our antitrust work to civil rights.

Senator CLARK. In that regard, you have a friend here.

Mr. BROWNELL. So your statement there, Mr. Chairman, does give me a chance to make one of the main points I have here this morning, which is that I am entirely in sympathy with the objective of this section 23, and I only ask for a modification, as you will see as I go along, for the purpose of not interfering with the regular antitrust work of the Department in other areas which may involve other regulatory agencies. I believe the two objectives are not necessarily inconsistent.

Senator ROBERTSON. Fine. You may proceed.

Mr. BROWNELL. Endorsing this view, the Comptroller of the Currency stated before the House Antitrust Subcommittee (subcommittee No. 5):

> We are in accord with the general purpose of H. R. 5948 (amending Clayton Act sec. 7 to cover bank assets, as it now does bank-stock acquisitions). We have no objection to the principle that the acquisition of one bank by another through purchase, merger, or consolidation should not be permitted if the effect of the acquisition may be substantially to lessen competition. It is no less important to have competition in banking, when this can be done soundly, as it is in other fields of commerce and industry.

In the course of analyzing various differences over methods, this broad agreement on principle should not be obscured.

This agreed-upon need for reasonable restraints on bank mergers proposed section 23 fails to meet. The proposed provision, I suggest, is deficient on at least two basic scores. First, it would set up competitive tests for bank mergers different from those that apply to other sections of American business. Second, in its present form, it might, even beyond the banking area, seriously dissipate enforcement efforts by decentralizing responsibility for decisions affecting Clayton Act section 7. Both objections, to repeat, to my view, are rooted in firm principles of equitable enforcement and uniform administration of justice.

Of these two points, first, weaker section 7 standards for bank mergers. According to proposed section 23, competitive factors would be only one of numerous considerations to be taken into account by a banking agency in scanning a merger. That in itself I do not object to. Beyond that, the competitive considerations specified, whether the acquisition may "lessen competition unduly or to tend unduly to create a monopoly," are completely novel and are intended simply to be less stringent than those specified by Clayton Act section 7 for other American business. As a result, not only does that proposal prescribe pale antitrust standards, but even that lesser standard is only one of many factors banking agencies must consider.

Senator ROBERTSON. May I interrupt again?

Mr. BROWNELL. Yes.

Senator ROBERTSON. I am sure you will agree with us that banks are under many more Federal regulations and controls than the average business. A bank is in business to accept deposits and lend money, but on all member banks the Government tells them how much they can pay on their deposits. The Government tells them to what extent they can invest their assets in loans. Therefore, I do not think it is too unusual that we put in this bill the words "undue competition," because the competition already is right strenuously regulated by other laws that the average business does not have.

For example, those making automobiles, or steel, or something like that, have no such regulations. When you consider the merger, for instance, of United States Steel and Bethlehem, it would not be up against what the Chase and Manhattan are, where let us say, one is a State bank and one is a Federal bank, and they are already regulated.

Mr. BROWNELL. I fully recognize there are separate and additional factors which must be taken into consideration with the banking agencies, when they come to pass upon the matter. Nevertheless, when they are passing on this one factor, it seems to me that they should, as I will point out a little more fully later, have the same standard as they do in the case of industrial corporations.

Senator CLARK. Might I ask a question at this point?

Senator ROBERTSON. Surely. The Senator from Pennsylvania.

Senator CLARK. Mr. Attorney General, I wonder how you react to this general point of view: It does seem to me that it is necessary with our expanding American economy to have financial institutions with resources big enough to be able to make the loans to these gigantic corporations whose needs are constantly expanding.

We in Philadelphia have that problem because we do not have any bank really big enough to deal with some of our local industries, and they have to go to New York in order to get their money—which we very much abhor from our parochial point of view.

However, at the same time I am very much concerned personally about the enormous power which is placed in the hands of a few large banks, if, as a result of merger and a consolidation process, they come to absorb almost all of the smaller banks in a given community.

I was sort of on the fence as to whether "unduly" was not a good enough word to put into this bank legislation rather than "substantially lessen competition," because I do know we have to have banks big enough to make these loans.

I wonder what your feeling would be with respect to how we can handle the economic needs, and at the same time attempt to maintain a competitive status, so that we will not vest all of this enormous financial power in these institutions?

Mr. BROWNELL. I am going to direct my remarks directly to that point as we go along. I think we have under the present Clayton Act a standard which has been interpreted now for about 40 years so we know pretty definitely what it means.

Senator CLARK. That is the rule of reason?

Mr. BROWNELL. Yes; among other things. More specifically, I refer to the "substantial lessening of competition" standard.

As I point out here, there is a very definite application to specific types of mergers and acquisitions. If you come in and introduce a new term like "unduly," which has never been interpreted before, in the first place you will have a period of uncertainty. Even more disturbing than that to me is that I think there will be an attempt to apply that new standard, that lesser standard, that weaker standard, to the industrial area. That will be very difficult for us when it comes to the administration of the antitrust laws.

Senator CLARK. I am no expert in antitrust litigation, but suppose we go back to "substantially" and you have a continuation of some of these bank mergers and consolidations. Is it not going to be almost impossible to permit any of them, because almost any bank merger at this point would seem to be more or less clearly substantially decreasing competition. How do you get around that one?

Mr. BROWNELL. Well, I would say that in the proposal which we are making here this morning, we recognize that there might be other factors. There would be straight banking factors that banking agencies would have to take into consideration. The antitrust factor would be only one of several. But the point we are trying to make is, to make the antitrust language the same as you have it in the general business field so you will not unduly interfere with our administration of that law, and yet you can give full recognition to the fact that there are straight banking factors which have to be taken into consideration. The banking agency passing on the matter could take the whole bundle of factors and make a final decision on them.

Senator CLARK. Has the Attorney General on the antitrust provision gotten into the bank merger and consolidation field in recent years?

Mr. BROWNELL. Yes; we have. I am going to cite one example this morning. I think there have been two or three suits under the Sherman Act provisions.

Under the Clayton Act we have had anywhere from a half a dozen to a dozen investigations of banking mergers that I can recall in the last year.

Senator CLARK. I imagine in your testimony you will comment on the administrative problems of having this expert group of regulators in the field, and yet having your own general antitrust responsibilities.

Mr. BROWNELL. Yes. And it is that danger of conflict between those two groups we are trying to avoid. We are trying to present to you this morning a proposal which would lead to cooperation between the two groups, and yet take into consideration the specialized banking factors involved.

Senator ROBERTSON. I am sure you want to help us keep this record straight. You proceeded against Transamerica under the Clayton Act.

Mr. BROWNELL. I believe that was the Federal Reserve Board rather than the Department of Justice, Senator.

Senator ROBERTSON. I thought the Department of Justice participated in that. The Federal Reserve Board did initiate it.

Mr. BROWNELL. I think it was only on the appeal, when, of course, it has come through the Department of Justice. But I believe—of course, it was before my time—but I believe I am correct in saying that was instituted by the Federal Reserve Board.

Senator ROBERTSON. I know the Government spent a lot of money on it. In the first place, it was a bank holding company, and, of course, the biggest in the United States, but a bank holding company and not a bank. In the second place, they lost the case. That was picked out as the most glaring example that you could not make it stick.

Can you cite any bank merger you ever prosecuted other than Transamerica?

Mr. BROWNELL. I do not want the record to show I do not know. I can say with some definiteness that was the Federal Reserve Board that commenced and handled that case—at least in the courts below.

Senator ROBERTSON. I understood you to say to the distinguished Senator from Pennsylvania that you had proceeded in some cases, and I did not know of any in which you had ever proceeded. Therefore, I wanted the record to show if it is a fact that you had not proceeded in any of them.

I do not want you to say you don't know if you do not know, but you have your expert with you and he ought to know. You came up to testify on this subject today, did you not?

Mr. BROWNELL. Yes, Senator. I would like to leave it in this way: If I may have your permission, I will file with the committee a list of investigations that we have had during the past 2 years in this area, some of which have resulted in the banks dropping their procedure as a result.

(The following was received for the record:)

List of proposed bank mergers held up or dropped as a result of antitrust investigation:

1. Acquisition by Marine Midland Trust Company of Central New York of the Auburn Trust Company of Auburn, N. Y.: after Department indicated a negative reaction, parties withdrew their request for merger-clearance and and abandoned proposal.
2. Acquisition by Manufacturers & Traders Trust Co. of the Liberty Bank of Buffalo, N. Y.: after Justice Department July 17, 1956, letter to parties indicating antitrust problem, New York superintendent of banks disapproved.
3. Contemplated acquisition by Michigan National Bank of the Peoples Savings Bank of Port Huron, Mich.: Comptroller has held up his approval after being advised by a Department letter of November 23, 1956, this matter is being investigated for antitrust problems.

Senator ROBERTSON. What do you mean there? Prosecutions?

Mr. BROWNELL. I am going to point out that the results of some of these investigations and discussions we have had are that the proposed merger has been dropped, so it was not necessary to go into the courts.

Senator ROBERTSON. I do not think we are particularly interested in some interoffice exchange where you look into this and report back to me with no publicity on it. What we want to know is, has it ever gotten to the point where you made it a public record that you thought something was going on that ought not to go on, and you proceeded criminally against somebody?

Mr. BROWNELL. I do not know of any case where we proceeded criminally against a bank. That is not the way we do it.

Senator ROBERTSON. Neither do I.

Mr. BROWNELL. It would be a civil proceeding.

Senator ROBERTSON. I agree with you if this was a matter of first impression we might say there would not be any great difference between "substantial" and "unduly." But is it not a fact that the courts have taken practically all of the meaning out of the word "substantial" as used in the King's English and in antitrust cases made it mean very little, if any, competition?

Mr. BROWNELL. I would have to respectfully disagree with that conclusion.

Senator ROBERTSON. Then let me read you a decision in which the principal exception to this word "substantial" is known as the "failing corporation" exemption. It is in the case of the *International Shoe Company* v. *the Federal Trade Commission* (260 U. S. 291).

Mr. BROWNELL. I was going to mention it this morning.

Senator ROBERTSON. The Court stated there:

> Where the corporation acquired is a corporation with resources so depleted and the prospect of rehabilitation so remote that it faced the grave probability of business failure * * * we hold that the purchase of its capital stock by a competitor (there being no other prospective purchaser), not with a purpose to lessen competition, but to facilitate the accumulated business of the purchaser and with the effect of mitigating seriously injurious consequences otherwise probable * * * does not substantially lessen competition or restrain commerce within the intent of the Clayton Act.

It says, "does not substantially." Long before the Federal Deposit Insurance Corporation was in charge of it. That is the difference I am trying to point out here. Your test "substantially" would not inhibit it as far as the banks are concerned, because the courts have taken all of the meaning out of the ordinary usage of the word. That is why we put a different word in here, "unduly," which would mean, I think—and I was not here at that time, but what I would have thought if I was here—what substantial means.

If I get a substantial contribution to my campaign I would not call it $1 or $5, you see.

Mr. BROWNELL. I am not sure I follow that analogy.

Senator CLARK. It is quite impossible to get an undue contribution.

Mr. BROWNELL. We think the interpretation of "substantial lessening of competition" is a very sound one. And we think it should be taken into consideration in bank mergers also.

Senator ROBERTSON. I mentioned it because last year you expressed the same viewpoint, and our committee, as I pointed out, did not agree with you.

Senator DOUGLAS. May I say one member of the committee agreed with him.

Senator ROBERTSON. There is always opportunity for difference of opinion on this committee.

You may proceed.

Mr. BROWNELL. All right. Just to get back on the main line of thought here while the relevant language of the Clayton Act, section 7, has been on the books for almost half a century, this proposed phrase of "unduly" in section 23 is new.

For example, Chairman Martin stated:

> We recognize * * * that you have a legal groundwork for substantially lessening competition already in the framework of the law and that it may not be possible to use unduly lessening competition.

In support of this novel and weaker standard, which I repeat, is but one of a number of factors to be considered, the Comptroller of the Currency has stated:

* * * That even though a sizable and even substantial reduction in competition were to be involved, the office of the Comptroller of the Currency would favor and approve consolidations, mergers, and purchases involving the absorption by strong banks of weak banks or those facing imminent or ultimate failure because of important asset of unsolvable management weaknesses, lack of an adequate banking field as reflected by their earnings, usually located in overbanked cities or areas or in communities too small to support a banking institution.

This gives me an opportunity to present my views on this point.

Contrary to the Comptroller's apparent understanding, however, upholding such acquisitions need not require abandoning section 7 standards. For situations he specifies apparently could fall within the so-called failing corporation exemption, as exemption firmly embedded in section 7. As the House committee reporting on amended section 7 put it:

The argument that a corporation in bankrupt or failing condition might not be allowed to sell to a competitor has already been disposed of by the courts. It is well settled that the Clayton Act does not apply in bankruptcy or receivership cases. In the case of *International Shoe Company* v. *The Federal Trade Commission* (260 U. S. 291) (the House report continues) the Supreme Court went much further.

The Court there reasoned that where the corporation acquired is:

* * * a corporation with resources so depleted and the prospect of rehabilitation so remote that it faced the grave probability of business failure * * * we hold that the purchase of its capital stock by a competitor (there being no other prospective purchaser), not with a purpose to lessen competition, but to facilitate the accumulated business of the purchaser and with the effect of mitigating seriously injurious consequencies otherwise probable * * * does not substantially lessen competition or restrain commerce within the intent of the Clayton Act.

Likewise adopting this exception, the Senate committee report deemed this proviso would come into play when the acquired corporation is "heading in (the) direction" of bankruptcy.

Further indicating the absence of need for standards different from section 7 is this Department's view of the International Shoe exception, which the chairman has mentioned. Thus we have not prosecuted mergers where, because of either inadequate management, obsolete equipment, or a failing market, the acquired corporation's prospects for survival seemed dim. Gaging the likelihood of future business success, of course, may involve different factors in different industries. And, considering bank mergers, let me assure you, the Department of Justice would without doubt pay heed to each banking agency's judgment of a bank's chances to prosper. This anticipated pattern of sections 7's enforcement against bank asset acquisitions should go a long way toward meeting the problem of "failing" banks some banking agencies have raised.

Even more basically, however, I would argue against the wisdom of tailoring section 7's strictures to the assertedly unique needs of the banking industry. In the more than 60 years since the Sherman Act's passage no one has suggested its provisions did not apply to banks as well as to all other sections of American business. Similarly, in the Transamerica case never was it urged that unamended section 7 did not apply with equal force to both banks and nonbanking corporations. And finally, in its 1950 amendment to section 7, Congress

Senator ROBERTSON. I agree with you if this was a matter of first impression we might say there would not be any great difference between "substantial" and "unduly." But is it not a fact that the courts have taken practically all of the meaning out of the word "substantial" as used in the King's English and in antitrust cases made it mean very little, if any, competition?

Mr. BROWNELL. I would have to respectfully disagree with that conclusion.

Senator ROBERTSON. Then let me read you a decision in which the principal exception to this word "substantial" is known as the "failing corporation" exemption. It is in the case of the *International Shoe Company* v. *the Federal Trade Commission* (260 U. S. 291).

Mr. BROWNELL. I was going to mention it this morning.

Senator ROBERTSON. The Court stated there:

> Where the corporation acquired is a corporation with resources so depleted and the prospect of rehabilitation so remote that it faced the grave probability of business failure * * * we hold that the purchase of its capital stock by a competitor (there being no other prospective purchaser), not with a purpose to lessen competition, but to facilitate the accumulated business of the purchaser and with the effect of mitigating seriously injurious consequences otherwise probable * * * does not substantially lessen competition or restrain commerce within the intent of the Clayton Act.

It says, "does not substantially." Long before the Federal Deposit Insurance Corporation was in charge of it. That is the difference I am trying to point out here. Your test "substantially" would not inhibit it as far as the banks are concerned, because the courts have taken all of the meaning out of the ordinary usage of the word. That is why we put a different word in here, "unduly," which would mean, I think—and I was not here at that time, but what I would have thought if I was here—what substantial means.

If I get a substantial contribution to my campaign I would not call it $1 or $5, you see.

Mr. BROWNELL. I am not sure I follow that analogy.

Senator CLARK. It is quite impossible to get an undue contribution.

Mr. BROWNELL. We think the interpretation of "substantial lessening of competition" is a very sound one. And we think it should be taken into consideration in bank mergers also.

Senator ROBERTSON. I mentioned it because last year you expressed the same viewpoint, and our committee, as I pointed out, did not agree with you.

Senator DOUGLAS. May I say one member of the committee agreed with him.

Senator ROBERTSON. There is always opportunity for difference of opinion on this committee.

You may proceed.

Mr. BROWNELL. All right. Just to get back on the main line of thought here while the relevant language of the Clayton Act, section 7, has been on the books for almost half a century, this proposed phrase of "unduly" in section 23 is new.

For example, Chairman Martin stated:

> We recognize * * * that you have a legal groundwork for substantially lessening competition already in the framework of the law and that it may not be possible to use unduly lessening competition.

In support of this novel and weaker standard, which I repeat, is but one of a number of factors to be considered, the Comptroller of the Currency has stated:

* * * That even though a sizable and even substantial reduction in competition were to be involved, the office of the Comptroller of the Currency would favor and approve consolidations, mergers, and purchases involving the absorption by strong banks of weak banks or those facing imminent or ultimate failure because of important asset of unsolvable management weaknesses, lack of an adequate banking field as reflected by their earnings, usually located in overbanked cities or areas or in communities too small to support a banking institution.

This gives me an opportunity to present my views on this point.

Contrary to the Comptroller's apparent understanding, however, upholding such acquisitions need not require abandoning section 7 standards. For situations he specifies apparently could fall within the so-called failing corporation exemption, as exemption firmly embedded in section 7. As the House committee reporting on amended section 7 put it:

The argument that a corporation in bankrupt or failing condition might not be allowed to sell to a competitor has already been disposed of by the courts. It is well settled that the Clayton Act does not apply in bankruptcy or receivership cases. In the case of *International Shoe Company* v. *The Federal Trade Commission* (280 U. S. 291) (the House report continues) the Supreme Court went much further.

The Court there reasoned that where the corporation acquired is:

* * * a corporation with resources so depleted and the prospect of rehabilitation so remote that it faced the grave probability of business failure * * * we hold that the purchase of its capital stock by a competitor (there being no other prospective purchaser), not with a purpose to lessen competition, but to facilitate the accumulated business of the purchaser and with the effect of mitigating seriously injurious consequencies otherwise probable * * * does not substantially lessen competition or restrain commerce within the intent of the Clayton Act.

Likewise adopting this exception, the Senate committee report deemed this proviso would come into play when the acquired corporation is "heading in (the) direction" of bankruptcy.

Further indicating the absence of need for standards different from section 7 is this Department's view of the International Shoe exception, which the chairman has mentioned. Thus we have not prosecuted mergers where, because of either inadequate management, obsolete equipment, or a failing market, the acquired corporation's prospects for survival seemed dim. Gaging the likelihood of future business success, of course, may involve different factors in different industries. And, considering bank mergers, let me assure you, the Department of Justice would without doubt pay heed to each banking agency's judgment of a bank's chances to prosper. This anticipated pattern of sections 7's enforcement against bank asset acquisitions should go a long way toward meeting the problem of "failing" banks some banking agencies have raised.

Even more basically, however, I would argue against the wisdom of tailoring section 7's strictures to the assertedly unique needs of the banking industry. In the more than 60 years since the Sherman Act's passage no one has suggested its provisions did not apply to banks as well as to all other sections of American business. Similarly, in the Transamerica case never was it urged that unamended section 7 did not apply with equal force to both banks and nonbanking corporations. And finally, in its 1950 amendment to section 7, Congress reiterated prohibitions on stock acquisitions to fit banks the same as all other corporations. So it seems to me, at least, against this background, I suggest that Congress move most slowly in creating or encouraging special antitrust treatment for banks.

Beyond equitable coverage is the problem of insuring uniform antitrust device.

This is the point I mentioned a moment ago, Senator Clark. Proposed section 23 in the committee print, you will recall, provides merely that the appropriate agency, if it desires "may * * * request the opinion of the Attorney General." The banking agency is not obliged to do so. This despite the fact that the Attorney General's advice would treat issues which, in the language of the Chairman of the Federal Reserve Board's testimony before the Senate Antitrust Subcommittee, "are of a character quite different from the functions normally exercised by the Board," and, again in his phrasing, involves "different spheres of Government operation." To the same effect, Comptroller Gidney has stated:

> I have not any competency in that (the antitrust) field. I do not know what the courts have done.

From this I conclude that proposed section 23 fails completely to insure informed advice on competitive factors in bank mergers.

Failure to insure informed advice on competitive factors could have effects far beyond the banking field. Without the right in the Department of Justice to intervene in bank mergers there might be as many different views of section 7's standards and scope as there were agencies charged with its enforcement. We think the result could well be disparities in view, which in turn spell real enforcement inequities. For enforcement effectiveness as well requires some procedure for this Department's intervention. Otherwise, in our overall responsibility for section 7's enforcement—and I refer here to responsibility entirely outside of the banking area—we would undoubtedly be bound by bank merger precedents we had no voice in picking or shaping.

For all these reasons, then, this Department feels section 23 in its present form has some real dangers and, therefore, we would like to go on record as opposing it in this present phraseology.

Instead, this Department favors simply amendment of Clayton Act section 7 to cover bank asset, as it now does bank stock, acquisitions.

In this connection, I might call attention to a statement made on behalf of the American Bar Association last year before the Senate Antitrust Subcommittee.

Senator ROBERTSON. If I may interrupt.

Mr. BROWNELL. Surely.

Senator ROBERTSON. The antitrust laws are under the jurisdiction of the Judiciary Committees.

Mr. BROWNELL. That is correct.

Senator ROBERTSON. You would not recommend we get into a row with them over jurisdiction, would you?

Mr. BROWNELL. No; I would not, but as I come to my third point here, we are going to ask you to take some note of this point——

Senator ROBERTSON. I read about the meeting on Friday and Saturday before the Judiciary Committee, and I formed the impression that that was not a good committee to get into a row with.

Mr. BROWNELL. I disagree with you, sir. I enjoyed it very much.

Senator ROBERTSON. That is fine.

Mr. BROWNELL. In fact it is considered part of our responsibilities to present our views, insofar as it affects the Department of Justice, to the appropriate committees, and we believe it is a part of the work we have to do in the Department.

What we are asking for here in our third point, which I will come to shortly, is action by this committee which would fit in with the action of the Judiciary Committees and prevent a clash there, which seems to us entirely unnecessary in the enforcement of banking and antitrust laws. It is one of those related matters that really deserves the attention of both committees. That is why we appreciate very much the opportunity to present our views here as well as to the Judiciary Committees.

The American Bar Association statement continues:

* * * the American Bar Association favors and recommends enactment of the proposal to embrace asset acquisitions by banks within the coverage of section 7. We believe that the law governing bank purchases of assets should conform to that which has controlled bank purchases of stock. The application of section 7 to bank mergers should not turn on the distinction between acquiring stock and acquiring assets.

Even more broadly, I suggest, such amendment of Clayton Act section 7 seems required by our basic belief in uniform application of our Nation's laws to all groups alike. In our more than half-century of Federal antitrust history, competition in banking has been deemed as important as in any other section of our economy. I would like to say that I see no reason for departing from that view now.

Senator ROBERTSON. The clerk calls my attention to the fact that the law section of the American Bar Association, acted on this without consulting the banking section, and the banking section is now considering reversing the law section, and we will shortly have their opinion.

Mr. BROWNELL. Good. Well, it emphasizes very clearly the point I am trying to make, that here is the place where problems of the antitrust laws come in touch with the laws relating to banks. It is going to take joint action and cooperative action, it seems to me, between the two committees, just as it would under our proposal take cooperative action between the Department of Justice and the banking agencies to work it out to the satisfaction of all.

If we leave it to one or the other I think we may miss some important part of the whole picture. With these preliminary remarks I would like to come to my third and final point which is to present a suggestion to you for your careful consideration that may lead to an accommodation of the two views, that is, the views as to the antitrust enforcement generally, and the views as to how the bank mergers and acquisitions should be handled. If this committee and the Congress should conclude bank consolidations should, at first at least, be treated under the FDIC Act, then I would suggest adoption of standards and procedures roughly paralleling those adopted last year, and reiterated in the pending committee print, controlling formation of, and acquisitions by, bank holding companies.

Briefly put, the Bank Holding Company Act, and this committee print, have the effect that the Federal Reserve Board, passing on any proposed bank holding company merger, will consider, among other factors, the standards of Clayton Act, section 7.

Senator ROBERTSON. May I interrupt to ask a question?

Mr. BROWNELL. Surely.

Senator ROBERTSON. At the bottom of page 9 you state—

> * * * the Department of Justice favors treatment of bank mergers, like other mergers, under Clayton Act, section 7 * * *

Mr. BROWNELL. Yes.

Senator ROBERTSON. Are all the rest of your suggestions based upon our acceptance of that thesis that we must proceed under the Clayton Act and, therefore, put it in the Department of Justice, or are your further suggestions in line with or do they have anything to do with the proposal in the committee print that these agencies that deal exclusively with banking should also deal with bank mergers? It is not clear to me whether you are carrying forward into this a thesis that it must be section 7 of the Clayton Act, without change, when you said you already have power under the Sherman Act which you never used.

Mr. BROWNELL. Yes, we have used it, Senator. I would like to file with the committee, if I may, the actions taken by the Justice Department in bank cases under the Sherman Act.

(The following was received for the record:)

FOUR COMPLAINTS UNDER SHERMAN ACT IN WHICH BANKS HAVE BEEN NAMED AS DEFENDANTS

District court, southern district of New York: *United States of America, plaintiff* v. *Henry S. Morgan et al. and the Investment Bankers Association of America, defendants.*

District court, southern district of New York: *United States of America* v. *The Mortgage Conference of New York et al.*

District court, district of Minnesota: *United States of America, plaintiff* v. *Investors Diversified Services et al., defendants.*

District court, northern district of Illinois, eastern division: *United States of America, plaintiff* v. *Chicago Mortgage Bankers Association et al., defendants.*

Senator ROBERTSON. You have used it in bank merger cases?

Mr. BROWNELL. No. Of course not.

Senator ROBERTSON. That is all we are dealing with.

Mr. BROWNELL. In the bank merger cases, to repeat what I tried to say a few moments ago, we have conducted a number of investigations. These were not secret investigations, but they were regular investigations with an eye to action under the antitrust laws. As a result of the conferences that we had with the banks involved in a number of cases that I remember, the proposed merger or acquisition was dropped without the necessity of litigation. So, in a way, you might say it is just as effective, or more effective, than enforcement of antitrust laws which have to go to litigation.

Senator ROBERTSON. Let me understand what you want us to do. You want to have jurisdiction under the Clayton Act and, if you get that, you do not object too much if we put in a parallel jurisdiction for the banking agencies of the Government. They both have jurisdiction and then we will see who gets there first. Is that the idea?

Mr. BROWNELL. No. I think not. If I may continue to outline this suggestion I think you will see 1 or 2 differences there that are fairly important.

Senator ROBERTSON. Very well. You may proceed.

Mr. BROWNELL. The specific proposition I would like to put up to the committee is this: If you in the Congress conclude that bank consolidations, at least in the beginning, should be treated under the FDIC Act rather than in the Clayton Act, then I would suggest adoption of standards and procedures roughly paralleling those adopted last year, and reiterated in the pending committee print, controlling formation of, and acquisitions by, bank holding companies.

(1) Briefly put, the Bank Holding Company Act, and this committee print, have the effect that the Federal Reserve Board, passing on any proposed bank holding company merger, will consider, among other factors, the standards of Clayton Act section 7. We have, in other words, an exact analogy in the law which this committee passed in the past. As the Vice Chairman of the Federal Reserve Board wrote on January 18, 1957:

> Section 3 (c) of the Bank Holding Company Act requires the Board, in passing upon each application by a bank holding company for approval of its acquisition of bank stock, to consider certain specific factors, including whether or not the effect of the proposed acquisition would be to expand the size or extent of the holding company system beyond limits consistent with the public interest and the preservation of competition in the field of banking. The concept involved in this factor is a broad one, and in the Board's opinion adequate consideration of the facts in this regard necessarily involves consideration of the standards mentioned in section 7 of the Clayton Act—that is, whether in any line of commerce in any section of the country the effect of such acquisition might be substantially to lessen competition or to tend to create a monopoly.

As a result, the Vice Chairman of the Federal Reserve Board concluded:

> You may be assured that the Board in consideration of (holding company mergers) will take into account * * * whether the proposed transactions might involve a violation of section 7 of the Clayton Act or other statutes.

Senator ROBERTSON. Is there a single word in the Bank Holding Company Act about the Clayton Act?

Mr. BROWNELL. This is the interpretation of it.

Senator ROBERTSON. That is something else. But I have had to write that on 4 or 5 different occasions, and if there was any reference in there to the Clayton Act I was certainly asleep when it went in because I did not think we had any specific reference to section 7 of the Clayton Act in the Bank Holding Company Act. We did write what we thought was a proper test in there.

Mr. BROWNELL. That is why I considered it important this morning to——

Senator ROBERTSON. You are asking us to change this bill to include that part of the test, and are you still advocating we put section 7 of the Clayton Act into our law?

Mr. BROWNELL. Only to include what you have for the bank holding companies. That is why I considered it so important this morning to present to you the way in which the Federal Reserve Board officials have interpreted the Bank Holding Company Act, because they interpreted it to incorporate the section 7 standards. That is exactly what we are asking for in this proposal that you should do for the banking institutions other than the bank holding companies.

Senator ROBERTSON. Of course, we are going to get the language with it, and we are going to put it in the record so we can see what it is.

We do have a present illustration, though, that the Federal Reserve Board made one ruling on what is the payment of interest on checking accounts, and the Federal Deposit Insurance Corporation made another one. The Federal Reserve Board made one interpretation of this language and I do not know whether the Federal Deposit Insurance Corporation did feel at liberty to make another one and the Comptroller another one, but those are the things we have to consider now. I will read the language.

Here is all we have to consider:

Financial history and condition of the company or companies or banks concerned.

Two is prospects. Three is the degree of management. Four is the convenience, needs, and welfare of the communities in the area concerned. Five—and this is the one you were speaking of—where the effect of such acquisition or merger or consolidation would be to expand the size or extent of the bank holding company system involved beyond the limits consistent with adequate and sound banking, the public interest, and the preservation of competition in the field of banking.

Mr. BROWNELL. Exactly right.

Now, the Vice Chairman of the Federal Reserve Board has interpreted your language and they have told us and told you how they interpreted it. The administrative interpretation is the thing I want to get across.

Senator ROBERTSON. But we cannot write some language and see the interpretation. That is what we mean this law to be. Do you want us to put in here "preservation of competition in the field of banking"?

Mr. BROWNELL. We would be satisfied to have exactly the same language apply to banks as now applies to the bank holding companies.

Senator ROBERTSON. All the way through there?

Mr. BROWNELL. Yes.

Senator ROBERTSON. You want all of that?

Mr. BROWNELL. Yes. Because the interpretation that is given by the Federal Reserve Board seems to us entirely the correct one. That, I think, I had better repeat, because I may not have made that clear.

This is what the statement says as to what that language means:

> The concept involved in this factor is a broad one, and in the Board's opinion adequate consideration of the facts in this regard necessarily involves consideration of the standards mentioned in section 7 of the Clayton Act—that is, whether in any line of commerce in any section of the country the effect of such acquisition might be substantially to lessen competition or to tend to creat a monopoly.

As a result, the Vice Chairman of the Federal Reserve Board concludes:

> You may be assured that the Board in consideration of * * * (holding company mergers) will take into account * * * whether the proposed transactions might involve a violation of section 7 of the Clayton Act or other statutes.

Senator ROBERTSON. That is sort of a prejudgment of how they are going to rule when it comes to them. It is a moot case, so to speak.

What will you do if this comes up? Here is what we propose to do. To begin with, in this new law they had no precedent and they were seeking to establish it, and it has not come to me that there is any case where they have misconstrued the law.

You may proceed.

Mr. BROWNELL. I will continue now.

From this it seems to us clear that the standard in section 7 of the Clayton Act, under present law as well as the pending proposal, must be considered by the Board in passing on formations of, or acquisitions by, bank holding companies. The chairman says that that has not yet been tested in the courts, but it is their interpretation that they are the administrative agency, and we believe it is the correct one. To the best of my knowledge, no banking agency official has challenged or even disagreed with consideration of section 7's competitive tests in the holding company context.

In light of this history, amendment of section 23, the one we are talking about, to require that section 7's standard—not the pending proposal's novel "unduly" phrasing—be considered, along with other factors, by appropriate banking agencies in passing on bank mergers should raise small issue.

(2) Beyond the issue of competitive standards, section 23 of the pending print, second, should be revised to specify for all bank mergers the same procedures for cooperative liaison, advice, and intervention this Department and the Federal Reserve Board have evolved for bank holding company mergers. Now, how does it work under the bank holding provision, the present law? As you know, the Federal Reserve Board is presently considering the first application for approval of a bank holding company merger under the 1956 act. To highlight the sort of mutually advantageous cooperation, between the Board and the Department of Justice, a procedure has been evolved, and let me review briefly the path that each agency has pursued in consideration of this proposed bank holding company merger.

Initially, after the Department of Justice had written to the Federal Reserve Board indicating knowledge of the proposed holding company's formation, the Board on November 29, 1956, replied that—

> * * * we will be pleased to advise you [of any hearing] and notice of the hearing will be published in the Federal Register.

And then the Department of Justice responded, on December 11, 1956:

> We appreciate your advice that, should the Board of Governors determine to hold a hearing on this matter, you will give us notice. In the event the Board determines not to hold a hearing, we would also appreciate being advised in advance of the Board's ultimate decision to approve or disapprove the application.
>
> As you know—

this Department's letter went on to emphasize—

> our responsibilities under the antitrust laws require us to remain conversant with this matter. It would be helpful, therefore, and might avoid a duplication of work by two different agencies on the same matter, if you would be able to furnish us with any basic competitive information you may have collected or compiled relating to these banks * * *.

Finally, after this Department has kept the Board abreast of the path of our antitrust investigation and of the possibility of some Justice Department participation in the Board hearing, the Board then replied on January 18, 1957:

> We will be very glad to have you submit a statement or file a brief at the appropriate time if you decide to do so. In the meantime, the Board or its staff will be glad to be of any assistance it can to the Department in connection with any aspects of this matter.

So much for this brief narration of dealings between this Department and the Federal Reserve Board of how we are getting along with this first test of the bank holding company provisions; in other words, in the course of a consolidation under the Bank Holding Company Act. But I would say that, more broadly than this, the bit of history that I have outlined here suggests appropriate roles for the Department of Justice and each banking agency in consideration of, not only holding company, but all bank mergers. And so we suggest that section 23 should be amended, therefore, specifically to require notice to the Attorney General and to enable him to intervene, or at least offer his views, to the banking agency considering any bank merger.

(3) Finally, beyond competitive standards and questions of intervention, section 23 should be amended, again paralleling Bank Holding Company Act provisions, to include some antitrust savings clause. You will remember that the Bank Holding Company Act and this pending committee print which is before you contains this provision:

> Nothing herein contained shall be interpreted or construed as approving any act, action or conduct which is or has been or may be in violation of existing law, nor shall anything herein contained constitute a defense to any action, suit or proceeding pending or hereafter instituted on account of any prohibited antitrust or monopolistic act, action or conduct.

Now, we believe that this savings clause should apply to all bank mergers as it now does to formation of, or acquisition by, bank holding companies. Such application would carry out the proposal that was advanced by the Federal Reserve Board Chairman that:

> The Attorney General * * * would continue to have full authority to institute proceedings under the Clayton Act, if he should deem it desirable, with respect to any situation resulting from the particular merger or consolidation" (statement by Federal Reserve Board Chairman Martin, explaining the Board's proposal for handling bank mergers, p. 691 of Hearings of Senate Antitrust and Monopoly Subcommittee, To Study the Antitrust Laws of the United States, and their Adiministration, Interpretation and Effect Pursuant to S. Res. 61 (84th Cong., 1st sess.)).

Accordingly, I would suggest that this committee write into the pending section 23 the same antitrust savings clause that is contained in the bank holding company provisions—reiterated in title II, chapter 9, section 61 of the pending committee print. As a corollary, of course, since the savings clause refers to "existing law," this committee should make clear its support of amendment to section 7 which would cover bank assets as well as stock acquisitions, for only in this way would the antitrust savings clause have real meaning.

Senator ROBERTSON. That brings us back to section 7 of the Clayton Act, does it not?

Mr. BROWNELL. Yes.

Senator ROBERTSON. That is what I thought.

Mr. BROWNELL. And if you could express the views of this committee informally, I am sure it would be of great help to the Judiciary Committees.

Senator ROBERTSON. We have enjoyed hearing you discuss this problem and giving the opportunity for other members to ask questions. But before he releases this to others, the chairman wants to mention the fact that we are dealing with a banking act that dates back to, oh, I imagine 1863—that was 93 years ago and dealing with the

Federal Reserve Act that dates back to 1913. Both of those acts have on numerous occasions been amended, and some of them, of course, have accumulated obsolete provisions that applied at the time but no longer apply and have not been used for years.

You know, of course, I was a practicing lawyer before you took charge of the Department of Justice. But there has never been any codification of those laws. Do you approve of the plan of this committee to codify them?

Mr. BROWNELL. Yes.

Senator ROBERTSON. Then our objective meets with your approval?

Mr. BROWNELL. That is correct.

Senator ROBERTSON. And endorsement?

Mr. BROWNELL. Yes.

Senator ROBERTSON. You would like to see Congress complete action on a bill?

Mr. BROWNELL. That is correct.

Senator ROBERTSON. And of all the provisions in 253 pages of it you just this morning referred to one slight matter and turned your attention to the error with respect to bank mergers?

Mr. BROWNELL. Well, it is not an error. In my mind it is not a slight matter. To us, some of the most important work that we have to do in the Department of Justice is in this antitrust area, and we believe that this proposal we have made here this morning will not only aid us tremendously but will tie in together in a cooperative way the banking laws and the antitrust laws. And I believe that would be the objective of this committee.

Senator ROBERTSON. As the Chairman sees it, about half the suggested amendments to what was in the Bank Holding Act refer back to section 7 of the Clayton Act. That is a difference in approach and philosophy from what the committee took last year and what the Senate took last year. But there is an issue well worth being considered.

Mr. BROWNELL. Well, that is what this committee really did when it came to the Bank Holding Act. You set it up in such a way that the standards of section 7 of the Clayton Act apply, and that is exactly what we are asking for.

Senator ROBERTSON. We used language which the Federal Reserve Board—and it did not even have the effect of declaratory judgment, but was in a letter—and we do not know how well it was considered—but in a letter they said that they would apply the interpretation of section 7.

Mr. BROWNELL. Of course, if you prefer to put it in writing in the statute, it would be equally agreeable to us.

Senator ROBERTSON. That was not the only decision that could have been reached on that language. Certainly, as the Chairman pointed out, there was no specific reference in the bank holding bill.

Mr. BROWNELL. Yes.

Senator ROBERTSON. We have no jurisdiction of antitrust legislation as regards amending any existing law.

The Chair recognizes now one of his colleagues. Do you wish to be recognized, Senator Bricker?

Senator BRICKER. I think it is within the jurisdiction of this committee if it involves banking in any sense. If banking is a primary responsibility of this committee and this law deals with banking mergers, I think that the question of antitrust laws or section 7, or whatever, of the Clayton Act comes withour our jurisdiction.

Senator ROBERTSON. The Chair qualifies his statement to say we did not have jurisdiction to amend the antitrust laws.

Senator BRICKER. But we could put the section in this bill.

Senator ROBERTSON. As we did, exactly.

On my left, the Senator from Pennsylvania.

Senator CLARK. Mr. Chairman, may I ask the witness a couple of questions?

Senator ROBERTSON. You may, Senator.

Senator CLARK. Mr. Attorney General, do you not have any segment of the banking economy outside of the banking field where there has been an effort to so completely exclude the Justice Department from jurisdiction over the antitrust aspects as is contemplated by this bill?

Mr. BROWNELL. I do not offhand recall any; no. I think that the standard concept that the Congress has always followed is to at least give the Department of Justice the right to intervene and be heard.

Senator CLARK. How about the industry under the jurisdiction of the Interstate Commerce Commission; do they not have substantially greater latitude in that field with respect to antitrust matters than other areas in the economy?

Mr. BROWNELL. Well, in that field and some of the other fully regulated industries, of course, there is a concept that certain antitrust exemptions are allowed. That has never been the concept as far as banking is concerned.

Senator CLARK. Would it not be your view that the real effect of this contemplated language would be to extend such an exemption to the banking field which has never been extended before?

Mr. BROWNELL. It comes perilously close.

Senator CLARK. As I understand it, while you say at the end of your testimony that these suggested revisions would mitigate, if not minimize, the force of your objections to present section 23, I would like to have you state for the record how you would write section 23 if you had your way.

Mr. BROWNELL. Well, I would, my first choice, I think, would be to make it explicit in the language where that section 7 applied.

Senator CLARK. In other words, you would, in effect, write section 7 into section 23 if you had your way?

Mr. BROWNELL. Yes; but if you want to do it by implication, by general language, as was done in the case of the Bank Holding Company Act, I would have no serious objection to that as long as the legislative history made clear that the Reserve Board's construction was intended.

Senator CLARK. Being a reasonable man, you are prepared to compromise.

Now, Mr. Attorney General, one final question. Is it possible to make a good legal case, in your judgment, for excluding the acquisition of bank assets from the provisions of section 7?

Mr. BROWNELL. I could never see any reason for that.

Senator CLARK. It is just a loophole, is it not?

Mr. BROWNELL. That is a loophole.

Senator CLARK. Thank you, sir.

Senator ROBERTSON. Any further questions?

Excuse me. Is it a fair summary that your first desire is to amend section 7 and, if that is done, we can do what we please on the rest of this?

Mr. BROWNELL. As long as we have the authority, I do not care where it appears.

Senator ROBERTSON. Thank you.

Now the Chair recognizes the Senator from Illinois.

Senator DOUGLAS. Mr. Brownell, when the same proposal was up before us last year I gathered some figures from the records of the Comptroller of the Currency on approving and disapproving mergers since 1950. My figure showed that there were 6 years, from 1950 to 1955, inclusive, in which he had approved 460 mergers, had formally disapproved 9, had informally disapproved 13; therefore, he had approved between 96 and 98 percent of all mergers during those 6 years.

Could you tell me if these figures which I collected are approximately accurate, according to your knowledge?

Mr. BROWNELL. Yes; they are. And I am not so sure that the 22 that were turned down were turned down on the ground of competitive factors.

Senator DOUGLAS. Oh, that is very interesting. You think they were turned down on other reasons, perhaps?

Mr. BROWNELL. We are not sure about that, but I think it would bear investigation.

Senator DOUGLAS. Have you made certain investigations?

Mr. BROWNELL. In the sense that if somebody was interested in a study of exact percentages that that factor would have to be examined into. But I think that the general figures are themselves conclusive enough to indicate that a stricter competitive standard should be applied.

Senator DOUGLAS. In other words, up to date the Comptroller of the Currency has tended to give little or no weight to the question as to whether or not competition would be substantially less?

Mr. BROWNELL. I believe that is a fact. And I think his own testimony indicates that.

Senator DOUGLAS. Yes, sir.

Mr. ROGERS. May I clarify for the record the Comptroller does not have authority under the law to consider competitive factors, so he does not turn it down for that reason.

Senator CLARK. I could not hear you.

Mr. ROGERS. I said the Comptroller does not have authority under the law to consider competitive factors. He could not turn it down officially on that basis.

Mr. BROWNELL. It was my understanding that he testified, however, that he did consider competitive factors, although it was not explicit in the language of the law.

Mr. ROGERS. He said they did not consider it. But it is not in the law.

Senator DOUGLAS. Yes, but is not the Attorney General correct that the Comptroller stated that that factor was taken into consideration?

Mr. ROGERS. I believe the Comptroller so testified.

Senator DOUGLAS. Mr. Attorney General, do you know what the record has been for 1956? These figures which I collected merely went through 1955.

Mr. BROWNELL. We do not have the 1956 figures.

Senator DOUGLAS. I notice the very able Deputy Comptroller is here. I wonder if he could give us information on this point?

Senator ROBERTSON. The Chair recognizes Mr. Jennings if he wishes to answer the question.

Mr. JENNINGS. The number of bank mergers approved by the Comptroller during 1956 numbered 105. Through the first 6 months of 1956, State superintendents approved about 54.

Senator DOUGLAS. How many were disapproved?

Mr. JENNINGS. I do not have those figures in my mind. I do not know for the State banking departments.

Senator DOUGLAS. How many were disapproved by the Comptroller?

Mr. JENNINGS. I would say 3 or 4.

Senator DOUGLAS. So that the percentage of 96 to 98 percent approvals still seems to be good for 1956 as well as the 6 preceding years?

Mr. JENNINGS. I believe that percentage would hold about true.

Senator DOUGLAS. Thank you.

Now may I ask the Attorney General a further question: You are apparently saying or urging that it be mandatory that the regulatory agencies consult with the Attorney General before they act upon whether or not a request for merger be approved, is that correct?

Mr. BROWNELL. We do not care about the consultation, as long as we have the right to intervene and be heard.

Senator DOUGLAS. Would you say that a joint approval by the Attorney General, as well as by the regulatory agency, would be desirable?

Mr. BROWNELL. My governmental experience would indicate to me that probably the one agency should have the final say.

Senator DOUGLAS. So you are not asking for joint approval?

Mr. BROWNELL. That is correct.

Senator DOUGLAS. You are merely asking to be heard or be given the right——

Mr. BROWNELL. Given our day in court, so to speak.

Senator DOUGLAS. That would require prior notification to you as well as the regulatory agency?

Mr. BROWNELL. That is right. And that is the end procedure we worked out in this instance under the bank holding company provisions.

Senator DOUGLAS. In the amendment that Senator Lehman and I introduced to the bank merger bill of last year, we wanted to clear up the possibility of confusion as to whether merger would be permitted in those cases where there was danger of failure, and we proposed that the ruling of the court in the International Shoe case be made explicit in the statute, so that even if a merger was designed to prevent probable failure it would be justified, even though it might substantially lessen competition. Would you approve of such an amendment?

Mr. BROWNELL. My offhand opinion, Senator, would be it would be better to leave that to the courts to interpret the matter case by case as they have in the past, you might miss 1 or 2 factual situations by explicit statutory statement of the failing corporation rule.

Senator DOUGLAS. I believe it is the view of some of my colleagues that if we merely use the "substantially lessen competition" test that you might strike some small city, for example, with 2 banks, 1 that was on the point of failure; and if there the "substantially lessen competition" test is paramount, then merger could be prohibited, even if it might be in the interest of the community that the weaker bank be saved from insolvency.

Mr. BROWNELL. I think there are two pretty clear answers to that fear. One is that the "failing corporation" test is so well established in the court decisions that it seems quite clear that that alone would take care of it; the other is that under our proposal, these additional, orthodox banking factors would also be taken into consideration by the banking agency in making its initial decision. So that those would be other and additional factors than the antitrust provisions, and I believe in those you would find enough to come to a just result. Of course, antitrust safeguards would, in any event be preserved by inclusion of a savings clause.

Senator DOUGLAS. In other words, what you are saying is that the test as to whether or not it would "substantially lessen competition" would not be the sole test?

Mr. BROWNELL. Not the sole test, initially.

Senator DOUGLAS. I want to congratulate you, Mr. Brownell, on your testimony. I have not always agreed with you on various stands that you have taken on public issues, but I think in the last 2 days in your testimony, both before the Judiciary Committee and this committee, you are getting back on the rails.

Senator ROBERTSON. Any further questions? If not, we want to thank you, sir, and I want to repeat the information which I think has already been given to you; we face a deadline on these hearings. The transcript of your testimony will be furnished to you this afternoon, and we hope that if you do not have time to go over it, that your assistant who is here and heard you testify will be authorized to go over it and get that record back to us this afternoon, so that these last hearings—and we have just one more agency coming down—can go to the printer and we will get the hearings the latter part of this week.

We thank you very much.

Mr. BROWNELL. Thank you very much, Mr. Chairman.

(The Attorney General's prepared statement follows:)

STATEMENT BY ATTORNEY GENERAL HERBERT BROWNELL JR.

I appear today at the invitation of your chairman to present the Justice Department's views on certain legal aspects of the pending committee print "to amend and revise the statutes governing financial institutions and credit." The great bulk of this bill treats matters beyond this Department's direct concern. Only a few of its provisions cover problems on which we might helpfully comment. Of these, I plan today to focus primarily on section 23, chapter 5, of title 3, covering bank mergers and consolidations.

That provision would, first, require premerger consent to most banking mergers by the appropriate banking agencies. "In granting or withholding consent," that proposal specifies, "the appropriate agency shall also take into consideration whether the effect thereof may be to lessen competition unduly or to tend unduly to create a monopoly." Finally, according to proposed section 23, "the appropriate agency may also"—and let me emphasize the word "may"—"request the opinion of the Attorney General with respect to such question."

Treating this provision, my plan is, first, to emphasize need for more effective curbs on certain bank mergers, a need recognized by the President of the United States, this Department, and interested banking agencies alike, but which we believe is not adequately met in this bill. Second, I propose to show why, in our opinion, proposed section 23 runs afoul of basic, governmentwide, principles of comity between prosecuting and supervisory agencies. Third, to meet these objections, I shall offer alternatives to presently proposed section 23.

I. First, the need for reasonable curbs on bank mergers. This need stems from present section 7's failure to cover asset acquisitions by banks, as distinguished from stock acquisitions. The section provides, as to stock acquisitions, that it applies to all corporations "engaged in commerce." Section 7's asset acquisition portion, in sharp contrast, covers only corporations "subject to the jurisdiction of the Federal Trade Commission." Further, section 11 of the Clayton Act exempts banks from Federal Trade Commission jurisdiction by specifying that "authority to enforce compliance" with section 7 "is hereby vested * * * in the Federal Reserve Board where applicable to banks, banking associations, and trust companies." On the basis of these provisions the Department of Justice has concluded, and all apparently agree, that asset acquisitions by banks are not covered by section 7 as amended in 1950.[1]

As a result, section 7 is for practical purposes useless to cope with what the Comptroller of the Currency has described as "this recent trend of [bank] mergers, consolidations, and sales."[2] Corroborating the rise in bank mergers, the Chairman of the Board of Governors of the Federal Reserve Board concluded that bank mergers "have gone up steadily."[3] In 1952, his testimony reveals, there were 100 bank mergers. This number jumped to 116 in 1953 and more than doubled to 207 in 1954 and reached 232 by the end of 1955.[4] Most important, the Federal Reserve Board Chairman concluded in mid-1955, this number is "still rising."[5] As a result, the Board Chairman has stated:[6]

"The current trend in bank mergers and consolidations is a matter which deserves careful consideration and one to which the Board of Governors has given a great deal of thought * * *."

This bank merger trend must be viewed against the background of present commercial bank asset concentration. In 9 of 16 of America's principal financial centers, 2 banks owned more than 60 percent of all commercial bank assets. And in each of these 16 centers, the first 2 banks owned more than 40 percent of all commercial bank assets.[7] From these figures, it seems clear, emerges a picture of a steadily increasing bank asset concentration.

It is true that we may still move against this tide of bank mergers to a limited extent under Sherman Act section 1. But mergers may meet Sherman Act standards yet fall before the Clayton Act's more stringent bans. Congress' clear object in its 1950 amendment of section 7 was to strike some mergers beyond the reach of the Sherman Act. Thus the Senate report explains that the "bill is not intended to revert to the Sherman Act test. The intent here * * * is to cope with monopolistic tendencies in their incipiency and well before they have attained such effects as would justify a Sherman Act proceeding."[8]

The report further states that the act's intent is to have "broad application to acquisitions that are economically significant * * * [The] various additions and deletions, some strengthening and others weakening the bill, are not conflicting in purpose or effect. They are merely different steps toward the same objective, namely, that of framing a bill which although dropping portions of the so-called Clayton Act test that have no economic significance, reaches far beyond the Sherman Act."[9]

---

[1] Reaching the same conclusion, a House judiciary subcommittee staff report explained that, because of revisions in amendments to sec. 7, "it became impracticable to include within the scope of the act, corporations other than those subject to regulation by the Federal Trade Commission. Banks, which are placed squarely within the authority of the Federal Reserve Board by sec. 11 of the Clayton Act, are therefore circumscribed insofar as mergers are concerned only by the old provisions of sec. 7 * * *" (staff report to Subcommittee No. 5 of the Committee on the Judiciary, House of Representatives, 82d Cong., 2d sess. (September 1952)).

[2] Hearings on Current Antitrust Problems, before House Antitrust Subcommittee, 84th Cong., 1st sess., May 17, 1955, p. 453.

[3] Hearings on A Study of the Antitrust Laws, before Senate Antitrust Subcommittee, 84th Cong., 1st sess., June 24, 1955, p. 680.

[4] Hearings on Current Antitrust Problems, before House Antitrust Subcommittee, 84th Cong., 1st sess., June 13, 1955, p. 2159. See also Annual Report of Board of Governors, Federal Reserve, for 1955, p. 79.

[5] Hearings on A Study of the Antitrust Laws, before Senate Antitrust Subcommittee, 84th Cong., 1st sess., June 24, 1955, p. 681.

[6] Hearings on A Study of the Antitrust Laws, before Senate Antitrust Subcommittee, 84th Cong., 1st sess., June 24, 1955, p. 681.

[7] Hearings on Current Antitrust Problems, before House Antitrust Subcommittee, 84th Cong., 1st sess., June 8, 1955, p. 1995.

[8] S. Rept. 1775, 81st Cong., 2d sess., pp. 4–5 (1950).

[9] Ibid.

To apply such a competitive standard to bank asset acquisitions, as it now does to bank stock mergers, is our clear aim. And this general broad aim, apart from disagreements over means, is endorsed, in principle, by the President of the United States, the Department of Justice, the Federal Trade Commission, and appropriate banking agencies. Thus the President, in his economic report sent to Congress within the month, has reiterated the need for "extension of Federal regulation to cover bank mergers by asset as well as by stock acquisition." [10] Similarly, Gov. J. L. Robertson of the Board of Governors of the Federal Reserve System stated last session before the House Antitrust Subcommittee considering like legislation: [11] "The Board favors the objective of this legislation." Endorsing this view the Comptroller of the Currency stated before the House Antitrust Subcommittee (subcommittee No. 5): [12]

"We are in accord with the general purpose of H. R. 5948 [amending Clayton Act section 7 to cover bank assets, as it now does bank stock acquisitions]. We have no objection to the principle that the acquisition of one bank by another through purchase, merger, or consolidation should not be permitted if the effect of the acquisition may be substantially to lessen competition. It is no less important to have competition in banking, when this can be done soundly, as it is in other fields of commerce and industry."

In the course of analyzing various differences over methods, this broad agreement on principle should not be obscured.

II. This agreed-upon need for reasonable restraints on bank mergers proposed section 23 fails to meet. The proposed provision, I suggest, is deficient on at least two basic scores. First, it would set up competitive tests for bank mergers different from those that apply to other sections of American business. Second, it might, even beyond the banking area, seriously dissipate enforcement efforts by decentralizing responsibility for decisions affecting Clayton Act, section 7. Both objections, to my view, are rooted in firm principles of equitable and uniform administration of justice.

First, weaker section 7 standards for bank mergers. According to proposed section 23, competitive factors would be only one of numerous considerations to be taken into account by a banking agency in scanning a merger. Beyond that, the competitive considerations specified, whether the acquisition may "lessen competition unduly or to tend unduly to create a monopoly," are completely novel and are intended simply to be less stringent than those specified by Clayton Act section 7 for other American business. As a result, not only does that proposal prescribe pale antitrust standards, but even that lesser standard is only one of many factors banking agencies must consider.

Some banking agencies have realized the difficulties inherent in construing this jerry-built standard. While the relevant language of Clayton Act section 7 has been on the books for almost a half century, proposed section 23's "unduly" phrasing is novel. Recognizing this, Chairman Martin has stated: [13]

"We recognize * * * that you have a legal groundwork for *substantially lessening competition* already in the framework of the law and that it may not be possible to use unduly lessening competition. [Italic added.]

In support of this novel and weaker standard, which, I repeat, is but one of a number of factors to be considered, the Comptroller of the Currency has stated:

"* * * That even though a sizable and even substantial reduction in competition were to be involved, the office of the Comptroller of the Currency would favor and approve consolidations, mergers, and purchases involving the absorption by strong banks of weak banks or those facing imminent or ultimate failure because of important asset or unsolvable management weaknesses, lack of an adequate banking field as reflected by their earnings, usually located in overbanked cities or areas or in communities too small to support a banking institution."

Contrary to the Comptroller's apparent understanding, however, upholding such acquisitions need not require abandoning section 7 standards. For situations he specifies apparently could fall within the so-called failing corporation exemption, an exemption firmly embedded in section 7. As the House committee reporting on amended section 7 put it: [14]

---

[10] Economic Report of the President, January 1957, p. 51.

[11] Hearings before Antitrust Subcommittee (Subcommittee No. 5) of the Committee on the Judiciary, House of Representatives, 84th Cong., 1st sess., on H. R. 5948, p. 50.

[12] Ibid., p. 71.

[13] Hearings on Legislation Affecting Corporate Mergers, before Senate Antitrust Subcommittee, 84th Cong., 2d sess., May 23, 1956, p. 52.

[14] H. Rept. 1191, 81st Cong., 1st sess. (1949), p. 6.

"The argument that a corporation in bankrupt or failing condition might not be allowed to sell to a competitor has already been disposed of by the courts. It is well settled that the Clayton Act does not apply in bankruptcy or receivership cases. In the case of *International Shoe Company* v. *The Federal Trade Commission* (260 U. S. 291) [the House report continues] the Supreme Court went much further."

The Court there reasoned that where the corporation acquired is [15] "a corporation with resources so depleted and the prospect of rehabilitation so remote that it faced the grave probability of business failure * * * we hold that the purchase of its capital stock by a competitor (there being no other prospective purchaser), not with a purpose to lessen competition, but to facilitate the accumulated business of the purchaser and with the effect of mitigating seriously injurious consequences otherwise probable * * * does not substantially lessen competition or restrain commerce within the intent of the Clayton Act."

Likewise adopting this exception, the Senate committee report deemed this proviso would come into play when the acquired corporation is "heading in [the] direction" of bankruptcy.[16]

Further indicating the absence of need for standards different from section 7 is this Department's view of the International Shoe exception. Thus we have not prosecuted mergers where, because of either inadequate management, obsolete equipment, or a failing market, the acquired corporation's prospects for survival seemed dim. Gaging the likelihood of future business success, of course, may involve different factors in different industries. And, considering bank mergers, let me assure you, the Department of Justice would without doubt pay great heed to each banking agency's judgment of a bank's chances to prosper. This anticipated pattern of section 7's enforcement against bank asset acquisitions should go a long way toward meeting the problem of "failing" banks some banking agencies have raised.

Even more basically, however, I would argue against the wisdom of tailoring section 7's strictures to the assertedly unique needs of the banking industry. In the more than 60 years since the Sherman Act's passage no one has suggested its provisions did not apply to banks as to all other sections of American business. Similarly, in the Transamerica case [17] never was it urged that unamended section 7 did not apply with equal force to both banks and nonbanking corporations. And finally, in its 1950 amendment to section 7, Congress reiterated prohibitions on stock acquisitions to fit banks the same as all other corporations. Against this background, I suggest that Congress move most slowly in creating or encouraging special antitrust treatment for banks.

Beyond equitable coverage is the problem of ensuring uniform antitrust advice. Proposed section 23, you will recall, provides merely that the "appropriate agency" if it desires "may * * * request the opinion of the Attorney General." The banking agency is not obliged to do so. This despite the fact that the Attorney General's advice would treat issues which, in the language of the Chairman of the Federal Reserve Board's testimony before the Senate Antitrust Subcommittee, "are of a character quite different from the functions normally exercised by the Board," and, again in his phrasing, involves "different spheres of government operation." [18] To the same effect, Comptroller Gidney has stated: [19]

"I have not any competency in that [the antitrust] field. I do not know what the courts have done."

From this I conclude that proposed section 23 fails completely to insure informed advice on competitive factors in bank mergers.

Failure to insure informed advice on competitive factors could have effects far beyond the banking field. Without this Department's right to intervene in bank mergers that might be as many different views of section 7's standards and scope as there were agencies charged with its enforcement. The result could well be disparities in view, which in turn spell real enforcement inequities. Enforcement effectiveness as well requires some procedure for this Department's intervention. Otherwise, in our overall responsibility for section 7's enforcement—and I refer here to responsibility entirely outside of the banking area—we would be bound by bank mergers precedents we had no voice in pick-

[15] 280 U. S. 291, 303 (1940).
[16] S. Rept. 1775, 81st Cong., 1st sess. (1940), p. 7.
[17] *Transamerica Corporation* v. *Board of Governors of the Federal Reserve System*, 206 F. 2d 163 (1953), certiorari denied, 1953.
[18] Statement of Chairman Martin of the Federal Reserve Board before the Senate Antitrust Subcommittee, May 23, 1956, p. 5.
[19] Ibid., p. 80.

ing or shaping. For all these reasons, then, this Department must opposed proposed section 23 in its present form.

Instead, this Department favors simply amendment of Clayton Act section 7 to cover bank asset, as it now does bank stock, acquisitions. As a spokesman for the American Bar Association put it last year before the Senate Antitrust Subcommittee: [20]

"* * * the American Bar Association favors and recommends enactment of the proposal to embrace asset acquisitions by banks within the coverage of section 7. We believe that the law governing bank purchases of assets should conform to that which has controlled bank purchases of stock. The application of section 7 to bank mergers should not turn on the distinction between acquiring stock and acquiring assets."

Even more broadly, I suggest, such amendment of Clayton Act section 7 seems required by our basic belief in uniform application of our Nation's laws to all groups alike. In our more than half-century of Federal antitrust history, competition in banking has been deemed as important as in any other section of our economy. I see no reason for departing from that view now.

III. To repeat, the Department of Justice favors treatment of bank mergers, like other mergers, under Clayton Act section 7—and amendment of that provision to cover bank asset, as it now does bank stocks, acquisitions. Should this committee and the Congress conclude, however, that bank consolidations should, initially at least, be treated under the FDIC act, then I would suggest adoption of standards and procedures roughly paralleling those adopted last year, and reiterated in the pending committee print, controlling formation of, and acquisitions by, bank holding comapnies.

(1) Briefly put, the Bank Holding Company Act [21] and this committee print [22] have the effect that the Federal Reserve Board, passing on any proposed bank holding company merger, will consider, among other factors, the standards of Clayton Act section 7. As the Vice Chairman of the Federal Reserve Board wrote on January 18, 1957:

"Section 3 (c) of the Bank Holding Company Act requires the Board, in passing upon each application by a bank holding company for approval of its acquisition of bank stock, to consider certain specific factors, including whether or not the effect of the proposed acquisition would be to expand the size or extent of the holding company system beyond limits consistent with the public interest and the preservation of competition in the field of banking. The concept involved in this factor is a broad one, and in the Board's opinion adequate consideration of the facts in this regard necessarily involves consideration of the standards mentioned in section 7 of the Clayton Act—that is, whether in any line of commerce in any section of the country the effect of such acquisition might be substantially to lessen competition or to tend to create a monopoly."

As a result, the Vice Chairman of the Federal Reserve Board concluded:

"You may be assured that the Board in consideration of * * * [holding company mergers] will take into account whether the proposed transactions might involve a violation of section 7 of the Clayton Act or other statutes." [23]

From this, it seems clear, Clayton Act section 7's standard, under present law as well as the pending proposal, must be considered by the Board in passing on formations of, or acquisitions by bank holding companies. To the best of my knowledge, no banking agency official has challenged or even disagreed with consideration of section 7's competitive tests in the holding company context. In light of this history, amendment of section 23 to require that section 7's standard—not the pending proposal's novel "unduly" phrasing—be considered, along with other factors, by appropriate banking agencies in passing on bank mergers should raise small issue.

(2) Beyond the issue of competitive standards, section 23 of the pending print, second, should be revised to specify for all bank mergers the same procedures for

---

[20] Hearings before the Subcommittee on Antitrust and Monopoly of the Committee on the Judiciary, U. S. Senate (84th Cong., 2d sess.), on S. 3341, S. 3424, and H. R. 9424, at p. 172.

[21] Sec. 3. (c) In determining whether or not to approve any acquisition or merger or consolidation under this section, the Board shall take into consideration the following factor[s]: * * * (5) whether or not the effect of such acquisition or merger or consolidation would be to expand the size or extent of the bank holding company system involved beyond limits consistent with adequate and sound banking, the public interest, and the preservation of competition in the field of banking.

[22] Pending committee print, S. ——, title II, ch. 9, sec. 54 (c).

[23] Letter dated January 18, 1957, from C. C. Balderston, Vice Chairman of the Federal Reserve Board, to Congressman Emanuel Celler, chairman of the House Judiciary Committee.

cooperative liaison, advice, and intervention this Department and the Federal Reserve Board have evolved for bank holding company mergers. As you may know, the Federal Reserve Board is presently considering the first application for approval of a bank holding company merger under the 1956 act. To highlight the sort of mutually advantageous cooperation the Board and this Department have evolved, and underscore the usefulness of the same procedures under section 23, let me review briefly the path each agency has pursued in consideration of this proposed holding company merger.

Initially, after this Department had written to the Board indicating knowledge of the proposed holding company's formation, the Board on November 29, 1956, replied that: "* * * we will be pleased to advise you [of any hearing] and notice of the hearing will be published in the Federal Register."

Some 2 weeks later (on December 11, 1956), this Department responded that:

"We appreciate your advice that, should the Board of Governors determine to hold a hearing on this matter, you will give us notice. In the event the Board determines not to hold a hearing, we would also appreciate being advised in advance of the Board's ultimate decision to approve or disapprove the application.

As you know, this Department's letter went on to emphasize, "our responsibilities under the antitrust laws require us to remain conversant with this matter. It would be helpful, therefore, and might avoid a duplication of work by two different agencies on the same matter, if you would be able to furnish us with any basic competitive information you have collected or compiled relating to these banks * * *."

Finally, after this Department had kept the Board abreast of the path of our antitrust investigation and of the possibility of some Justice Department participation in the Board hearing, the Board replied on January 18, 1957:

"We will be very glad to have you submit a statement or file a brief at the appropriate time if you decide to do so. In the meantime, the Board or its staff will be glad to be of any assistance it can to the Department in connection with any aspects of this matter."

So much for this brief narration of dealings between this Department and the Federal Reserve Board in the course of a consolidation under the Bank Holding Company Act. More broadly, however, this bit of history suggests appropriate roles for this Department and each banking agency in consideration of, not only holding company, but all bank mergers. Section 23 should be amended, therefore, specifically to require notice to the Attorney General and enable him to intervene, or at least offer his views, to the banking agency considering any bank merger.

(3) Finally, beyond competitive standards and questions of intervention, section 23 should be amended, again paralleling Bank Holding Company Act provisions, to include some antitrust savings clause. The Bank Holding Company Act,[24] and the pending print,[25] specify that:

"Nothing herein contained shall be interpreted or construed as approving any act, action or conduct which is or has been or may be in violation of existing law, nor shall anything herein contained constitute a defense to any action, suit or proceeding pending or hereafter instituted on account of any prohibited antitrust or monopolistic act, action, or conduct."

This savings clause should apply to all bank mergers as it now does to formation of, or acquisition by, bank holding companies. Such application would carry out the proposal advanced by the Federal Reserve Board Chairman that:

"The Attorney General * * * would continue to have full authority to institute proceedings under the Clayton Act, if he should deem it desirable, with respect to any situation resulting from the particular merger or consolidation."[26]

Accordingly, I would suggest that this committee write into pending section 23 the same antitrust savings clause contained in Bank Holding Company provisions (reiterated in title II, ch. 9, sec. 61 of the pending committee print). As a corollary, of course, since the savings clause refers to "existing law," this committee shouud make clear its support of amendment of section 7 to cover bank asset as well as stock acquisitions. Only thus would the antitrust savings clause have real meaning.

---

[24] 70 Stat. 133, May 9, 1956.

[25] Title II, ch. 9, sec. 61.

[26] Statement by Federal Reserve Board Chairman Martin, explaining the Board's proposal for handling bank mergers, p. 691 of hearings of Senate Antitrust and Monopoly Subcommittee To Study the Antitrust Laws of the United States, and Their Administration, Interpretation, and Effect, Pursuant to S. Res. 61 (84th Cong., 1st sess.).

In sum, these suggested revisions would maintain banking agencies' primary initial responsibility to pass on bank mergers and go a long way toward insuring effective application of a uniform competitive standard. They would apply to all bank mergers those provisions this committee, and indeed the Congress, has specified for bank holding companies. Taken together, I conclude, these suggested revisions would mitigate, if not minimize, the force of my objections to present section 23.

Senator ROBERTSON. The next witness is from the Bureau of Federal Credit Unions. We are glad to have before us Hon. J. Deane Gannon, Director of the Bureau of Federal Credit Unions.

We will be glad to hear from you.

STATEMENT OF J. DEAN GANNON, DIRECTOR, BUREAU OF FEDERAL CREDIT UNIONS, DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE

Mr. GANNON. Mr. Chairman, gentlemen, I am J. Deane Gannon, Director of the Bureau of Federal Credit Unions, Department of Health, Education, and Welfare.

Last fall the committee asked our Department for recommendations to improve the Federal Credit Union Act through removal of obsolete provisions and similar measures. Such recommendations were made to Senator Robertson in our letter of October 4, 1956, and were further discussed in my testimony before the committee on November 10, 1956. Subsequently, a committee print was prepared in which many of these recommendations were included either without change or with modifications that still retained much of their initial purpose.

In response to your request for our views on the committee print, the Secretary of Health, Education, and Welfare is submitting a written report commenting on title VII and on those parts of VIII which are of concern to the Bureau of Federal Credit Unions. I accordingly propose to address my testimony to two of the provisions of the bill affecting us that in our opinion merit special consideration.

The first of these is a provision for mandatory annual audits of Federal credit unions contained in the proposed section 7 (b) of the Federal Credit Union Act, as included in title VII of the committee print. This section would require Federal credit unions with assets of $50,000 or more to have an annual audit made by an "independent individual or firm approved by the Director" of the Bureau of Federal Credit Unions. For those Federal credit unions with assets of less than $50,000 an annual audit would have to be made by the Bureau.

In order to indicate the reasons for our reservations about this proposed change I should first like to review briefly the situation at the present time. Section 11 (e) of the present Federal Credit Union Act, which is section 16 in the committee print, requires the supervisory committee of each Federal credit union to make audits at least quarterly. The Bureau believes that this process of audit by persons not responsible for operation, but still part of the management of the credit union, is sound since the responsibility for audit and internal control is peculiarly appropriate for management to assume.

Mr. ROGERS. Mr. Gannon, may I ask you a question?

Mr. GANNON. Yes, Mr. Rogers.

Mr. ROGERS. I wonder for the record if you would give the membership of the supervisory committee and how they are selected.

Mr. GANNON. As to the members of the supervisory committee, three members are elected annually by the members under the present provisions of the Federal Credit Union Act, and they are responsible to the members only.

Senator BUSH. Is that a similar arrangement to a board of directors?

Mr. GANNON. No, sir. They just have the responsibility for audit, and they also have power to remove officers and directors. The board of directors manages the credit union and is a separate body.

Senator BUSH. And does each authorized credit union have such a supervisory committee?

Mr. GANNON. Yes, Senator, they do.

Mr. ROGERS. You have actually three groups? Your supervisory committee, your board of directors, and your credit committee?

Mr. GANNON. Credit committee.

Senator BUSH. Are these members of the supervisory committees compensated by the credit union?

Mr. GANNON. No, Senator, the act prohibits compensation for the members of any of the committees or the directors.

We have been working steadily in an effort to strengthen the auditing activities of management and have given as much help as we could in the development of internal control and audit. We recently issued a comprehensive manual designed to improve the quality of audits performed by the supervisory committees and independent auditors. When this manual was issued we furnished each Federal credit union with a copy. We were greatly heartened to learn that the Government Printing Office sold 3,500 additional copies in a 3-month period. This suggests both the desire of credit-union officials to do a good job and the acceptance ofthe manual as a real help to them. In a further effort to strengthen this function of supervisory committees, we recommended, and this committee included in the proposed section 14 of the Federal Credit Union Act, a specific provision for compensated auditing assistance to supervisory committees.

The Bureau certainly does not oppose independent audits for credit unions and encourages those audits for credit unions where earnings are sufficiently large.

As distinguished from the audit function which, as I indicated, we believe to be a function of management, section 7 (a) of the act, as contained in title VII of the print, provides for examinations of Federal credit unions by the Bureau. It is our belief that this is the proper role for the Federal agency and we believe it important that its examination function be kept distinct from that of independent audit. We accordingly question the desirability of the Bureau's undertaking to audit the smaller credit unions.

Several specific questions are posed by the new provision. We seriously question whether the Director of the Bureau of Federal Credit Unions should have the responsibility for approving the individuals or firms who would make independent audits for credit unions with assets of $50,000 or more. In addition, the earnings of some of these credit unions with assets only slightly above $50,000 are sufficiently low that we doubt very much that they can pay the cost of a worthwhile independent audit annually and still have sufficient earnings to meet their obligations for reserves, operating costs, and dividends.

The annual audit of those credit unions whose assets are less than $50,000 by the Bureau poses questions of a different type. Aside from our basic question as to whether the supervising agency examination should relieve Federal credit unions of independent audits on a regular basis, it would seem apparent that the assumption of this responsibility would substantially increase the cost of Bureau operation. The Bureau, you will recall, receives no appropriated funds and is dependent on the fees that it charges for supervision and examination.

If, as the provision would seem to recognize, the Federal credit unions of this size have insufficient earnings to pay for an independent audit, it is not likely that they could pay an increased examination fee to the Bureau for the performance of this function. If smaller credit unions were unable to pay the added costs and the Bureau is to remain self-sustaining the only source of additional revenue would be higher examination fees for the larger credit unions. We seriously question whether this is equitable or desirable.

Finally, we should like to point out that, so far as we have been able to determine, other financial institutions are not subject by law to a requirement for independent annual audit.

As we indicated in the discussion of the recommendations included with our letter of October 4, 1956, to the committee, and as I have indicated today, we have been making an effort progressively to strengthen the internal audit function coupled with the encouragement of independent audits where this appears feasible. This is a subject of continuing study on our part. Should our study indicate the desirability of any legislative changes, we will wish to make recommendations for such changes to the committee at the appropriate time.

The recommendation incorporated in the proposed section 14 of the act, as included in the committee print, is a change in this field which our previous studies have indicated is desirable. However, we would at this time recommend against the inclusion of the changes made by the proposed section 7 (b) of the act, as contained in title VII of the print.

Senator BRICKER. What does that say?

Mr. GANNON. Compensation for auditing. In other words, while the supervisory committee may not be compensated, they may engage competent people and pay for the assistance.

Senator BUSH. And you want to oppose it?

Mr. GANNON. Now, we are in favor of that part.

Section 21 (i) of the Federal Credit Union Act, as contained in title VII of the committee print, and the amendments to sections 217 and 218 of the criminal code proposed by section 803 of the committee print would regulate the relationships between Bureau employees and credit unions in an effort to eliminate conflicts of interest. These sections deal with gifts, gratuities, or loans to a Bureau employee by a Federal credit union.

In discussing these provisions, I should like to make it perfectly clear that the Department is wholly in accord with the objective sought in the eliminating of conflicts of interest. If there were any way in which all risks of such a conflict could be eliminated without placing undue restrictions on employees—restrictions that might actually hamper the effectiveness of operation for the Bureau and the Federal credit unions—we would be strongly in favor of adopting it. With regard to the proposed provisions of the criminal code dealing with gifts, gratuities, or loans by a Federal credit union, it should be noted that we now have definite policies which are in agreement with the objectives sought. Fortunately, problems have not arisen in this area and we accordingly are inclined to examine closely any adverse effects that the proposed legislation might have on Bureau operations.

It is our judgment that if these areas are to be regulated by statute at all, so far as the Bureau is concerned, it would be preferable that this be done through revision of the criminal code rather than through the type of regulation by the Director that would be provided by the proposed section 21 (i) of the Federal Credit Union Act. We would accordingly not recommend the inclusion of the latter.

The subparagraphs designated (ii) in sections 217 and 218 of the criminal code, included in title VIII of the committee print, might well be construed to preclude the offer by any Federal credit union, or the acceptance by any former Bureau employee, of employment by a Federal credit union, within a period of 2 years following his employment by the Bureau.

As I have indicated, we are anxious to avoid possible damage that could result from a conflict of interest. On the other hand, it is our judgment that, in those instances where former Bureau employees have subsequently been employed in Federal credit unions, there is some mutual advantage derived by both. We should also like to point out that employment in Federal credit union work is a relatively narrow field and that mobility from one job to another would be considerably restricted by this provision. This might have the result of making it more difficult for the Bureau to secure the services of some of the most competent people in the field. These considerations should be weighed against any possible advantage which might result from the proposed revisions of sections 217 and 218 of the criminal code.

We are particularly concerned because these sections appear to us to be sufficiently broad to cover not only instances where the subsequent employment is of a Bureau employee who examined or supervised the Federal credit union concerned, but also instances where other employees are involved, including those in stenographic and clerical positions. It would not seem desirable or necessary to apply the provisions to the latter.

We would, therefore, like to recommend that the proposed revisions of sections 217 and 218 of the criminal code be modified to apply only in those areas and to those employees who, because of their specific duties, create an appreciable risk of damage because of a possible conflict of interest.

The Bureau of the Budget advises that while it perceives no objection to the submission of this testimony to your committee it wishes to reserve its position with respect to the proposed section 7 of the Federal Credit Union Act pending further study.

May I express my appreciation for the opportunity to appear before the committee today.

Senator SPARKMAN. Thank you, Mr. Gannon.

Are there any questions? Senator Bricker? Senator Bush? Senator Douglas?

Senator DOUGLAS. Mr. Gannon, I think many of us have been disturbed by embezzlements and defalcations from financial institutions. We have, in Chicago, an organization called the Association of Bank Depositors which, from time to time, issues bulletins on the number of bank embezzlements, and the total numbers from year to year are appreciable, and from time to time there are rather startling cases.

In recent periods the attention of the public has been called to embezzlements in the building and loan field and in the credit union field. I am not saying that there is a greater incidence of embezzlements in the credit unions than is the case with other financial institutions; but I wondered if you could give us some information on the number of embezzlements which you have traced in the field of Federal credit unions in recent years?

Mr. GANNON. I do not have that information with me, Senator. We will be very happy to furnish it for the committee.

Senator DOUGLAS. Is it in such shape that it could be sent up immediately?

Mr. GANNON. I think so, yes, sir.

Senator DOUGLAS. Could you hazard a guess as to it?

Mr. GANNON. Well, I would just be a little bit reluctant to hazard a guess, Senator, for this reason—that we have what we call shortage statistics, but they include loses from burglary and robbery, and so forth, so we would have to sort of sift out from that the fraud and embezzlements.

Senator DOUGLAS. Have you been alarmed over this tendency?

Mr. GANNON. I would not say that we are alarmed, but we are deeply conscious of this situation, and that is why we are working so hard in this field of developing internal audit and control for the credit unions.

Senator DOUGLAS. Of course the danger with an internal audit is that all too frequently there is the case of where the guilty audit themselves.

Mr. GANNON. That is what we seek to prevent, sir.

Senator DOUGLAS. I notice that in your statement on page 4, the end of the first paragraph, you say:

> Finally, we should like to point out that, so far as we have been able to determine, other financial institutions are not subject by law to a requirement for independent annual audit.

Are you certain that your statement is correct on this point?

Mr. GANNON. Well, I feel, sir, that we are talking about an annual, independent audit being a requirement of the law. We examined the statute, and we did not find any reference in the other——

Senator DOUGLAS. I would like to ask counsel.

Mr. ROGERS. I think that Mr. Gannon is technically correct. The authorization for audit in the Home Loan Bank Board is done by regulation.

Mr. GANNON. Yes, sir.

Senator DOUGLAS. But they do require it by regulation?

Mr. ROGERS. That is right.

Senator DOUGLAS. That is, they require an independent audit?

Mr. ROGERS. They have three different ways of doing it.

Senator DOUGLAS. Do they permit internal audits?

Mr. ROGERS. Yes.

Senator DOUGLAS. All right. Then what you are saying is that even by regulation no more severe tests are imposed on building and loan associations than now are imposed on credit unions?

Mr. GANNON. That is right, sir.

Senator DOUGLAS. No more severe; no more lax?

Mr. ROGERS. I do not think that is absolutely correct, Senator.

Mr. GANNON. Maybe I misunderstood.

Mr. Rogers. Under the Federal Home Loan Bank Board system, you have either, (1) the Federal Home Loan Bank Board making the audit, or (2) an acceptable CPA making the audit, or (3) under very limited and very specified conditions they may have an internal audit. But is is very restricted. It is only applicable to a few cases. I think that they are not comparable. I think the Home Loan Bank Board is much tougher.

Senator Douglas. I would also like counsel to inform me what the procedure is in the case of national banks, banks insured by FDIC, and banks members of the Federal Reserve System.

Mr. Rogers. In all three cases the law does not require audits and they are not required by regulations.

Senator Sparkman. Let me get that straight. It is not required in the law, but is set up by regulations?

Mr. Rogers. No; it is also not required by regulations in the case of the banks.

Senator Douglas. Mr. Gannon, is your point this: As long as this is not required by law for banks, why should it be required of credit unions?

Mr. Gannon. That is one of the considerations, Senator. However, that is not the most important consideration.

Senator Douglas. The second is that credit unions tend to be smaller than banks?

Mr. Gannon. That is right.

Senator Douglas. And to require an independent annual audit with the fees charged by the accountants would in many cases be a crushing financial burden?

Mr. Gannon. Yes, sir. That is one. And, on the other hand, if we were to undertake to do that it would become a burden for the Bureau, in the case of the small credit union.

Senator Bush. Would the Senator yield at that point for a question in point?

Senator Douglas. Yes, sir.

Senator Bush. How did the Bureau come out last year for its income and expenses?

Mr. Gannon. Sir, we collected enough fees to pay for our expenses, and we came out a little bit in the black. You see, we have a loan that we have to pay back at the rate of $25,000 a year, so that we always have to be at least $25,000 ahead until that loan is retired.

Senator Bush. But you are staying pretty close to the line, financially?

Mr. Gannon. Yes, sir.

Senator Bush. Thanks, Senator Douglas.

Senator Douglas. What are your total revenues?

Mr. Gannon. They were approximately $2 million, Senator Douglas.

Senator Douglas. And your surplus?

Mr. Gannon. What is that, sir?

Senator Douglas. And your surplus?

Mr. Gannon. Well, the surplus, as I said, has to be $25,000 to repay the loan, and then we are trying to accumulate enough funds to become——

Senator Douglas. What was your surplus?

Mr. GANNON. I am just guessing, Senator. I am guessing in the neighborhood of $80,000, including this $25,000.

Senator DOUGLAS. How many credit unions do you actually examine?

Mr. GANNON. We examined 85 percent of our credit unions at the end of the calendar year 1956. We have about 8,400 Federal credit unions as of now. So that means that we are examining them within about every 15 months on the average. Our lack of 100 percent is only due to the lack of recruitment of a sufficient number of examiners.

Senator DOUGLAS. And the 15 percent that you have not examined; what type of credit unions are those?

Mr. GANNON. They are—well, I will qualify that statement. If we have any problem cases, we make a point of having them examined as soon as possible. However, otherwise, we make no distinction as to which ones we will postpone or examine.

Senator DOUGLAS. You mean you have the right to examine any?

Mr. GANNON. That is right, sir.

Senator DOUGLAS. You take, in practice, 85 percent?

Mr. GANNON. That is right.

Senator DOUGLAS. They do not know in advance whether they are going to be in the percent left out?

Mr. GANNON. No, sir. That is a surprise examination.

Senator DOUGLAS. Will you have the same 15 percent year after year which are not examined?

Mr. GANNON. No, sir. We do examine all Federal credit unions, but we have difficulty in recruitment, and we lose a certain number of our examiners to industry, so that it is a matter of manpower. We would like to examine substantially 100 percent within each 12-month period.

Senator DOUGLAS. What is your assessment now? What is the assessment which you levy upon the credit unions to finance your work?

Mr. GANNON. We have two types of assessment: One is the supervision fee, which is based upon assets and paid annually in January each year. Then we have an examination fee which is charged if and when the credit union is examined.

Senator DOUGLAS. How much is that?

Mr. GANNON. It is based on the size of the credit union.

Senator DOUGLAS. Supposing you have a credit union with $40,000 of assets; what would your charge be?

Mr. GANNON. Let me put it in these two categories, Senator: For those credit unions of $25,000 and less, the charge is 50 cents a hundred of assets. So the $20,000 credit union would pay $100.

Now, for those credit unions over $25,000 we have a combination asset and per diem charge. The per diem charge is $44 a day plus 3 cents per hundred of assets up to a million, thence decreasing over that.

Senator DOUGLAS. Thence what?

Mr. GANNON. Three cents a hundred of assets up to one million of assets. Then it decreases.

Senator DOUGLAS. Three cents?

Mr. GANNON. Yes, sir.

Senator SPARKMAN. Plus $44 per diem.

Mr. GANNON. $44 per day.

Senator DOUGLAS. How much of an increase in fees would you have to make in order to have a 100-percent inspection each year?

Mr. GANNON. Well, we would not have to increase our fees at all to have 100 percent. All we need to do is increase the number of examiners that we have, Senator.

Senator DOUGLAS. In order to meet those, you would have to have more revenue.

Mr. GANNON. Well, you see——

Senator SPARKMAN. As I understand, he said the difficulty was in finding the examiners.

Mr. GANNON. That is right, Senator. It is not a matter of revenue. It is a matter of finding qualified men and keeping them.

Senator DOUGLAS. If you were required to make the examination, you could find the men; could you not?

Mr. GANNON. Well, I do not believe it would be any easier, Senator, if we were required than it would be now. We are in competition, as other Government agencies are, with private industry, and——

Senator DOUGLAS. It might serve as a stimulant for you to get a full staff of examiners.

Mr. GANNON. Well, we are particularly conscious of that, Senator, and we are exerting every effort we can to recruit capable examiners. We train them to be good examiners. We feel quite proud of the job we are doing.

Senator DOUGLAS. The subject of accountancy is the most popular subject in our schools of commerce and business, and our schools of commerce and business are overflowing with students. To the ordinary eye, the profession of accountancy is not undermanned.

Mr. GANNON. They are in terrific demand, Senator.

Senator DOUGLAS. I said "undermanned."

Would you object if there was a requirement for annual examination by the Bureau of Credit Unions?

Mr. GANNON. Now you are talking of annual examination as distinct from audits, Senator?

Senator DOUGLAS. Well, yes. All right.

Mr. GANNON. No, we—well, I think we should reserve this one condition: We would like very much to examine every credit union within 12 months. However, I think we have to be realistic, that if you cannot recruit 100 percent of your force you might not do it. However, that is our goal. Our concern with this provision is only that we do not want to become the substitute for good internal audit.

Senator DOUGLAS. I understand that. But the external examination is a stimulus to keeping the house in order internally.

Mr. GANNON. That is right.

Senator DOUGLAS. Have you found many cases of embezzlement in your examinations?

Mr. GANNON. Yes, Senator; we have uncovered them.

Senator DOUGLAS. What do you do in these cases?

Mr. GANNON. Well, in such cases, of course, we report them to the United States attorney immediately, and then we work to determine the amount of the loss to the credit union and to help them in any way recover through their surety bonds.

Senator BUSH. May I ask a question there, Senator?

Senator DOUGLAS. Oh, surely.

Senator BUSH. We had a very big loss up in Connecticut last year. You recall that?

Mr. GANNON. That is right, Senator.

Senator BUSH. Is that one of the largest losses of the year?

Mr. GANNON. Yes, it was. Very definitely.

Senator BUSH. What had been the practice there regarding audit? Had this union employed outside auditors or——

Mr. GANNON. No, sir. They had not, and that was one of their failings.

Senator BUSH. How about examination by your headquarters?

Mr. GANNON. We had examined that credit union, but the type of loss was such that you would not uncover that unless you had a confirmation with the membership. In other words, cards were removed from the ledgers so there would be no way of anybody knowing unless there was a complete verification with the members.

Senator BUSH. Yes.

Mr. GANNON. That is properly a function of the supervisory committee, Senator.

Senator BUSH. They had to check with each member to make sure that each account was correct?

Mr. GANNON. That is right, Senator.

Senator BUSH. Any satisfactory audit would have to do that, would it not?

Mr. GANNON. Well, that would be a complete type of audit in order that you would confirm all of the members' accounts and then make an announcement that you are so doing.

Senator BUSH. Thank you, Senator.

Senator SPARKMAN. Any further questions?

Go ahead, Senator Douglas.

Senator DOUGLAS. What size credit union do you think could stand an independent audit with the fees which are customarily charged?

Mr. GANNON. I would guess——

Senator DOUGLAS. How big would it have to be?

Mr. GANNON. I think offhand a $100,000 credit union and above could do that, Senator. There is a possibility——

Senator DOUGLAS. Do you feel if this is done for credit unions it should also be done for savings and loan institutions, for mutual savings banks, for national banks, for State banks? Under the RFC, the State banks insured——

Mr. GANNON. Senator, I think most banking institutions employ independent auditors, and that is a judgment of management. I do not think that it should be a requirement for Federal credit unions because of the problem that it poses, Senator, not as is related particularly to banks or savings and loan associations.

Senator DOUGLAS. Is not the real problem of the smaller institutions across the board which may need this but which cannot afford it?

Mr. GANNON. That is right, to a certain degree. We are working to help them get this proficiency for the smaller credit unions, and I think that they can saisfactorily meet that problem.

Senator DOUGLAS. The Senator mentioned an embezzlement up in Connecticut. Was that a small credit union or a large one?

Mr. GANNON. No, Senator, that was a good-sized credit union. I do not recall offhand its assets. It was what we would term a large credit union. It was over several hundred thousand dollars.

Senator SPARKMAN. Senator Monroney.

Senator MONRONEY. In addition to the accounts of the members, the loan accounts, do they have a portfolio of investments for their surplus funds? Or are they required merely to keep them in banks?

Mr. GANNON. Their investment powers are very limited, Senator—United States Government securities or securities guaranteed as to principal and interest by the Government and shares of savings and loan associations which are insured.

Senator MONRONEY. Of course, your examiners, when they examine these 85 percent each year, check on the portfolio of other investments?

Mr. GANNON. Yes, they do, Senator.

Senator MONRONEY. Do they check on the age of the account, for past dues, and——

Mr. GANNON. Yes indeed. That is an important part of the examination requirement.

Senator MONRONEY. And require write-offs under standard forms when the accounts become uncollectible?

Mr. GANNON. That is right. And special reserve requirements in that interim process of becoming uncollectible.

Senator MONRONEY. Some of them have some remarkable records of collections. I just wondered if the accounts were properly aged.

Mr. GANNON. Yes, Senator. We are very proud of their experience, and I think it is due to a number of things. But we certainly do. That is one of our most important procedures—to age the accounts. And we have requirements for special reserves to meet delinquent accounts.

Senator MONRONEY. Would it be too expensive to have an outside audit that maybe would not be as complete as the one we were talking about but where they could give a general examination in between times or at the beginning of the calendar year of the assets and spot check some of the accounts to give an added degree? I personally feel that our other financial institutions also should have the outside audit, in that the limitations of a Government inspection sometimes do not go to the internal operation of the agency.

Mr. GANNON. Well, I think that is entirely possible, Senator. As a matter of fact, that is why we made this one recommendation to the committee to permit auditing assistance to be compensated for. Now, the supervisory committee may employ an individual who is a competent accountant to come in and do the type of thing that you are talking about.

Senator MONRONEY. That was what I was wondering about, because this supervisory board, as well-intentioned as they may be, are usually workmen in the industry or they are employees of the concern and do not have perhaps the competence in auditing to do more than to examine the audit that the man who is running the institution is submitting to them.

Mr. GANNON. That is right.

Senator MONRONEY. So your idea would be that you would allow—if you call it that—a secondary type of audit to be run by an independent outside source to advise the supervisory group?

Mr. GANNON. That is right, Senator. And a large number, a growing number each year, are engaging professional accountants to make audits.

Senator MONRONEY. And up to the ability of those to afford that independent, outside audit you would be in favor of that?

Mr. GANNON. That is right, Senator.

Senator MONRONEY. About $100,000 you think would be the——

Mr. GANNON. That would be just an offhand guess. Any above that certainly should be in a position to do it.

Senator MONRONEY. That is all.

Senator SPARKMAN. Do you want to ask some questions, Mr. Rogers?

Mr. ROGERS. Yes.

Mr. Gannon, are you familiar with the General Accounting Office recommendation that members of the credit committee and the Treasurer be excluded from the supervisory committee? I wonder if you would care to comment on that.

Mr. GANNON. Well, of course, we feel very strongly that the Treasurer should not be a part of the supervisory committee, and we question whether anybody who is in the operation should examine themselves, as Senator Douglas once mentioned. We think that is unsound. So that we feel that the committee, if there is a committee, should be composed of persons independent of the actual operation.

Mr. ROGERS. That would include the credit committee?

Mr. GANNON. Yes, that is our feeling.

Mr. ROGERS. That is all I have.

Senator SPARKMAN. Thank you very much.

Senator MONRONEY. Are these accounts insured in any way?

Mr. GANNON. No, Senator, they are not insured.

Senator MONRONEY. You require the bonding of the operators?

Mr. GANNON. We do. By regulation we have quite a stringent bonding requirement.

Senator SPARKMAN. I notice by your statement that the Budget Bureau reserves its opinion as to your recommendation on section 7.

Mr. GANNON. Section 7. That is right, Senator.

Senator SPARKMAN. I wonder when the committee is going to get the Budget Bureau's position on that.

Mr. GANNON. That is——

Senator SPARKMAN. But I take it from that that the Budget Bureau is in agreement with your position on the other matters. Is that right?

Mr. GANNON. That would be my understanding, Senator, yes. That is, on the full report which has been made.

Senator SPARKMAN. Yes. Thank you, Mr. Gannon.

Senator Robertson had to leave. I did have a matter that I would have liked to have called up while he was here, although I think those of us that are present could decide upon this as a wise procedure.

I have been rather overwhelmed by this bill, the size of it, in trying to go through it. It amounts to a rewriting of the law and there is nothing in there to indicate what the specific change is. I have a suggestion that seems to me would be good. You know on several different occasions when we were considering housing legislation a table was made that showed the amendments that were proposed and just what they would seek to do and what the position of the various groups or representatives who were present was. If that is not too big a job for the staff to do, it seems to me it would be most helpful to us in considering this bill.

Senator BRICKER. Is that not what this is?

Senator SPARKMAN. That does not exactly do it. We had parallel columns.

Senator BRICKER. I see. The old and the new? And which involved changes in the tentative draft?

Senator SPARKMAN. Yes.

Mr. WALLACE. Tomorrow morning there should be available a draft of the committee report which goes through the bill section by section and says whether or not there is a change in the present law and the degree to which there is such a change. In addition, we have made arrangements with the Federal Reserve Board to have one of their staff assist us in briefing any member of the committee who would like further individual briefing in addition to this draft report which we will have available tomorrow.

Senator SPARKMAN. I am not sure that reaches just what I had in mind. I see that all of that would be helpful. That committee report then would show if a certain provision in the present law has been changed?

Mr. WALLACE. That is right.

Senator SPARKMAN. I mean if it is sought to be changed it would show what that change is? Is that right?

Mr. WALLACE. Yes. Where there was no change it would so state, and it would state what it was about. When there was a change from existing law, it would say what the change was.

This has been done in as brief a manner as possible to permit members of the committee to raise further questions if they wish. And then we will, of course, have Mr. Rogers and myself and Mr. McKenna and also an expert from the Federal Reserve Board to help us with any questions that are raised in addition.

I would like to show you the report tomorrow morning and then we can go further into it to make sure we do have what you want.

Senator SPARKMAN. It just seems to me whatever help we get to help us along in consideration would be good. For instance, on the last point I asked Mr. Gannon, I noted he said the Budget Bureau has given clearance on this except as to section 7. They reserved their opinion on that. I think it is sometimes helpful for us to know what the Bureau of the Budget thinks about this or what the agency concerned thinks about this, what the arguments are pro and con.

Senator BRICKER. I think it might be well, but I do not think the Bureau of the Budget should be in a position to hold up testimony——

Senator SPARKMAN. Neither do I. I am just talking about what would be helpful to us.

The second thing is this: According to the chairman, this does conclude the hearings. Did he say anything about how long the record would stay open?

Mr. ROGERS. It will close today.

Senator SPARKMAN. Closes today? If there is nothing further, the committee will stand in recess subject to the call of the chairman for its next meeting.

(Whereupon, at 11:47 a. m., the subcommittee was recessed subject to the call of the chairman.)

(The following letters, telegrams, and statements were received for the record.)

ST. LOUIS, MO., *February 15, 1957.*

Hon. A. WILLIS ROBERTSON,
Chairman of the Subcommittee to the Senate Committee on Banking and Currency, United States Senate, Washington, D. C.

DEAR SENATOR ROBERTSON: At your committee hearings on January 28, 1957, you indicated that you would like to have a further statement from the advisory committee at the conclusion of all the testimony. Thus, I would appreciate this statement being inserted in the record.

Since testifying on January 28, 1957, I have been provided with substantially all of the prepared statements of the witnesses who followed me, but I have not had the benefit of the discussions which took place at the hearings. This material has been carefully reviewed, and while it contains many new approaches to the problems, nevertheless it does not contain any new basic principles which were not previously considered by the advisory committee. Hence, I felt there was no occasion, nor did time permit, the distribution of such material to the members of the advisory committee. In reaching this conclusion, I have assumed that matters such as that mentioned by Mr. Paul Warner in regard to section 5 (g) as it appears at page 209 of the committee print bill, and by Mr. Henry Bubb in regard to section 13 as it appears at page 196 of the committee print bill have been or will be corrected.

Accordingly, the advisory committee makes no changes in its recommendations as a result of the hearings on the committee print bill, and we see no occasion to change or amend the testimony which we gave on January 28, 1957.

Time and facilities have not permitted the advisory committee and its volunteer staff to consider all of the language of the committee print bill. Thus, I am confident that your committee will agree that we should not assume, and we are not assuming, any responsibility for the language used in the final version of the bill.

Sincerely yours,

KENTON R. CRAVENS,
Chairman, Advisory Committee to Senate Committee on Banking and Currency for the Study of Federal Statutes Governing Financial Institutions and Credit.

DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE,
February 15, 1957.

Hon. J. W. FULBRIGHT,
Chairman, Committee on Banking and Currency, United States Senate, Washington 25, D. C.

DEAR MR. CHAIRMAN: This letter is in response to your request of January 5, 1957, for a report on committee print of the Financial Institutions Act of 1957, dated January 7, 1957.

The bill would amend and revise the statutes governing financial institutions and credit.

Title VII of the committee print would revise the Federal Credit Union Act in a number of respects. Insofar as the changes are in accord with the recommendations made in our letter of October 4, 1956, to Senator Robertson (implemented by the testimony of Mr. J. Deane Gannon, Director of the Bureau of Federal Credit Unions, before the committee on November 10, 1956) and in Mr. Banta's letter of November 20, 1956, to Mr. Donald L. Rogers, commenting on his proposed outline of the revised act, no further comment by the Department would appear necessary. This report will instead be confined to comment on the other changes included in this title and title VIII of the committee print which are of concern to us and on those changes recommended by us which were not included or were included with modification.

We observed that two of the recommendations made by the Department were not included. One of these proposed that the supervisory committee should not include persons who are involved in or responsible for any operations of the Federal credit union. We still think this exclusion is desirable but it can be considered with the study commented on with respect to section 7 (b). The other was related to a need indicated by credit unions for authority to provide for a loan officer. We have believed that there was merit in this proposal so long as the delegated authority was held within well-defined limitations.

Subsection (b) of section 7 adds a new provision for mandatory annual audits. For those Federal credit unions with assets of $50,000 or more the audit would be made by an independent individual or firm. The individuals or firms making such audits would be approved by the Director. Federal credit unions with assets of less than $50,000 would be audited annually by the Bureau of Federal Credit Unions. We do not feel that the determination of qualifications of individuals or firms as auditors should be made by the Director. We further believe that the role of the Government should be that of making examinations as provided for in subsection (a) of this section and should not be one of auditing each credit union. The responsibility for audit and internal control is considered to be a function of management. Section 16 presently requires the supervisory committee to make audits at least quarterly. We had recommended to your committee and section 14 now provides authority for compensation for auditing assistance for the supervisory committee. With this revision we anticipate that independent audits will be more extensively made for those credit unions whose earnings will permit. The Bureau has a real interest in the development of internal control and audit and has just recently issued a comprehensive manual which will enhance the quality of audits performed by the supervisory committees and independent auditors. Further study is being carried on in this area and as indicated in our letter of October 4, 1956, to the committee we may subsequently offer suggestions for changes in the basic law. The cost of the proposed additional activity for the Bureau which operates without appropriated funds would also be a consideration. We, therefore, would not favor the revision of this subsection as contemplated by the committee print and suggest that legislation in this area be deferred until further study will develop the desirable revisions.

The proposed changes incorporated in section 18 with respect to the declaration of dividends were not recommendations of this Department. The declaration of dividends by the members has been traditional in Federal credit unions since the original law in 1934. We acknowledge that the declaration by the board has something to recommend it and, therefore, interpose no objection to this change or to permissive authority for semiannual dividends and the grace period of 5 days as proposed. We do feel that the objectives sought could be more properly stated in language similar to that enclosed.

The Federal Credit Union Act now permits the discretionary allotment of space, if available, in Federal buildings to Federal credit unions whose membership is composed exclusively of Federal employees and members of their families. Section 25 of the bill would permit space allocation for Federal credit unions whose membership also included retired Federal employees. The committee's attention is directed to the fact that certain Federal agencies, such as Veterans' Administration hospitals, do have a small number of persons, such as representatives of veterans organizations and the Red Cross, who are employed within the installation but who are not Federal employees and who would be excluded from membership if the Federal credit union occupied space in a Federal building.

In the existing Federal Credit Union Act there is a provision making its applicable specifically to the Panama Canal Zone. While section 26 of the bill makes the act applicable to the Territories and possessions, it does not specifically mention the Panama Canal Zone. To make clear the act's continued applicability to the Canal Zone, we believe it would be desirable to include the specific reference to it.

Subsection (i) of section 21 is related to sections 217 and 218 of title 18 of the United States Code as revised by title VIII of the committee print. It is our opinion that if these areas are to be regulated, the revision to the Criminal Code is preferable to regulation by the Director and we, therefore, recommend deletion of subsection (i) of section 21.

Section 803 of the committee print would revise sections 217 and 218 of the Criminal Code to apply to all employees of the Bureau of Federal Credit Unions with respect to the offering of gratuities, gifts or loans by a Federal credit union to such employees and the acceptance of gifts, gratuities and loans by the employees. The revision would further cover offers of employment and acceptance of employment by such employees. These provisions with respect to gifts and gratuities are in line with present Bureau policy. The examiners for the Bureau also are now precluded from examining a Federal credit union to which they may be indebted. While we have had no problem in these areas we do appreciate the objectives sought. We do, however, feel that subsection (ii) is too broad in its apparent application to all employees of the Bureau. It does not seem necessary or desirable to apply these provisions to the clerical, stenographic or other employees who are not in a position of having a conflict of interest by reason of their duties or responsibilities. We, therefore, would recommend modifications in subsection (ii) in both sections 217 and 218 to apply to only those employees who by virtue of their specific duties would be in a position to render an abuse from a conflict of interest.

There are a number of changes of a technical and drafting nature which we would be glad to discuss with your committee at your convenience.

We would therefore recommend that the bill with sections 7 (b) and 21 (i) deleted, with the suggested modification of section 18 of title VII, and with the modification of sections 217 and 218 of title VIII be enacted by the Congress.

The Bureau of the Budget advises that while it perceives no objection to the submission of this report to your committee it wishes to reserve its position with respect to the proposed section 7 of the Federal Credit Union Act pending further study.

Sincerely yours,

——— ———, *Secretary.*

SUGGESTED LANGUAGE FOR SECTION 18 DIVIDENDS

Annually or semiannually, as the bylaws may provide and after provision for the required reserves, the board of directors may declare a dividend to be paid from the remaining net earnings. Such dividend shall be paid on all paid-up shares outstanding at the end of the period for which the dividend is declared. Shares which become fully paid up during such dividend period and are outstanding at the close of the period shall be entitled to a proportional part of such dividend. Dividend credit for a month may be accrued on shares which are or become fully paid up during the first 5 days of that month.

UNITED STATES SENATE,
COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE,
Washington, D. C., February 16, 1957.

Hon. WILLIS ROBERTSON,
Chairman, Subcommittee on Banking, Banking and Currency Committee, United States Senate, Washington, D. C.

DEAR SENATOR ROBERTSON: I am writing to urge that your subcommittee eliminate from legislation pending before your group a proposed amendment to paragraph 26, section 3 of the FDIC Act which would prohibit the absorption of exchange by nonmember banks of the Federal Reserve System.

This proposed amendment would seriously affect the operations of approximately 80 small banks in South Carolina and approximately 1,800 other banks across the country. Passage of this amendment would, in some instances, reduce already small profit margins of these banks by at least one-third, and most of these banks are located in small agricultural communities which are already suffering from the adverse effects of reduced farm income.

During the past few weeks I have received a huge volume of correspondence from bankers in South Carolina on this matter. Every letter and telegram has contained remarks of protest and opposition to this pending amendment. I am enclosing several of these letters and telegrams, and I would appreciate your having these, along with my letter, included in the record of your hearings.

Thanking you for your attention to this matter, and with kindest personal regards,

Sincerely,

STROM THURMOND.

for a loan officer. We have believed that there was merit in this proposal so long as the delegated authority was held within well-defined limitations.

Subsection (b) of section 7 adds a new provision for mandatory annual audits. For those Federal credit unions with assets of $50,000 or more the audit would be made by an independent individual or firm. The individuals or firms making such audits would be approved by the Director. Federal credit unions with assets of less than $50,000 would be audited annually by the Bureau of Federal Credit Unions. We do not feel that the determination of qualifications of individuals or firms as auditors should be made by the Director. We further believe that the role of the Government should be that of making examinations as provided for in subsection (a) of this section and should not be one of auditing each credit union. The responsibility for audit and internal control is considered to be a function of management. Section 16 presently requires the supervisory committee to make audits at least quarterly. We had recommended to your committee and section 14 now provides authority for compensation for auditing assistance for the supervisory committee. With this revision we anticipate that independent audits will be more extensively made for those credit unions whose earnings will permit. The Bureau has a real interest in the development of internal control and audit and has just recently issued a comprehensive manual which will enhance the quality of audits performed by the supervisory committees and independent auditors. Further study is being carried on in this area and as indicated in our letter of October 4, 1956, to the committee we may subsequently offer suggestions for changes in the basic law. The cost of the proposed additional activity for the Bureau which operates without appropriated funds would also be a consideration. We, therefore, would not favor the revision of this subsection as contemplated by the committee print and suggest that legislation in this area be deferred until further study will develop the desirable revisions.

The proposed changes incorporated in section 18 with respect to the declaration of dividends were not recommendations of this Department. The declaration of dividends by the members has been traditional in Federal credit unions since the original law in 1934. We acknowledge that the declaration by the board has something to recommend it and, therefore, interpose no objection to this change or to permissive authority for semiannual dividends and the grace period of 5 days as proposed. We do feel that the objectives sought could be more properly stated in language similar to that enclosed.

The Federal Credit Union Act now permits the discretionary allotment of space, if available, in Federal buildings to Federal credit unions whose membership is composed exclusively of Federal employees and members of their families. Section 25 of the bill would permit space allocation for Federal credit unions whose membership also included retired Federal employees. The committee's attention is directed to the fact that certain Federal agencies, such as Veterans' Administration hospitals, do have a small number of persons, such as representatives of veterans organizations and the Red Cross, who are employed within the installation but who are not Federal employees and who would be excluded from membership if the Federal credit union occupied space in a Federal building.

In the existing Federal Credit Union Act there is a provision making its applicable specifically to the Panama Canal Zone. While section 26 of the bill makes the act applicable to the Territories and possessions, it does not specifically mention the Panama Canal Zone. To make clear the act's continued applicability to the Canal Zone, we believe it would be desirable to include the specific reference to it.

Subsection (i) of section 21 is related to sections 217 and 218 of title 18 of the United States Code as revised by title VIII of the committee print. It is our opinion that if these areas are to be regulated, the revision to the Criminal Code is preferable to regulation by the Director and we, therefore, recommend deletion of subsection (i) of section 21.

Section 803 of the committee print would revise sections 217 and 218 of the Criminal Code to apply to all employees of the Bureau of Federal Credit Unions with respect to the offering of gratuities, gifts or loans by a Federal credit union to such employees and the acceptance of gifts, gratuities and loans by the employees. The revision would further cover offers of employment and acceptance of employment by such employees. These provisions with respect to gifts and gratuities are in line with present Bureau policy. The examiners for the Bureau also are now precluded from examining a Federal credit union to which they may be indebted. While we have had no problem in these areas we do appreciate the objectives sought. We do, however, feel that subsection (ii) is too broad in its apparent application to all employees of the Bureau. It does not seem necessary or desirable to apply these provisions to the clerical, stenographic or other employees who are not in a position of having a conflict of interest by reason of their duties or responsibilities. We, therefore, would recommend modifications in subsection (ii) in both sections 217 and 218 to apply to only those employees who by virtue of their specific duties would be in a position to render an abuse from a conflict of interest.

There are a number of changes of a technical and drafting nature which we would be glad to discuss with your committee at your convenience.

We would therefore recommend that the bill with sections 7 (b) and 21 (i) deleted, with the suggested modification of section 18 of title VII, and with the modification of sections 217 and 218 of title VIII be enacted by the Congress.

The Bureau of the Budget advises that while it perceives no objection to the submission of this report to your committee it wishes to reserve its position with respect to the proposed section 7 of the Federal Credit Union Act pending further study.

Sincerely yours,

——— ———, *Secretary.*

SUGGESTED LANGUAGE FOR SECTION 18 DIVIDENDS

Annually or semiannually, as the bylaws may provide and after provision for the required reserves, the board of directors may declare a dividend to be paid from the remaining net earnings. Such dividend shall be paid on all paid-up shares outstanding at the end of the period for which the dividend is declared. Shares which become fully paid up during such dividend period and are outstanding at the close of the period shall be entitled to a proportional part of such dividend. Dividend credit for a month may be accrued on shares which are or become fully paid up during the first 5 days of that month.

UNITED STATES SENATE,
COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE,
Washington, D. C., February 16, 1957.

Hon. WILLIS ROBERTSON,
Chairman, Subcommittee on Banking, Banking and Currency Committee, United States Senate, Washington, D. C.

DEAR SENATOR ROBERTSON: I am writing to urge that your subcommittee eliminate from legislation pending before your group a proposed amendment to paragraph 26, section 3 of the FDIC Act which would prohibit the absorption of exchange by nonmember banks of the Federal Reserve System.

This proposed amendment would seriously affect the operations of approximately 80 small banks in South Carolina and approximately 1,800 other banks across the country. Passage of this amendment would, in some instances, reduce already small profit margins of these banks by at least one-third, and most of these banks are located in small agricultural communities which are already suffering from the adverse effects of reduced farm income.

During the past few weeks I have received a huge volume of correspondence from bankers in South Carolina on this matter. Every letter and telegram has contained remarks of protest and opposition to this pending amendment. I am enclosing several of these letters and telegrams, and I would appreciate your having these, along with my letter, included in the record of your hearings.

Thanking you for your attention to this matter, and with kindest personal regards,

Sincerely,

STROM THURMOND.

BANK OF FORT MILL,
FORT MILL, S. C., *February 8, 1957.*

HON. STROM THURMOND,
United States Senate, Washington, D. C.

DEAR MR. THURMOND: We shall appreciate it if you will oppose with all your might amendment the FDIC Act, section 26, title 3, to prohibit the paying of interest through the absorption of exchange.

Very truly yours,

L. F. ABERNETHY,
Executive Vice President and Cashier.

THE SALUDA COUNTY BANK,
Saluda, S. C., February 9, 1957.

HON. J. STROM THURMOND,
United States Senate, Washington, D. C.

DEAR SENATOR THURMOND: Enclosed is a copy of a letter to Senator Sparkman requesting his consideration in eliminating a clause in a tentative bank bill which would end the practice of FDIC insured nonmember banks absorbing exchange charges.

The small banks in rural communities need the small exchange charge to operate, and when a larger city bank with large industrial accounts can absorb this exchange for its depositors, it seems to be for the best interest of country banks that they be allowed to do so.

Your consideration in this will be deeply appreciated.

Respectfully yours,

S. R. E. ADDY, *President.*

WOODRUFF, S. C., *February 15, 1957.*

STROM THURMOND,
Senate Office Building, Washington, D. C.

Received your letter. Urgent you request that Senator Robertson delete from his section prohibiting FDIC members from paying interest by absorbing exchange. This is extremely important to small banks of South Carolina. Very few could exist without exchange. I must repeat that this is most important and needs immediate attention.

E. R. ALEXANDER, Jr.,
Manager Woodruff State Bank.

WOODRUFF STATE BANK,
Woodruff, S. C., February 11, 1957.

HON. J. STROM THURMOND,
State of South Carolina,
Senate Office Building, Washington, D. C.

DEAR SENATOR THURMOND: This is in protest to the bill before the Senate Banking and Currency Committee to the effect of amending the FDIC Act, section 26, title 3 to prohibit the paying of interest through the absorption of exchange.

I feel that since you are from South Carolina, and this being predominately an agricultural State, you appreciate the condition our small communities are in at the present time. Banks in large cities have many ways in which they make their existence profitable. In the small communities of this State, of which Woodruff certainly is a good example, these means of support are few. I am sure this situation exists all over the South and in the other agricultural States of our country as well.

When the income of a bank is curtailed the whole structure of the bank is in jeopardy. Without income, banks, as any other business, cannot operate. When this operation ceases to exist the whole community is at a loss. After all, banks have but two things to sell—service and safety—and any community is static without these two. We bankers are proud of the service we are able to give our communities and at all times we stand ready to render more and better service to our customers. I feel that the amendment substituted will be a decided detriment to banks in small agricultural communities.

Therefore, I ask that you oppose the inclusion of this proposed change with all the strength and means at your disposal.

Yours very truly,

E. R. ALEXANDER, Jr., *Manager.*

UNION, S. C., *February 15, 1957.*

HON. STROM THURMOND,
United States Senator, Washington, D. C.:

Imperative you don't wait for Robertson bill to reach the Senate floor. Ask him to delete from his bill section prohibiting FDIC insured nonmember banks from absorbing exchange. Very important to small country banks in South Carolina. His committee votes on this February 25. Please do this immediately for your small country banks constituents. Many cannot exist without exchange.

HARRY M. ARTHUR.

BANK OF MANCHESTER,
MANCHESTER, GA., *February 15, 1957.*

Senator A. WILLIS ROBERTSON,
United States Senate,
Washington, D. C.

DEAR SENATOR ROBERTSON: We understand that in your proposed Financial Institutions Act of 1957 that the Federal Deposit Insurance Act would be changed. Title III, section 26, of the Robertson bill reads in part as follows: "No insured bank shall directly or indirectly by any device pay interest on any deposit which is payable on demand and for such purpose the Administrator may define the term demand deposits." There is a difference between the above and the present Federal Deposit Insurance Act, section 18, subsection (g) which reads in part as follows: "The Board of Directors shall by regulation prohibit the payment of interest on demand deposits in insured nonmember banks and for such purpose it may define the term demand deposits."

It is through the power to issue regulations that the FDIC has permitted nonmember State banks to absorb exchange. If we could not absorb exchange it would be extremely difficult to charge exchange. Many of our city friends who are members of the Federal Reserve System think nothing of entertaining their customers regularly. Those of us who live in small towns have rather limited facilities for entertaining and thus find the practice of absorbing exchange for our good customers an excellent way of promoting good public relations without running up large expense accounts.

It appears that some of the effects of section 26 of your proposed FDIC Act on insured nonmember State banks would be as follows:

(1) Create bad public relations.

(2) Tend to shrink deposits in our smaller banks because of the relatively greater appeal that larger par banks in the surrounding area would have through entertainment, etc.

(3) Fewer private institutional loans to small-business men and farmers because with less deposits we small-town bankers would have to reduce our loans.

(4) Transfer entirely the cost of banking services in almost 1,900 communities to the people in these communities least able to pay for such services. The merchants, distributors, and manufacturers who are now selling in areas such as ours are through the payment of exchange helping the little people in our area to have a bank which is progressive at a cost that they can afford. As a collection agency and a developer of customers for the distributors and manufacturers, we feel that we small banks are entitled to some help.

(5) A backward step in the development of hundreds of small towns and rural communities.

(6) A service charge in about 1,900 small communities which would discourage the use of banking services, thrift and sound financial development.

(7) A lower caliber of bank personnel, efficiency, service and safety.

In view of the above and many other undesirable results of what is now proposed in section 26 of title III, we urgently request you to amend this section in such a manner that the FDIC will have the authority to regulate its members to the best interest of the country as a whole.

We would like for this letter to become a matter of record with your subcommittee.

Very truly yours,

CLAUDE A. BRAY,
Executive Vice President and Cashier.

DENVER, COLO., *February 12, 1957.*

Hon. A. WILLIS ROBERTSON,
Senate Office Building, Washington, D. C.

DEAR SENATOR ROBERTSON: I understand your committee is considering legislation that will eliminate mandatory cumulative voting in the election of national banks. Please have this letter inserted in the hearings concerning the Financial Institutions Act of 1957.

Mandatory cumulative voting was one of the means selected in the early 1930's to put our banking system on a sound footing. It certainly would be unwise to eliminate a safeguard protecting the soundness of our national banking system. A half million people now enjoy this democratic voting right. In fact, it is considered by investors to be a very valuable property right. The destruction of this property right not only will eliminate a valuable asset of the public stockholders but it also will permit bank managers to once again engage in the type of practices that brought our banking system to the brink of disaster in 1932.

Twice before your committee has heard testimony on mandatory cumulative voting and not a single case has been brought to your attention where cumulative voting has operated unfavorably to the bank. True, it may operate unfavorably to some bank presidents who desire to engage in practices that the public stockholders will not permit if they know of them. Through mandatory cumulative voting independent directors are elected who can watch the way the president operates the affairs of the bank.

Please do not destroy mandatory cumulative voting for the sake of pleasing some self-seeking bank presidents who wish to obtain monopolistic control for their own selfish ends.

Respectfully yours,

JAMES BRENNAN,
An Owner of Stock in a National Bank.

TARHEEL BANK & TRUST CO.,
Gatesville, N. C., February 14, 1957.

Senator A. WILLIS ROBERTSON,
United States Senate, Washington, D. C.

DEAR SENATOR ROBERTSON: There are approximately 214 small nonmember banks in North Carolina which derive a considerable part of their earnings from exchange.

We operate three of these banks in rural northeastern North Carolina at Gatesville, population 315, Lewiston, population 339, and at Winton, population 812.

Other small banks are in the same situation. That is, they depend to a large extent on the collection of exchange in order to keep in a healthy condition.

Should your banking bill pass with section 26 under title III as now written, it is our opinion that the collection of exchange would soon be a thing of the past.

Many of these small banks in our State might be forced to close, and the people in those areas who are dependent on them for banking services, would then be without such services.

On account of this situation, we feel that the past Congress acted wisely in giving the FDIC power of free decision in the matter of absorbing exchange, and they were wise in using that discretion in promulgating a regulation to do so. There appears to us to be no need for changing this at the present time and thereby jeopardize our capacity to serve our customers.

We respectfully urge you to leave the law on this point as it is now written.

Yours very truly,

PAUL F. EDMOND, *Executive Vice President.*

CITIZENS BANK & TRUST CO.,
Andrews, N. C., February 16, 1957.

Re Financial Institutions Act of 1957

Senator A. WILLIS ROBERTSON,
United States Senate, Washington, D. C.

DEAR SENATOR ROBERTSON: We operate four small banking offices in western North Carolina under the name of Citizens Bank & Trust Co. The bank was organized in Andrews in 1924, Murphy was opened in 1933, Robbinsville in 1943, and Hayesville in 1945. Since inception, we have been providing banking credit to the small-business men and farmers in the western counties of our State. In order to properly operate this bank, we are forced to lean heavily on income we derive from exchange.

I understand that you are chairman of a subcommittee holding hearings on the new banking bill which proposes to invoke by indirection the effect of regulation Q and now applying to Federal Reserve member banks but not insured nonmember banks. We hope that you will not allow this handicap to be placed on our bank and other small institutions similar to ours. It will be the true wedge to do away with exchange. We could hardly charge exchange to our customers unless we were in a position to absorb exchange.

Our institution respectfully requests that you delete from the bill section 26 under title 3 and insert in its place the wording of section 18 subsection G of the present Federal Deposit Insurance Corporation Act.

Yours very truly,

PERCY B. FEREBEE, *President.*

Andrews, N. C., population, 1,397; Hayesville, N. C., population 356; Murphy, N. C., population 2,433; Robbinsville, N. C., population, 515.

THE CITIZENS BANK,
Micro, N. C., February 14, 1957.

Senator A. WILLIS ROBERTSON,
Senate Office Building, Washington, D. C.

DEAR SENATOR ROBERTSON: We operate 2 banking offices in the State of North Carolina, one located in Micro (population 310), and another located in Princeton (population 608). The combined deposits of these two offices during our peak season are around $1,800,000 and in our low season, approximately $1,200,000. Our bank was chartered in Micro in 1915, and we opened our Princeton office in 1934. We have, over a period of years, made what we believe to be a major contribution in the development of these two small towns and in serving the small-business men and farmers in the surrounding area.

We implore you not to introduce a bill containing a section such as No. 26 of title III of your proposed Financial Institutions Act of 1957. The enactment of such legislation will adversely affect our small institution and its capacity to render a worthwhile service. Almost all of our net revenues are derived from the collection of exchange. It would be impossible to increase service charges so that it would give us any substantial relief in the event we lost our exchange revenue. Of course, our bank, along with many other small institutions, has relied upon exchange as an important source of income. We understand that section 26 referred to above would not directly prohibit us from collecting exchange, but we would be terribly handicapped by the provisions of said section if we were deprived of absorbing exchange because we could not hope to retain the business of our best commercial customers if we did not treat exchange as a two-way matter. It is also our opinion that if we should be deprived of absorbing exchange, it would only be a matter of time before we would be forced to give up collecting exchange. We are certain that there are many other institutions throughout North Carolina and in other agricultural States that are confronted with the same problem that we are in the matter of collecting and absorbing exchange.

Over a period of 36 years, the Citizens Bank has been operated on a most economical, basis particularly in respect to the compensation of its personnel and in that way, and with the income from exchange, has been able to keep its capital funds in a ratio satisfactory to its deposits.

Under the provisions of section 26, the continuation of this policy of keeping capital funds in a safe ratio to deposits cannot be maintained despite our very low operating expenses.

In conclusion, we respectfully request you to rewrite section 26 of title III of your proposed bill in such a manner that the FDIC will have the same authority to deal with this matter as it now has. I hope very much that this letter can be inserted in the subcommittee hearings on the bill.

Yours truly,

H. M. FITZGERALD, *President.*

CLINTON, S. C., *February 12, 1957.*

Hon. STROM THURMOND,
United States Senate:

Request you urge elimination of provision in Robertson bill prohibiting insured nonmember banks from absorbing exchange.

BANK OF CLINTON,
R. P. HAMER, *President.*

THE LUCAMA-KENLY BANK,
Lucama, N. C., February 16, 1957.

Senator A. WILLIS ROBERTSON,
Senate Office Building, Washington, D. C.

DEAR SENATOR ROBERTSON: Reference is made to title III, section 26 of your bill now before the Senate Banking and Currency Committee. This section should be changed so as to conform to section 18, subsection g of the present Federal Deposit Insurance Act.

The Federal Deposit Insurance Corporation has, by regulation, in the past permitted insured nonmember State banks to absorb exchange by ruling that the absorption of exchange was not the payment of interest on demand deposits. We heartily concur with the position taken by the FDIC and the North Carolina State Legislature and Banking Commission in respect to this practice. We contend that the absorption of exchange for a customer does not represent the payment of interest on demand deposits any more than the numerous services rendered by metropolitan banks who furnish their customers with free parking, free personalized checks, free business information and entertainment, which in many instances, amounts to hundreds and thousands of dollars each year.

The absorption and charging of exchange has been an accepted practice in the banking industry in this country since its inception. The passage of section 26 of your bill will, we believe, jeopardize the banking industry in small towns, particularly in agricultural areas of this and other States. The practice of absorption of exchange is, in our opinion, a necessary element in the continued acceptance of the practice of charging exchange.

It is our honest opinion that no real benefit will be derived from the passage of section 26 as now written, but on the contrary, irreparable harm and damage will be done small insured nonmember banks, small towns and communities, small-business men and agriculture. Before you proceed with this matter further, we earnestly ask you to review the effects which might result from the passage of section 26 as now written.

1. Make banking unprofitable and unattractive in our and in hundreds of other small agricultural communities located throughout the country.
2. Reduce the banking services and credit available to farmers and small-business men.
3. Promote the liquidation and merger of many hundreds of small banks.
4. Greatly increase the likelihood of failure of small banks by taking away from them their best source of income.
5. Increase the cost as well as the availability of credit to farmers and small-business men at a time when they can least afford to assume such additional cost. Farmers have been hard hit by increasing costs, acreage curtailment, and declining support prices for the past 3 years.
6. Prevent small insured nonmember State banks from attracting the high type of personnel which is a must if they are to be operating in a manner which would be conducive to the best interest of their communities.
7. Take away from the small insured nonmember State banks one of their few competitive advantages in comparison with banks located in metropolitan areas. Without this advantage, more and more of our deposits will flow into the city banks and, inevitably, result in our giving less and less service to our community.

Please make this letter a part of the minutes of your subcommittee hearings.

Sincerely yours,

S. E. HIGH, JR., *President.*

DENVER, COLO., *February 14, 1957.*

Hon. A. WILLIS ROBERTSON,
Senate Office Building,
Washington, D. C.

DEAR SIR: As a stockholder in one of the national banks of Denver I am interested that the mandatory cumulative voting law be retained. Abolition of it would be good only for bank presidents and not for the stockholders like myself who are actual owners of the bank, and who have our savings invested therein.

I would appreciate very much having this letter made a part of the record in the Financial Institutions Act of 1957.

Sincerely yours,

SIDNEY S. JACOBS.

THE COMMERCIAL BANK,
Douglasville, Ga.

Senator A. WILLIS ROBERTSON,
United States Senate, Washington, D. C.

DEAR SENATOR ROBERTSON: It has come to our attention that you are in the process of introducing a bill which would prohibit the absorption of exchange and eventually lead to universal par clearance (reference sec. 26, title III). Such a change in the FDIC Act would, in our opinion, result in many undesirable effects on the banking industry in the United States and particularly in agricultural areas located predominantly in the South and North Central States.

In view of the seriousness of this proposed change, I would like to take this opportunity to list a few of the disadvantages of this proposed change.

(1) That many insured nonmember State banks will be unable in the future to maintain adequate capital funds and reserves in relationship to their increasing deposit liability as result of inflationary pressures similar to those which have existed in this country since before 1940. Should this occur, the entire banking structure of the country will be weakened because the FDIC will have considerably more exposure than presently exists.

(2) That banks presently charging exchange will lose this irreplaceable source of income and many of them will either liquidate, merge with larger institutions, or seriously reduce the services they are now rendering.

(3) That the dual banking system will, as an effective system, cease to exist and there will be a very serious concentration of the control of banking facilities and credit in the States in which the practice of absorption and the charging of exchange is practiced on a broad scale.

(4) That State nonmember insured banks will lose the principal benefits of being a nonmember bank without receiving the benefits of being a member of the Federal Reserve.

(5) That the city industrialists and manufacturers will receive a windfall profit at the expense of the small towns and rural communities in which nonpar banks are located.

It will be appreciated if you will make the contents of this letter a part of the minutes of the hearings of your subcommittee.

Sincerely,

W. D. LLOYD, *President.*

FLAGLER FEDERAL SAVINGS AND LOAN ASSOCIATION OF MIAMI,
Miami, Fla., February 15, 1957.

Mr. DONALD ROGERS,
Counsel, Committee on Banking and Currency, United States Senate,
Senate Office Building, Washington, D. C.

DEAR MR. ROGERS: Your letter of January 23 in response to my letter of January 11 was received. As you will recall, I telephoned you to advise that I would be in Mexico City on February 8, 1957, and would file a letter in lieu of my testimony.

Mr. Henry Bubb, of the United States Savings & Loan League, and Mr. James Bent, of the National Savings & Loan League, have presented the views of the savings and loan industry very capably and particularly expressed their opposition (and the opposition of the industry) to any provision of the act that would tie the hands of the Federal Home Loan Bank Board in the granting of branches to savings and loan associations.

I have also read the report together with minority view (Calendar No. 522, Rept. No. 518) covering Federal savings and loan branches and find that the minority view of Senators Douglas, Morse, and Lehman expresses my opinion fully.

However, I would like for the committee to have clearly the situation before it as it affects Florida and a number of other States. In the State of Florida, branch banking is prohibited but there is no prohibition against group banking or chain banking. As a result, a number of group banks with interlocking directors have sprung up over the State. Enclosed is the statement of the Florida national group of banks showing 25 banks over the various cities of the State, stretching from Key West to Fernandino Beach to Pensacola; and more recently the Sotille banking division (group banking) that is locally operated and covers 7 banks and I believe the eighth in the recent control of the Curtiss National Bank of Miami Springs, Fla. If you will notice in both of these banking groups or chains, the control lies in one person or one group with interlocking directors throughout the group system.

I understand the same situation holds true with other group banking in Jacksonville, Fla., and other cities in Florida.

Commercial banks for many years neglected the savings. As a result, the Home Loan Bank System came into existence. Savings and loan associations have done a tremendous job in the Nation in the promotion of thrift and home financing through the stimulus of savings. The commercial banks have been agitating against the savings and loan associations to the extent of trying to prohibit branches of savings and loan associations in States that prohibit it. It is not fair, democratic, or American to permit commercial banks on one hand to have group and chain banking with interlocking directors, and prohibit savings and loan associations to have branches in the very same State where the commercial banks operate outside the technical provisions of the State law.

To show you how far the commercial banks have gone in their agitation against savings and loan associations, the official State banking organization here has published a pamphlet (which is now being distributed by one of the local banks) attacking the Federal Savings and Loan Insurance Corporation and savings and loan associations as compared to commercial banks and the Federal Deposit Insurance Corporation. Enclosed is one of the pamphlets that was obtained from a local bank this date. There is room in the economy of America for commercial banks, life-insurance companies, and savings and loan associations without one or the other reflecting on the other and trying to restrict the other's operations. If the commercial banks are permitted to have group banking and chain banking in a State that prohibits branch banking, then savings and loan associations should have the same privilege whether it be by branch banking or otherwise. In addition, I think pamphleteering by the official organ of a State banking association of the kind enclosed is detrimental to the best interests of the United States Government and will reflect on the financial stability of this Government. One cannot attack one agency of the Government without hurting the other, another agency of the Government.

Congressman Multer introduced a bill in the House of Representatives on March 1, 1955, known as H. R. 4527, in which a proviso was made to exclude any prohibition against branch banking in States which permitted the practice of chain, group, or affiliated banking to exist.

It is the position of the writer that any restriction on the granting of branches should be left in the wise and sound discretion of the Federal Home Loan Bank Board as it is today, but that in any event none should be made in States that prohibit branch banking where group or chain banking is permitted to flourish.

Sincerely yours,

PAUL H. MARKS, *President.*

(The material attached to Mr. Marks' statement will be found in the files of the committee.)

STATE PLANTERS BANK,
WALNUT COVE, N. C., *February 15, 1957.*

Senator A. WILLIS ROBERTSON,
United States Senate,
Washington, D. C.

DEAR SENATOR: We operate the State Planters Bank at Walnut Cove (population 1,132) and King (population 800), North Carolina. We serve a rural area which would be without banking service if it was not for our operations.

There are many similar cases in our State. We have very concerned over section 26, title III, of your new proposed banking law. It would seriously cripple our operation and comparable banks throughout our State.

A large part of our net revenues are derived from exchange. While section 26 applies only to the absorption of exchange, we feel that it would be an opening wedge to force us to clear at par.

The FDIC is familiar with our operation and has seen fit to exempt the absorption of exchange. This ruling keeps our small country nonmember banks in a healthy condition.

We hope that you will not change this section, especially in view of the rising operational costs and other headaches which we are facing more and more each day. We urge you to strike from your bill section 26 and leave the law as it is now written.

Yours very truly,

WILLIAM F. MARSHALL, *Chairman.*

DENVER, COLO., *February 12, 1957.*

Hon. A. WILLIS ROBERTSON,
Senate Office Building,
Washington, D. C.

DEAR SENATOR ROBERTSON: The elimination of mandatory cumulative voting will permit bank presidents to select directors on a basis of discrimination.

The elimination of mandatory cumulative voting will destroy a property right now enjoyed by tens of thousands of American stockholders.

The elimination of mandatory cumulative voting will mean that the bank can be run in the interest of a few wealthy and powerful men instead of for the majority of stockholders.

The elimination of mandatory cumulative voting eliminates the bill of rights now incorporated in our national banking system.

The elimination of mandatory cumulative voting will mean that the market value of bank stocks will fall.

The elimination of mandatory cumulative voting will mean more monopolistic power in the hands of a few men.

The elimination of mandatory cumulative voting will mean that depositors and stockholders will not have adequate protection to see that their bank is well managed.

For the foregoing reasons, please keep mandatory cumulative voting on the statute books.

I would appreciate it if you would have this letter made a part of the testimony regarding the Financial Institutions Act of 1957.

Respectfully yours,

JOSEPH C. MURRAY.

DENVER, COLO., *February 12, 1957.*

Hon. A. WILLIS ROBERTSON,
Senate Office Building,
Washington, D. C.

DEAR SENATOR ROBERTSON: The only ones wishing to destroy cumulative voting are a few bank managers who do not trust the owners of our national banks and feel that they should not be watched by the representatives of the public stockholders as to the way in which they carry out their duties. These bank presidents prefer to have dummy directors on the boards who will be yes men to their every action and desire rather than to have independent directors who have a considerable amount of money invested in the bank and represent other people who have money invested in the bank and will, of course, wish to have the bank run in a sound manner.

Please do not be influenced by the desires of these few powerful bank presidents who wish to take away rights from their own stockholders so that they will gain monopolistic power.

I would like to have my opinion expressed here inserted in the record of the Financial Institutions Act of 1957.

Respectfully yours,

THOMAS E. MURRAY.

NATIONAL ASSOCIATION OF INSURANCE AGENTS,
New York, N. Y., February 18, 1957.

Re Financial Institutions Act of 1957

Hon. J. W. FULBRIGHT,
Chairman, Committee on Banking and Currency,
United States Senate, Washington, D. C.

DEAR MR. CHAIRMAN: This representation is made on behalf of the National Association of Insurance Agents, a voluntary membership association numbering in excess of 32,000 insurance agency members. Included in this membership are over 100,000 individuals, duly licensed by the respective States, who are proprietors, partners, or corporate principals in the firms and corporations which comprise said insurance agency members. This organization is comprised of independent businessmen who specialize in the production and servicing of policies of fire, casualty, surety, marine, and all other lines of general insurance for clients ranging from the smallest householder or automobile owner to the largest industrial corporation.

We have been advised that the Committee on Banking and Currency is now considering a bill to amend and revise the statutes governing financial institutions and credit, which enactment may be cited as the Financial Institutions Act of 1957. This association commends the efforts of the Committee on Banking and Currency to improve the laws pertaining to financial institutions, but at the same time we feel compelled to protest a proposal to extend the powers of national banks to engage in the business of insurance, presently contained in the committee print of January 7, 1957, title I, chapter 1, section 45, entitled "Acting as Insurance Agent or Broker." This proposal would allow a national bank to engage in business as an insurance agent in towns with a population greater than 5,000, which is the population limit now contained in the present statute, title 12, section 92, United States Code.

The original purpose in the enactment of section 92 was to enable national banks to procure needed insurance covering the subject of a loan in those areas where insurance facilities may have been lacking. This was deemed essential in order to fill a void in areas with very small population. However, there would be no sound basis for extending authorization for national banks to act as insurance agents in those towns with a population greater than 5,000, since there could be no showing of any necessity on the part of a national bank to act as an insurance agent in order to procure required insurance for its borrowers. Those coverages are readily available through established insurance agents.

This association does not believe that an insurance business is a proper function to be carried on by national banks. Because of the complexities of the banking field and the expanding functions of banking in the American economy, it is axiomatic that national banks should be primarily concerned with the basic requirements of sound banking practices and that activities of national banks should be limited to rendering of service within the well-defined limits of the banking business.

A sound banking procedure is of the highest importance to the economy of the country and to the welfare of all citizens. Concentration of activities within the highly technical framework of banking, without extension into unrelated fields, would best serve the economy and public interest. It is, of course, of great importance that the security of loans made by national banks be fully protected by adequate insurance. It is the primary function of the insurance industry, and specifically members of this association, to render the specialized service necessary to effect such full protection.

Like banking, insurance is a highly technical business. True insurance protection is best attained through those persons who make a specialty of the insurance business. Successful operation of an insurance agency and complete protection of the public are best performed by insurance men. There are obvious dangers in allowing an extension of the performance of insurance functions merely as an unrelated sideline to a banking business.

An example of dangers to national banks in pursuing the unrelated business of insurance would be the legal liabilities to which the bank's assets would be exposed in performing insurance functions. For example, the status of an insurance agent carries with it a multitude of common law liabilities to the company as well as to the assured. Numerous decisions are found in the law imposing heavy liability upon insurance agents for failure to exercise such skill and diligence as the law requires of one who serves the insurance industry and the public as an insurance agent.

This association firmly believes that it is detrimental to the best interests of the public to further extend the right of national banks to carry on an insurance business. Experience has proved that those who are in a position to influence placement of insurance through the power of credit may have the tendency to influence, or even coerce, the borrower to place insurance covering the security of loans through a particular channel. This interferes with the privilege of a borrower to select his own agent in the placing of insurance, and the right to select the best-qualified insurance adviser in all of his insurance needs.

We strongly urge the deletion of the aforesaid section 45 of title I, chapter 1, in the enactment of the Financial Institutions Act of 1957. The public interest is best served by the conduct of a banking business by financial institutions constituted for that purpose, and insurance functions conducted by those who are primarily in the insurance business.

Respectfully submitted.

ROBERT E. BATTLES, *President.*

WILLIAMS BANKING CO.,
Rhine, Ga., February 15, 1957.

Senator A. WILLIS ROBERTSON,
United States Senate,
Washington, D. C.

DEAR SENATOR ROBERTSON: It has come to our attention that you are in the process of introducing a bill which would prohiibt the absorption of exchange and eventually lead to universal par clearance (reference sec. 26, title III). Such a change in the FDIC Act would, in our opinion, result in many undesirable effects on the banking industry in the United States and particularly in agricultural areas located predominately in the South and North-Central States.

In view of the seriousness of this proposed change, I would like to take this opportunity to list a few of the disadvantages of this proposed change.

(1) That many insured nonmember State banks will be unable in the future to maintain adequate capital funds and reserves in relationship to their increasing deposit liability as result of inflationary pressures similar to those which have existed in this country since before 1940. Should this occur, the entire banking structure of the country will be weakened because the FDIC will have considerably more exposure than presently exists.

(2) That banks presently charging exchange will lose this irreplaceable source of income and many of them will either liquidate, merge with larger institutions, or seriously reduce the services they are now rendering.

(3) That the dual banking system will, as an effective system cease to exist and there will be a very serious concentration of the control of banking facilities and credit in the States in which the practice of absorption and the charging of exchange is practiced on a broad scale.

(4) That State nonmember insured banks will lose the principal benefits of being a nonmember bank without receiving the benefits of being a member of the Federal Reserve.

(5) That the city industrialists and manufacturers will receive a windfall profit at the expense of the small towns and rural communities in which nonpar banks are located.

It will be appreciated if you will make the contents of this letter a part of the minutes of the hearings of your subcommittee.

Sincerely,

JIMMY D. NESMITH, *President.*

THE SECURITY BANK,
Edgefield, S. C., February 8, 1957.

Hon. J. STROM THURMOND,
United States Senate,
Washington, D. C.

DEAR STROM: Enclosed is a copy of telegram sent to Hon. John Sparkman today protesting the amendment of FDIC Act, section 26, title 3, to prohibit the absorption of exchange. More than 1,800 nonpar banks, most of them smaller country banks, would be affected by this amendment.

It would, in our case for example, eliminate approximately one-third of our net profit. With greatly increased operating costs due to inflated prices and wages, increased cost of money, it would be most untimely and would work extreme hardship on the country banks.

Please use all of your influence to defeat this move.

With kind personal regards,

Yours sincerely,

R. H. NORRIS, *President.*

THE BANK OF PINE LEVEL,
Pine Level, N. C., February 16, 1957.

Senator A. WILLIS ROBERTSON,
Senate Office Building, Washington, D. C.

DEAR SENATOR ROBERTSON: Reference is made to your proposed Financial Institutions Act of 1957. It is our opinion that section 26 of title III of this proposed act should be amended so as to conform to section 18, subsection g, of the present Federal Deposit Insurance Corporation Act.

The present Federal Deposit Insurance Corporation Act permits the Board of Directors, by regulation, to prohibit the payment of interest on demand deposits to insured nonmember banks; whereas in section 26 of your proposed act it is specifically stated that, "No insured bank shall directly or indirectly, by any device, pay any interest on any deposit which is payable on demand, and for such purpose the Administrator may definite the term 'demand deposits'." The Federal Deposit Insurance Corporation has, by the use of its regulatory power, under the present law, specifically exempted the absorption of exchange from being construed as the payment of interest.

Should your proposed act be adopted, we believe that we will eventually be forced to clear at par and thus give up exchange, which is our most important source of income. In our case, and in respect to many hundreds of small nonpar banks, this loss of income cannot now or at a later date be replaced by an upward revision of our service charges because the activity to support such a revenue from service charges simply is not available in our or in these communities.

If your section is approved as now written we, along with many other small banks, will be damaged beyond repair. Before continuing with this matter as is now proposed, please think over the following things which might happen to our bank and community, as well as to similar banks and communities located in agricultural areas:

1. Being deprived the right, which is now permitted by the Federal Deposit Insurance Corporation and by the State of North Carolina, to absorb exchange, we will find it increasingly difficult, if not impossible, to collect exchange. Our customers understand that we must charge exchange in order to exist. However, many of our best customers feel very strongly, since we are collecting exchange, that we should absorb some of their costs. The net effect of what you are proposing appears to be to force us to give our right to absorb and collect exchange and thus the one source of income which has made the existence of this institution possible.

2. The services and credit which we are now providing for the farmers in this area will be terribly hurt and it is doubted that anything short of an outright Government subsidy could replace this loss.

3. Without profits our bank and similar banks will over a period of time be weakened, and greatly increase the liability of the FDIC and, therefore, weaken the banking structure of the United States.

4. Without some customer appeal, the small banks in agricultural areas will become a much less attractive place for the large depositor to do business and thus our total deposits and resources will be seriously curtailed, thereby reducing the amount of credit which we can safely make available to the farmers in this area.

5. Inasmuch as most of our loans are made on a seasonal basis, we are not able to obtain anything like the effective rate of interest on our loans that the larger banks are able to obtain on personal and installment type credit, which loans are paid weekly or monthly. This fact, along with your proposal, makes it impossible for me to see or understand how this institution could continue to be operated.

Please enter this statement in the minutes of your subcommittee hearing.

In the interest of the country as a whole, and particularly in the interest of the small-business men and small farmers, please recommend to your committee that section 26 of title III be changed in order that we may continue to absorb and collect exchange.

Sincerely yours,

W. B. OLIVER, *President.*

DENVER, COLO., *February 12, 1957.*

Hon. A. WILLIS ROBERTSON,
Senate Office Building, Washington, D. C.

DEAR SENATOR ROBERTSON: Under our present system of electing directors of our national banks, we have majority control and minority representation. The elimination of cumulative voting will mean that majority control will be changed to monopoly control, and minority representation as it now exists will be obliterated. In short, we will take a big step backward concerning democracy in our national banks.

Cumulative voting is democratic for it gives the public stockholders the right to have representation on the boards of the banks which they own. We need more democracy and less monopolistic power in our banking system. The elimination of cumulative voting puts the bank managers in a position of monopolistic power over the banks which is very detrimental to our banking system.

Please have this communication inserted into the hearings regarding the Financial Institutions Act of 1957.

Very truly yours,

RUTH PANKOSKI,
A National Bank Stockholder.

ANDREWS BANK & TRUST CO.,
Andrews, S. C., February 15, 1957.

Senator J. STROM THURMOND,
United States Senate, Washington, D. C.

DEAR SENATOR THURMOND: Enclosed you will find copy of letter to Senator Olin D. oJhnston in regard to proposed legislation which is now being considered by a subcommittee of the Banking and Currency Committee headed by Senator A. Willis Robertson of Virginia. I am very much opposed to any change in the present laws and regulations of the Federal Deposit Insurance Corporation pertaining to absorption of exchange by State nonmember insured banks.

Anything you might do in our behalf, as well as the many small State banks in South Carolina would be appreciated.

With kind personal regards to you and Mrs. Thurmond, I remain,

Sincerely yours,

A. H. PARSONS,
Executive Vice President.

ANDREWS BANK & TRUST CO.,
Andrews, S. C. February 15, 1957.

Senator OLIN D. JOHNSTON,
United States Senate, Washington, D. C.

DEAR SENATOR JOHNSTON: We have recently learned that Senator A. Willis Robertson, who is chairman of a subcommittee of the Senate Banking and Currency Committee, has been holding hearings prior to introducing a new Financial Institutions Act. We have learned that in title III, section 26, there is a provision which would deny the FDIC the authority to regulate the payment of interest on demand deposits and would, in fact, place all insured nonmember State banks under the same restrictions as banks which are members of the Federal Reserve System. The fact is, that the same wording and terminology as is now used in the Federal Reserve Act pertaining to this subject, is being written into section 26 of the proposed act.

Should section 26 of the new Financial Institutions Act become law, approximately 80 country banks here in South Carolina, to say nothing of the nineteen-hundred-odd insured nonmember State banks located throughout the country, will be adversely affected because:

(1) The FDIC will be deprived of its authority to establish appropriate regulations pertaining to the payment of interest on demand deposits.

(2) Under present regulations issued by the FDIC, an insured nonmember State bank is permitted to absorb exchange for its customers without having this practice deemed a payment of interest on demand deposits.

(3) An institution which could not absorb exchange would find it most difficult, and virtually impossible, to charge exchange. And, therefore, the passage of this section 26 as now written will, in our opinion, result in forcing nonmember State banks to give up their practice of charging exchange, which is their most reliable, and in many cases their largest, source of income.

The repercussions from the above would be most serious, and in the interest of time we will list only a few:

(1) Tend to do away with the dual banking system, and to deny and violate States rights in formulating the laws, regulations, and procedures to be followed by State-chartered institutions.

(2) Tend to cause a concentration of ownership and control of the banking facilities in this and other States in which the practice of exchange is broadly employed.

(3) Reduce the facilities and services now available to many of our farmers and small-business men, because they will find their bank in a weakened condition and with less money available to meet the needs of its customers.

(4) Deprive the insured nonmember State banks of one of their few advantages, while at the same time not giving them the benefits to be derived from being a member of the Federal Reserve, such as the rediscount privilege and the free shipment of currency.

(5) Tend to weaken the entire financial structure of our State and the country by depriving these nineteen-hundred-odd nonmember banks of a large portion of the net income which they have been able to earn in time past. If the banks are unprofitable, they inevitably will tend to become unsafe. We all have losses, and must have sufficient income to absorb such losses in the future.

We urge you to make a determined effort to get section 26 of title III of the proposed Federal Deposit Insurance Act rewritten to conform with section 18, subsection G, of the present Federal Deposit Insurance Act.

Please contact Senator Robertson no later than Saturday, February 16, and have this statement made a part of the minutes of the hearings held by his subcommittee. The minutes will close on this date.

With every good wish, I am,

Yours truly,

A. H. PARSONS,
Executive Vice President.

COMMERCIAL STATE BANK,
Laurel Hill, N. C., February 15, 1957.

Senator SAM J. ERVIN, Jr.,
United States Senate,
Washington, D. C.

DEAR SENATOR ERVIN: It is our understanding that the Financial Institutions Act of 1957, in title III, section 26, denies the FDIC the authority to regulate the payment of interest on demand deposits.

Such a change in my opinion would prohibit a small insured nonmember bank such as ours from absorbing exchange for its customers. Many of our customers would naturally resent the fact that we were charging exchange, but at the same time could not absorb any exchange for them even if their account justified such consideration on our part.

We believe that this proposed change is a circuitous method of denying small nonmember banks from charging exchange and of eventually causing all banks to go into Federal Reserve System.

It is our sincere conviction that should this section of title III be passed by your subcommittee and eventually become law, that the repercussions would be far reaching and disastrous in regards to the banking industry as it now exists in this country. A few of these probable repercussions are listed below for your consideration:

(1) That many nonpar banks would be eventually forced on par and thereby lose one of their best sources of income which could not be in many cases replaced by the employment of any other method short of assuming hazardous risks in the loan portfolio or by the investment in other poor quality securities.

(2) Without exchange literally hundreds of banks which are now building adequate reserves and capital funds to safeguard its depositors and provide

the crying need for service, will in time lose their usefulness in their trade areas.

(3) Without exchange and without the possibility of recapturing this income from a service charge because of the limited commercial activity and deposits in areas such as ours, many of we small insured nonmember bankers will be forced to get out of the banking business. We probably won't close the bank in our town but would operate more like a teller's window employing only clerks with very limited authority and therefore be unable to serve the economic needs of our area.

We respectfully request you to enter this statement in the minutes of the subcommittee hearings.

Yours very truly,

COMMERCIAL STATE BANK,
EDWIN PATE, President.

BANK OF VARINA,
Varina, N. C., February 16, 1957.

Senator A. WILLIS ROBERTSON,
United States Senate, Washington, D. C.

DEAR SENATOR ROBERTSON: Title III, section 26 of a new banking bill now before your subcommittee should be amended in such a manner as to permit insured nonmember State banks to continue absorbing exchange.

The right to charge exchange carries with it, in our opinion, an obligation to absorb exchange for customers whose accounts justify same. Our customers approve of the practice of charging exchange and understand that it is absolutely necessary for us to obtain this revenue if we are to continue to operate our bank. On the other hand, we are confident that they would take a dim view of our charging exchange and not absorbing exchange for them. We cannot help but feel that this situation does exist in most of the nineteen hundred-odd insured nonmember State banks located predominately in agricultural areas. It has never been our opinion that the absorption of exchange was in effect the payment of interest but was rather a service which we were rendering such as larger banks render their customers when they provide them with fee personalized checks, parking facilities, extensive entertainment, and a multitude of other services at no direct cost to the customer.

Exchange and, therefore, the power to absorb exchange is the lifeblood of our small institutions. We could not exist without it and our community and its small businessmen and farmers will be greatly injured unless section 26 is revised.

During the past 3 years, farmers and small-business men have been caught between rising costs and a reduction in farm commodity prices. Many of these farmers need more credit and banking service than they have needed since the 1930 depression. Destroying the small banks which have, in our opinion, provided more credit and service to the farmer than any other private source is definitely not the way to maintain our present standard of living, full employment, and the general well-being of the rural areas of this State as well as other States.

During the past 10 years, we have been beset by continuing competition from savings and loan associations located in nearby cities for our best savings customers to say nothing of the quantity of local savings which have gone into series E and other savings bonds. None of these funds which are now invested in shares of savings and loan associations and United States Government bonds are available to finance the small-business man and farmers located in our trade areas. To take away from us one of our best selling points in the solicitation of accounts seems to us to be most unfortunate because many of these accounts will find their way into the larger banks.

The fact is that if section 26 should become law, I am at a loss as to how this institution and many other similar institutions will be able to continue in operation and provide the necessary services to the people in our and their areas.

We will thank you to make this letter a part of the minutes of your Hearing.

Respectfully,

T. E. PERSON, *Cashier.*

BANK OF SUMMERTON,
Summerton, S. C., February 15, 1957.

Senator J. STROM THURMOND,
Senate Office Building, Washington, D. C.

DEAR SENATOR THURMOND: A subcommittee of the Senate Banking and Currency Committee is now considering a proposed Financial Institutions Act of 1957.

Section 26 of title III should be changed so as to conform to section 18, subsection g of the present Federal Deposit Insurance Act. The present act permits the FDIC to issue regulations pertaining to the payment of interest on demand deposits. Whereas the proposed section 26 does not allow any discretion on the part of the FDIC, it is through the use of this discretionary perogative that the FDIC has permitted insured nonmember State banks to absorb exchange for its customers without having such action condemned on the grounds that it was in effect the payment of interest on demand deposits.

On the surface this does not appear to be a big change. However, it is our opinion that it will result in forcing universal par clearance on approximately 1,900 nonpar banks located in predominately the agricultural sections. There are approximately 80 banks and communities in South Carolina which will be severely hurt if section 26 is approved as it is now written.

To give you some idea of the extreme urgency of this matter, we will list briefly below some of the repercussions of the passage of this section:

(1) That approximately 80 banks in this State and over 1,800 banks in other States, most of which are small institutions, will lose a sizable portion of their net revenues.

(2) The revenues obtained from exchange cannot be adequately replaced by service charges and therefore this loss will be permanent to these small institutions.

(3) Banking services in these small towns and the areas that they serve will be reduced and the Goverment may have to make available additional subsidies to the small-business men and farmers who are operating in such areas.

(4) Increase the hardships in which these small banks operate in attracting sufficient deposits to adequately serve its trade areas. Our best and largest depositors might easily be persuaded to keep their accounts in larger banks if we cannot absorb exchange for them. In this connection the competition for savings customers by the savings and loan associations located in the larger cities has already seriously handicapped our capacity to serve our trade area.

(5) The bigger banks will get larger and the smaller banks will inevitably become smaller. Thus we will have further concentration of our population, industry, and other developments in the larger towns.

(6) The past record of smalltown country bank failures may be repeated in the future.

(7) Banking services and credit in our small towns will become more expensive to the people now living in these areas, the time when they can least afford additional expenses. Agriculture and many smalltown industries have suffered greatly during the past several years and this appears to be just one more cross that they will have to bear. We are confident that big business has inspired this proposed change in the law and further believe that if you were to investigate the matter, you will not find any small nonmember insured State banks which has recommended or approved of this drastic, ill timed, and unfair proposal.

Please intercede in our behalf and make this letter a part of the minutes of the hearing which Senator Robertson is holding in regards to the proposed Financial Institutions Act of 1957. These minutes will close Saturday, February 16, 1957.

With kindest personal regards, I am

Sincerely,

CHARLES N. PLOWDEN, *President.*

PETERS, WRITER & CHRISTENSEN, INC.,
Denver, Colo., February 12, 1957.

Hon. A. WILLIS ROBERTSON,
Senate Office Building, Washington, D. C.

DEAR SENATOR ROBERTSON: Mandatory cumulative voting is the only type of voting that is meaningful to the public stockholders in national banks. The elimination of mandatory cumulative voting means that a half million men and women in the United States are deprived of electing directors of their own choosing in their own banks.

No one is more concerned over the proper management of the bank than the people who have their life savings invested in it. To deprive these people of the only means they have to supervise and safeguard their investment would certainly be unfair and undemocratic.

Will you please see that this letter is made a part of the record in the hearings on the Financial Institutions Act of 1957.

Yours respectfully,

GEORGE SEEMAN,
A Stockholder of a National Bank.

DEPOSITORY OF LAKE VIEW,
Lake View, S. C., February 14, 1957.

Senator J. STROM THURMOND,
United States Senate,
Washington, D. C.

DEAR SENATOR THURMOND: We have just learned that there is proposed legislation which would change the present Federal Deposit Insurance Act and that a subcommittee headed by Senator Robertson is holding hearings on this proposed bill which is entitled "Financial Institutions Act of 1957." They plan to rewrite section 18, subsection G of the present FDIC Act and insert a new section known as section 26. We believe that the adoption of such a proposed change could have devastating results, as follows:

(1) Prevent the FDIC from issuing regulations which would permit insured nonmember State banks from absorbing exchange.

(2) Bring considerable pressure to force universal par clearance which would result in losses of a substantial portion of the income now received by about 1900 insured nonmember State banks, 80 of which are located in the State of South Carolina.

(3) With income seriously impaired, many of these small country banks will be prevented from providing the necessary financial services to its customers and in the long run, it will be most difficult, if not impossible, to attract the caliber of personnel required to operate a bank in a sound and efficient manner.

(4) Take away from these small insured nonmember State banks one of the most important competitive tools that it has in competing with the larger banks for deposits.

(5) Tend to destroy the dual banking system and increase without justification Federal control of loan credit needs in small communities. In this connection, it is important to realize that the credit requirements, terms, etc., in a rural area sometimes call for an approach vastly different from what might be in order for large metropolitan areas.

(6) Prevent many of these small rural banks from encouraging small customers to use banking services and thereby developing sound business practices and procedures.

(7) Destroy a banking system which has for 25 years been most helpful in providing banking service wherever it was needed and at a cost which a small-business man, farmer, and daily wage earner can afford to pay.

(8) Weaken banking system and the FDIC by preventing these small banks from accumulating sufficient capital to insure deposits against losses without recourse on the FDIC.

(9) Generate additional profits for big manufacturers and distributors who would think nothing of spending a comparable amount of money as their annual exchange charges on advertising during a 2-week period during the year. We feel that by helping to make these banking facilities possible, that they will in the long run, as has been evidenced in the past, develop larger markets for their products.

Please have this statement entered in the minutes of the hearings which are being held by Senator Robertson. We understand that this statement must be delivered to him by Saturday, February 16, in order that it can be entered in the minutes.

This matter is worthy of your most serious consideration. We shall appreciate your interest in behalf of the small insured nonmember State banks.

Sincerely yours,

J. H. STANLEY, *Vice President and Cashier.*

WHITEVILLE, N. C., *February 15, 1957.*

Hon. SAM J. ERVIN,
United States Senate, Washington, D. C.:

We desire to express our strong opposition to section 26, title 3, of the proposed Robertson banking bill. If this section is enacted it will, in our opinion, prove disastrous to many small banking institutions in North Carolina and banks in other States operating in small towns in agricultural communities. Please insert this telegram in the proceedings of the hearing on the bill.

C. LACY TATE,
President, Waccamaw Bank & Trust Co.

PENNSYLVANIA CREDIT UNION LEAGUE,
Harrisburg, Pa., February 18, 1957.

Re proposed Financial and Credit Institutions Act.
Hon. A. WILLIS ROBERTSON,
Banking and Currency Committee, United States Senate, Senate Office Building, Washington, D. C.

DEAR SENATOR ROBERTSON: Having reviewed this proposal to amend various existing statutes we wish to offer for the consideration of your committee the following views as to certain proposed changes in section 701, Federal Credit Union Act (48 Stat. 1216).

Section 7, subsection (b).—The proposal to require that certain credit unions would be required to have an annual audit and that others would be audited by the Bureau of Federal Credit Unions does not appear to be legislation of the nature that the Congress should approve for the following reasons:

(*a*) many credit unions, through their own supervisory committee, provide an adequate internal control and a quarterly examination as required and an annual audit as specified by the act.

(*b*) an increasing number of credit unions have voluntarily arranged for independent audits and provide competent accountant assistance to their own supervisory committee.

(*c*) the Bureau of Federal Credit Unions is making an annual comprehensive examination of every credit union with the full cost paid by the credit unions.

(*d*) that the credit unions and their State and National associations are in accord with the desirability of an extensive examination by the supervisory agency.

(*e*) that the proposed responsibility to be placed upon the Bureau of Federal Credit Unions to audit some credit unions is going far beyond the normal accepted responsibility of any governmental agency and would place them in a very embarrassing position in relation to responsibility and liability for conditions not disclosed if a default were exposed later which occurred during the period covered by the Bureau audit.

(*f*) that it is not, within the past or present, the practice under good government to establish laws requiring audits by institutions and corporations which are owned by shareholders as the responsibility for the exercising of proper business practices rests with management.

(*g*) that under laws governing institutions which accept savings of the public the Federal Government has not provided, within the law, regulations as to required independent audits or authority to supervisory agencies which would permit them to require such audits.

(*h*) that credit unions are not institutions which accept savings but receive from their members, the product of their practice of thrift for the purchase of shares, and therefore become the owners of their own credit union. That the owners have the privilege of electing their own executives and committees and of operating their own credit union, and place upon them the responsibility for good management.

(*i*) that the Congress in approving the Federal Credit Union Act in 1934, recognized the desirability of providing that the people have the opportunity of establishing a credit union, owning its shares, electing from their number their own officials, operating their own thrift and credit service, auditing their own records and thereby in that way enjoying benefits and privileges of certain rights, liberty and pursuit of happiness within reasonable limits established by law and without excess governmental regulation.

(*j*) that recently the revised informational manual prepared and released by the Bureau of Federal Credit Unions as an improved guide and training manual will result in improved internal controls and audits.

(*k*) that the several State credit union leagues have been developing new training procedures which are producing better internal control and audits.

(*l*) that the Bureau of Federal Credit Unions has conferred with the Credit Union National Association and that they are jointly engaged in a study of methods to further improve internal control and audit by the individual credit union's own supervisory committee.

(*m*) that the study of improved controls and audit procedure may justify the introduction of a more comprehensive amendment to the law.

(*n*) that this proposed change in the law, on the basis of the foregoing facts, is premature, undesirable and unnecessary.

Section 12.—In this section which is similar to section 11 of the present law, while it is desirable to retain the privilege of having at least one member of the board of directors serve on the supervisory committee, it is inadvisable to permit the treasurer to be a member of that committee wherein he could audit his own accounts and the accounts of employees he supervises.

This section should be amended accordingly.

Section 15.—We suggest that this be amended to provide as an addition to the second sentence "or by any loan officers appointed by the credit committee, provided that no loan officer may approve a loan in excess of the unsecured loan limit unless such excess is fully secured by unpledged shares."

This is a desirable amendment as the majority of the credit unions operate with volunteer credit committees and other officials who generally fulfill the duties of their office on their own time, after the working hours of their regular employment. Many members of the credit union working at other hours are unable to confer with the committee and officers during their regular hours of employment. Therefore, a conflict of hours available to all concerned creates disadvantages and delays consideration and approval of certain loans by the credit committee.

The suggested amendment would provide relief and permit for prompt loan service within the area of average loans and desirable flexibility of operation essential to good service on small loans.

Section 15.—The last paragraph of the proposed section would permit the Director to establish certain maximum loan limits below the present secured loan limit established in the present law at 10 percent of a credit union's unimpaired shares and surplus. This proposal is opposed for the following reasons:

(*a*) The Congress in adopting the Federal Credit Union Act very wisely recognized the need for reasonable regulation as to signature loan limits, and the need for flexibility as to a limit on secured loans which would enable a credit union as it increased in assets to assist its members in relation to their credit needs.

(*b*) They recognized that the close common bond of association would enable a credit union to dispense its services with greater understanding because of the very personal relationship and resulting with greater assurance of repayment.

(*c*) The increase in the amount of the loans granted and the average outstanding loan balance has been in keeping with increased standards of living, average income, cost of goods and other living expenses.

(*d*) There is little evidence to indicate that further limitation is required. The loss record, due to nonrecovery on the millions of loans made, is less than 20 cents for every $100 loaned.

(*e*) Little or no evidence has been presented to indicate that the past experience makes it necessary to change the current secured loan limit.

(*f*) Credit unions serve broad segments of the people, school groups and farmers, small industrial groups and professional people, small community religions and fraternal groups consisting of persons with various occupations and diversified credit needs. Any set rule as to loan limits could impair the ability of a credit union to serve the credit needs of one or more of its members.

(*g*) Within the States, credit union laws preceded laws regulating the rate of interest on consumer credit loans. The Federal credit union system of thrift and credit was established by Congress when credit was not normally available to the average person. It was not until more than a decade later that other financial institutions, in general, reversed their position of opposition to installment credit, and made low cost credit available to the public on a limited basis. At present, credit unions continue to provide, for many of their members, the only source of adequate low cost credit, which this proposal would further limit.

(h) Credit unions have made some loans, above the average consumer credit needs of a member, to assist the members to start a small business, as credit for this purpose is not normally available from other financial institutions or under governmental procedure.

(i) The granting of a loan limitation to the Director is placing within the scope of that office, a privilege which should be the responsibility of the directors of a credit union.

(j) Under this proposal, which needs serious reevaluation, successful operation of a credit union and the use of its services could be hampered by the arbitrary decisions of an individual, and further retarded by the frequency of changes in rules and regulations.

(k) As credit unions have available the funds created by the investments in shares made by their own members, rather than funds received as savings and accounts from the public to be held for safekeeping, the need for regulation is greatly decreased and its imposition would tend to destroy the intent of the law which gives to a credit union some control over its own destiny.

(l) The law provides that the Bureau be an agency to issue charters, supervise and examine, whereas this proposal tends toward giving the Bureau management prerogatives which should be reserved for individual credit union management.

We urge that this regulation as to granting permission to the Director to establish loan limits be not approved.

Section 21 (i).—While it may be desirable to provide for rules as to future employment of persons within the Bureau, the effectiveness of such rules should not extend beyond a period of 2 years after employment.

CRIMINAL CODE

The proposals in section 217 and 218 appear to be unduly restrictive as to seeking or soliciting employment and should be eliminated as the situation can be controlled under section 21 (i) of the credit union law.

The subsection II in sections 217 and 218 should not apply to an employee of the Bureau of Federal Credit Unions who is a member of a Federal or State credit union within which he is eligible for membership and which such person does not examine.

Furthermore, under normal conditions employees of a Government agency should not be completely barred from being employed by a financial institution and such institutions should not be prohibited from obtaining qualified personnel.

We earnestly seek your full and favorable consideration of our petition.

Respectfully,

A. R. THOMPSON, *President.*

STATEMENT BY HARRISON TILGHMAN, EASTON, MD.

To the honorable the members of the Committee of the United States Senate on Banking and Currency:

Observing that there is now a bill, known as the Financial Institutions Act of 1957 of which title I is a redraft of the National Banking Act before your committee for consideration, and that therein is a provision which if enacted into law would strip shareholders of national banks of their right to cumulate their votes, I respectfully enter objection to the enactment of such a provision, and also make certain recommendations as to other provisions which should appear in the National Banking Act or be stricken from the bill under consideration.

These recommendations are made from the following background and experience: I am, and since January 1925 have been, a member of the bar of the State of New York. I also am a member of the bar of the State of Maryland.

From October 1919 (when I left the Army) to some time in 1932 (when I returned to Maryland) I was employed in the financial district of New York City. I was at first in the employ of one of the principal national banks, and subsequently in that of the Committee on Stock List of the New York Stock Exchange. Finally I was in corporate and financial legal practice with a firm whose senior partner was then counsel for the Association of Stock Exchange Firms, in which work I assisted him.

I am generally familiar with the development of Securities and Exchange legislation and the facts which led to its enactment. I am also aware of the excellent work done by the Stock Exchange (through the Committee on Stock List), in the absence of statute, to protect the investing public from the possibilities of the abuse of power by corporate management, including requiring publication of adequate, frequent, and timely reports of operation as well as balance sheets conforming to fixed standards.

I am a stockholder in a national bank. The shares which I own were the property of my maternal grandfather who died in 1890 and had then owned them for many years. I have exercised my right to cumulative voting and regard it as a primary property right and its exercise, or even its potentiality, as having a decided salutary effect upon management and to the benefit of stockholders generally.

Last July, when I learned through the New York Times that a bill was under consideration which would have spripped stockholders in national banks of their cumulative voting rights if it became law, I wrote the House of Representatives committee objecting to its enactment. I regard it as fortunate that the bill died with the adjournment of the 84th Congress.

Now that a provision of like tenor appears in the bill now before your committee, I respectfully submit that such a provision is not in the public interest and should not be enacted.

Even before the enactment of securities and exchange legislation, the stock exchange set its face against nonvoting common stocks and refused to list them. The proposed provision is however one which attempts to place stockholders of national banks in the same position, to all intents and purposes, as is the owner of nonvoting common stocks.

While not here considering preferred stocks, it is appropriate here to say that the stock exchange required that they should have voting power in certain contingencies.

In the absence of the right of cumulative voting the management of a national bank possess such power that the real owners are impotent and without any power over their property.

This is said advisedly, for while the majority in voting power ostensibly control the management, it is the management which controls the majority in voting power through proxies, which are generally signed and returned automatically by the preponderance. Only a vigilant minority ever does otherwise.

If therefore the management can assure itself that the vigilant minority shall have no representation on the board of directors—as it can do through the enactment of such a provision as is now before your committee—it can operate the bank primarily to its own benefit, fix its own compensation undisturbed, and allow stockholders only such minimum dividends as will render them innocuous.

The virtue of cumulative voting goes deeper than providing a vigilant sufficient minority with the means for acquiring and maintaining a voice in management. It creates in management a sense of responsibility to stockholders generally, which otherwise may be, and often is, absent.

It is significant that the Chairman of the Federal Reserve Board is on record as favoring cumulative voting.

To provide that cumulative voting powers may be authorized by the articles of association is of no avail for the very same management which attains and retains its powers through proxies would see to it, if it suited their purposes, that the articles contain no such provision. Only the presence of a mandatory provision in the statute (and it is now there) will preserve the right to stockholders.

It appears that the primary argument which has been advanced against cumulative voting is that it can result in the election of "undesirable persons" to the board of directors.

Undesired by whom? And why undesirable?

The answers seem obvious. Undesired by those who wish to exercise absolute power over the property of others. And undesirable because the presence of minority representation on a board of directors, acts as a check upon those who would otherwise be able more readily to conduct the affairs of the corporate body to their own purposes.

As well say that there should be but one party in Congress and no opportunity to debate any policy before its enactment.

It is reported that the Comptroller of the Currency advances the theory that the examinations of national banks conducted by his agents are sufficient to insure to stockholders everything to which they are entitled and therefore that they do not need, and should not have, the cumulative voting right.

Since when has the Comptroller of the Currency become a trustee for stockholders?

Assuming the results of the Comptroller's examinations to be perfect (which newspaper reports from time to time indicate they are not), it is submitted that such examinations are not conducted for the benefit of stockholders but to determine whether or not a bank is solvent and should be permitted to continue to operate. In brief, they are to assure the public that its deposits are safe.

However, because there were bank failures even though there were bank examinations, the Federal Deposit Insurance Corporation was established, and the depositor now has the assurance, even in the event of a bank failure (whether or not the Comptroller's examinations discovered any defect when it would have been possible to prevent its consequences), that his deposits up to $10,000 in any bank so insured (and practically every bank is), will be recovered.

The stockholder has no such prospect. Only his own vigilance can serve him in good stead. He is entitled to the full support of the law, and that there be interposed no barriers, so that he can protect his own property most effectively.

Not only would the extraction from the National Banking Act of the mandatory provision as to the right of cumulative voting be most detrimental to stockholders, but the proposed change in his right of inspection of the stockholders' list (also in the bill) would be a further barrier to his effective action.

The stockholder should not only have free and ready access to the names and addresses and amounts held by his costockholders but he is entitled to far more information as a matter of law as to the condition of his property and its gross earnings and the disposition made of them by the management, than is now required.

Therefore the statute should provide (and it does not now so provide) not only for an adequate statement of condition, including (among other things) how assets are valued (whether at cost or market), the number of shares outstanding and the par value per share; and for a statement of operations in adequate detail, including earnings per share; and that any request by the management for proxies must be accompanied by such financial statements and that they be submitted sufficiently in advance of the stockholders' meeting to permit an analysis and the formation of an intelligent opinion before proxies are submitted and action is taken predicated on the results displayed.

I also respectfully submit that any provision which would tend to dilute stockholders' interests is not in accord with sound public policy, and that the provisions in the present bill which provide for the issuance of warrants, or for stock, otherwise than pro rata to stockholders should not become law. They open the door to abuses. Let all employees of stockholders from the chairman of the board to the most minor one obtain their shares by open-market purchases and not otherwise, and all payments to them be made solely in money.

The Government of the United States is already supporting such policies as are here recommended through its securities and exchange legislation. It cannot justly do less as to corporations of its own creation.

M. S. BAILEY & SON, BANKERS,
Clinton, S. C., February 7, 1957.

HON. STROM THURMOND,
United States Senate,
Washington, D. C.

DEAR SENATOR THURMOND: It has been brought to my attention that there is included an amendment to paragraph 26, section 3, of the FDIC law which would prohibit the absorption of exchange by nonmember banks of the Federal Reserve. This bank, as so many other banks in our State, is not a member of the Federal Reserve, and to allow the inclusion of the above amendment would be most detrimental to us.

I do hope that you will see your way clear to oppose this amendment if it should ever come before you. At the present time it is my understanding that Senator Willis Robertson is chairman of a committee which is studying this problem. Your help in this matter will be greatly appreciated, not only by this bank, but by our many customers and the customers of many other nonmember banks, as it is my belief that if this law should go through that it would be but a matter of time until it would be necessary for banks of our type to levy far more charges than we find necessary at this time in order to meet current expenses.

A copy of the wire which was sent to Senator Willis Robertson and Senator John Sparkman, members of the committee making the study, is enclosed.

Respectfully yours,

ROBERT M. VANCE, *President.*

THE COLORADO BEDDING CO.,
Denver, Colo.

Mr. J. H. YINGLING,
Chief Clerk, Senate Committee on Banking and Currency,
Washington, D. C.

DEAR MR. YINGLING: I would appreciate it if you would make this letter a part of the testimony concerning the Financial Institutions Act of 1957 pertaining to the elimination of mandatory cumulative voting.

I should like to point out that for the most part the men testifying on behalf of the elimination of mandatory cumulative voting are bank managers who naturally wish to attain and accumulate as much power as possible as bank managers. Cumulative voting permits independent directors who are not afraid to stick up for the rights of the public or the stockholders in opposition to the management for through cumulative voting they have the right to be on the board without the approval of the top management of the bank.

I am firmly convinced that the banks should remain under the control of the stockholders rather than under bank managers. We know from the horrible experience of the 1920's that bank managers failed to live up to their obligations at a time when they were not subject to the restraint of mandatory cumulative voting.

Sincerely yours,

LOUIS A. WALDBAUM,
National Bank Stockholder.

BANK OF RED BAY,
Red Bay, Ala., February 15, 1957.

Re Financial Institution Act, 1957, known as Robertson bank bill.

Hon. A. WILLIS ROBERTSON,
United States Senate,
Senate Chamber, Washington, D. C.

DEAR MR. ROBERTSON: I have just been informed that your subcommittee is now having hearings on the proposed new banking bill that will rewrite section 18, subsection G, of the FDIC Act and insert a new section known as section 26 on page 162.

It is my personal opinion that it could result in the following things:

1. Bring undue and unnecessary pressure on nonmember banks to remit at par, if this is done it would greatly reduce the earnings of small country banks.

2. It would place nonmember banks under the same restrictions as to the absorption of exchange as member banks without the benefits of the Federal Reserve System.

3. It would also take away from small country banks the much needed revenues in face of rising operational costs, it would also cripple banks in certain territories where opportunities for revenue are somewhat less than in larger industrial areas.

4. We cannot see the wisdom of this change since it will not help national banks and it would greatly harm nonmember State banks.

5. There are approximately 1,900 nonpar banks in this country who depend on exchange for a large portion of income, since their volume is small and their loans are small, consequently, their earnings would be greatly impaired.

6. This possibly could provoke by statute on nonmember banks regulation Q of the Federal Reserve Bank. We feel like small country banks do render a very valuable service to the farmers and have very limited amount of revenues.

Will you please make this letter a part of the minutes of the hearings of your subcommittee. Will you also help us remove section 26 and insert section 18, subsection G in your bill.

Thanking you very much, I am

Very truly yours,

Z. L. WEATHERFORD, *President.*

CITIZENS BANK,
Vienna, Ga., February 15, 1957.

Senator A. WILLIS ROBERTSON,
United States Senate,
Washington, D. C.

DEAR SENATOR ROBERTSON: In your proposed Financial Institution Act of 1957, there is a section No. 26 in title III which, in our opinion, should be amended so as to permit the FDIC to regulate the payment of interest on demand deposits in a manner which would be to the best interest of its members. There are many pros in favor of the suggestion made above and very few reasons of consequence for permitting such a proposed change to become law. In order that you and the other members of your committee may have the benefit of our thinking, we will enumerate below our principal reasons for objecting to this proposed amendment to the present FDIC Act. Please make this letter a part of the minutes of the hearings before your subcommittee.

(1) That the timing of this proposed change is wrong because the communities and areas most affected by the proposed change are in need of all the help that a sound, efficient, and progressive bank can provide. The farming communities have been struck with declining prices and rising costs for several years. They do not need and can ill-afford to have additional interest and service charges made upon them to provide the essential banking services for existence.

(2) That the small nonmember insured State banks will be deprived of one of their strongest selling points by prohibiting them from absorbing exchange. The larger city banks will capture our best depositors because of their capital resources and thus the smaller banks will get smaller and the bigger banks will become more powerful.

(3) That the areas most affected by this change would be those in which commercial activity is at a minimum and thus where there is little opportunity to effectively collect sizable revenue from service charges. With this loss of exchange and with the inability to recapture a similar amount of revenue from service charges, we might be forced to pursue loan and investment policies which will in time do great injury to the development of our institution and area.

(4) That with income reduced, we will, along with other banks similar to ours, be in a very poor position to attract the type of management and personnel which we must have in order to provide for the present and future safety and efficiency of our bank.

This letter represents the views of the four banks in Dooly County, all of which will appreciate your consideration in the matter.

Sincerely yours,

W. G. WILLIAMSON,
Vice President and Cashier.

STATEMENT OF JOHN STENNIS, A UNITED STATES SENATOR FROM THE STATE OF MISSISSIPPI

I have this morning, less than an hour before your committee hearings are to adjourn, received telegrams from the Mississippi Bankers Association and several bankers in Mississippi in which they urge that their opposition to sections 22 and 26 of title III be made a part of the record. So that the committee may have the full benefit of their views on this important legislation. I would like for their telegrams to be inserted in the record. I regret that time does not permit me to go into this matter further now, but I do solicit the committee's attention to these telegrams.

Telegrams from:

Mississippi Bankers Association, C. E. Morgan, vice president, Kosciusko, Miss.
Leo W. Seal, president, Hancock Bank, Gulfport, Miss.
R. P. Parish, Jr., president, The Bank of Greenwood, Greenwood, Miss.
G. M. Moore, president, Grenada Bank, Grenada, Miss.
E. P. Peacock, Jr., president, Bank of Clarkdale, Clarksdale, Miss.

KOSCIUSKO, MISS., *February 17, 1957.*

Senator JOHN STENNIS,
Washington, D. C.:

We interpose our objection to section 26, title 3 of the proposed Robertson banking bill including section 22, title 3 for the reason that this measure would be destructive to the earnings of small banks in Mississippi as well as every other State in the Union and on behalf of the Mississippi Bankers Association, I interpose this objection.

C. E. MORGAN,
Vice President, Mississippi Bankers Association.

GULFPORT, MISS., *February 17, 1957.*

Senator JOHN C. STENNIS,
Senate Office Building, Washington, D. C.:

Before 11 o'clock Monday please insert in the hearings on the proposed Robertson bank bill our firm opposition to section 26, title 3 and our deep concern over the drastic and injurious effect enactment of this section would have on our many small and medium-sized banks located in small communities and which primarily serve farmers and small-business men. It is our opinion these banks would be adversely affected by this section and their ability to serve their communities impaired. Please use your influence to prevent adoption of section 26, title 3.

LEO W. SEAL, *President, Hancock Bank, Gulfport.*

GREENWOOD, MISS., *February 18, 1957.*

Senator JOHN C. STENNIS,
Senate Office Building, Washington, D. C.:

We desire to express objection to section 26, title 3, of proposed Robertson banking bill. This wire may us used as evidence. Inclusion of section 26, title 3, of the bill would be disastrous to small banks of our State. They would be unable to further serve their agricultural communities with loss of such income caused thereby; furthermore, politicalwise it shows administration's favoritism to strengthen big business and ignore smaller operations.

R. P. PARISH, Jr.,
President, the Bank of Greenwood.

GRENADA, MISS., *February 18, 1957.*

Senator JOHN C. STENNIS,
Senate Office Building, Washington, D. C.:

As a bank with 11 branches located throughout north central Mississippi, I seriously object to section 26, title 3, of proposed Robertson banking bill. I believe this section to be detrimental to all small banks, particularly those located in agricultural sections of country and that it will greatly curtail their profits and operations even to the extent that some small banks may be forced to discontinue operations. It seems impossible for small banks in agricultural sections to compete with large banks in this field and would tend to appear that big business is being heavily favored. I urge that you favorably consider this plea for the majority of the banks in the State of Mississippi.

G. M. MOORE,
President, Grenada Bank, Grenada, Miss.

CLARKSDALE, MISS., *February 18, 1957.*

Senator JOHN STENNIS,
Senate Office Building, Washington, D. C.:

We desire to express opposition to section 26, title 3, of proposed Robertson banking bill. In our opinion would serve hardships on small banks in agricultural communities.

E. P. PEACOCK, Jr.,
President, Bank of Clarksdale, Clarksdale, Miss.

×