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Statement of

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Member, Board of Governors of the Federal Reserve System

before the

Subcommittee on Domestic Finance

of the

Committee on Banking and Currency

of the

House of Representatives

on

S. 1698

and related bills

August 30, 1965

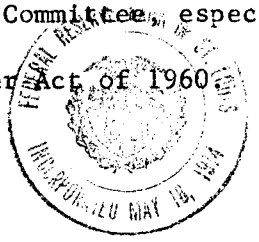
Mr. Chairman:

I am pleased to have this initial opportunity to appear before your Committee. I believe that hearings such as this play a valuable role in creating understanding of the extremely complex problems involved in the area of banking and credit. This and similar efforts of your members help to improve the basic functioning of our financial system.

Because I am the fourth member of the Federal Reserve Board to appear in the current hearings, as well as its most junior member, I probably cannot add much to your knowledge. My colleagues who testified previously have done an excellent job in explaining the major problems which the Board faces under the Bank Merger Act.

My membership on the Board of Governors dates only from May 1, 1965. Therefore, I lack the long experience in these matters of your previous witnesses. During this period I have considered only 10 proposed mergers (in which I voted to approve seven applications and to deny three). We have also considered about 75 applications for new branches.

While my administrative experience has been short, I have long been interested in the field of workable competition. Since joining the Board, I have given considerable thought and effort to these problems. In re-examining this topic, I was particularly impressed with the careful consideration given to the problem of banking structure by your Committee, especially in the actions which resulted in the Bank Merger Act of 1960.



I believe your Report on that bill established proper and reasonable standards for administrative action. I agree heartily with your statement of the basic purposes of the statute: namely, that it is intended

> "to promote a sound banking system, in the interest of the Government, borrowers, depositors, and the public; and to promote competition as an indispensable element in a sound banking system."

I also believe that you established proper guidelines when you stated:

> "We are convinced, also, that approval of a merger should depend on a positive showing of some benefit to be derived from it. . . . We . . . reject the philosophy that doubts are to be resolved in favor of bank mergers. At the risk of saying the same thing another way, we feel the burden should be on the proponents of a merger to show that it is in the public interest, if it is to be approved."

Equally admirable are the objectives stated in the Senate Report:

> "Vigorous competition between strong, aggressive, and sound banks is highly desirable; lack of competition, restraints on competition, and monopolistic practices are undesirable."

I am concerned, however, because I feel that we are not making as rapid progress as we should towards achieving these desirable goals expressed by Congress.

To explain my beliefs it may be advisable to express my general attitude on banking competition. I am convinced that in this field, as in others, vigorous competition benefits not only the economy and the general public, but the competitors themselves. As an economist I feel certain that our national policy of encouraging

and maintaining competition is one of the most important forces in our country's pre-eminent record of growth and productivity in manufacturing, distribution, transportation, and finance. Strong competition is the lifeblood of our free enterprise system.

In the recent past, banking was characterized by a lack of a strongly competitive drive. Because of the enormous importance of banking stability and continuity and in order to protect the economy from the destructive effects of bank failures, an elaborate system of supervision and governmental control of entry and expansion in this field was established.

As a result of unfortunate past experiences, governmental regulation and oversight of this industry have tended to bolster existing organizations rather than to stimulate and enhance competition. The Bank Holding Company and Merger Acts indicate that a change in emphasis has been taking place, a change that I consider to be strongly in the public interest.

My present conviction--which may be refined and modified in the crucible of administrative experience--is that Federal bank supervisors can do more than they have done to improve the competitive functioning of our banking system. Particularly it appears that, on grounds of the national interest, they may well be justified in looking with greater favor on expansion by the smaller competitors in a market, and with less favor on expansion by the larger. The latter have advantages of personnel and resources that frequently enable them to step into promising areas before such action is practicable

for their smaller competitors. I believe this situation should be actively recognized by supervisory agencies. Affirmative efforts should be made to increase the amount of competition in banking by placing smaller banking organizations, whether existing or new ones, on a more nearly equal basis with relatively gigantic competitors. The development of a policy stressing further competition in individual markets, its general adoption, and its realistic implementation, constitute one of the most challenging tasks confronting Congress, the Board of Governors, and coordinate agencies.

I believe it should be clear that in such an attempt to maintain and improve competition among banks we must be concerned with far more than the problems of mergers alone. The banking structure is extremely dynamic. Constant change occurs in each banking market as a result of four separate influences:

1. Banks grow in their existing offices.

2. Mergers, or an expansion of group banking through the medium either of holding corporations or of individual ownership, may alter the basic framework.

3. The structure can be and has been rapidly changed by the granting to banks of the right to establish branches in new locations.

4. Finally, new banks may be brought into the market if the Comptroller of the Currency or State supervisory authorities grant charters for new institutions.

Alhadeff has shown that, in most cases, the banking structure is influenced more strongly through branching and new entry than by merging.1/

1/ D. H. Alhadeff, "Bank Mergers: Competition Versus Banking Factors," Southern Economic Journal, Vol. XXIX, No. 3, January 1963.

I have attached two tables which may help to illustrate this fact. The first table shows that since 1950 the number of banking offices has increased from 18,870 to 28,546. In this period, while there was a net decrease of over 400 banks caused by the excess of mergers over new charters, the number of new branches increased by over 10,000. The table also shows equivalent changes for three of our largest States--California, New York, and Illinois. The contrasts, reflecting differing patterns of development in states with statewide branch banking, with limited branching, and with unit banking, are interesting. We note again the high percentage of change arising from branch policy.

The second table shows related information. It makes clear that, with the exception of Illinois, in the states with the highest concentration ratio (defined as the smallest percentage of banks holding over 50 per cent of deposits) a large amount of the concentration is related to the large number and growth of branches.

The Commission on Money and Credit and the Committee on Financial Institutions, established by President Kennedy and chaired by Walter Heller which reported in April 1963, discussed this problem at length. Both pointed out that the supervisory authorities and the statutes have no consistent approach or standards in their dealings with these varied influences on competition and the banking structure. In particular they note that although the effect on competition is specified as a relevant factor in merger and holding company cases, the statutory authority to grant charters and branches does not require that the effect on competition be considered.

In your initial hearings and reports on the bank merger problem, this Committee expressed concern that regulatory bodies were often approving mergers for the wrong reasons; that is, because of competition among themselves rather than among the banks. It was pointed out that since each agency acted on the basis of assumptions as to what others might do rather than upon its own judgment, a weaker policy than even the weakest of the agencies would adopt if it held sole responsibility often resulted.

I fear that this same situation still exists with respect to the over-all problem. While some coordination has resulted from your prior actions, it is still insufficient. The amount of competition, its growth or destruction, emerging at the present in each banking market results from a vast number of uncoordinated decisions. Many of these decisions are made without any recognition or consideration of the major influence the decisions themselves wield on the development of our total banking structure. There is certainly no attempt among the banking supervisory agencies to agree in any way on what a logical competitive banking structure would be like in any market. Clearly, since there are no agreed-upon goals, any policy or administrative action dealing with these problems can achieve a desirable result only by the purest chance.

The existing situation appears far from optimal if it is to establish the type of competitive banking structure which Congress has indicated it desires, and which I firmly believe to be most advantageous for our country. My brief experience indicates that if

these goals are to be achieved, Congress will have to give more specific instructions in the spheres of branching and chartering. In addition I believe there will have to be a better defined and simpler procedure for coordination.

As to my personal views on the specific provisions of S. 1698 as passed by the Senate, I have mixed reactions. I should perhaps make it clear that I was not on the Federal Reserve Board when it took a stand on this bill and I did not participate in the Board's discussion of this matter.

Under the Bank Merger Act of 1960, the Attorney General already is apprised of each proposed merger at least 30 days before it can be approved or disapproved by the bank supervisory agency with jurisdiction over the particular transaction. The Attorney General is required to make "a report on the competitive factors involved." Although I am not familiar with the procedures of the Antitrust Division of the Department of Justice, it appears to me not unreasonable to require, in these circumstances, that a decision to prosecute under the Sherman Act or the Clayton Act be made within 30 days after the Comptroller, the Board of Governors, or the FDIC has approved a proposed bank amalgamation. In effect, the Department would have a period of at least 60 days--and usually longer--to decide whether to initiate antitrust proceedings. Without jeopardizing the public interest, it appears that this administrative arrangement can obviate needless uncertainty and can avoid the danger that banks, their stockholders, and the banking public will be injured or inconvenienced by a subsequent "unscrambling" of a merged institution.

I believe it is also important that the bill, as I understand it, applies only to a merger as such, and does not confer continuing antitrust exemption upon any merged institution. That is to say, if the Department of Justice decides not to seek to enjoin a merger under the antitrust laws within the period prescribed, the transaction itself is thereafter immune from such attack. However, the immunity is confined to the merger alone; if the bank should thereafter engage in forbidden practices or gain monopoly power, the provisions of the antitrust laws would be applicable as in any other situation.

While I, therefore, support S. 1698 in general, I am unable to support the provision that would exempt from the antitrust laws all mergers of banks that were consummated prior to the bill's enactment. I found the statement of the Attorney General before your Subcommittee on this matter extremely persuasive. I feel that he has established that this proposed section does raise a broad issue of public policy and that its passage would give special treatment to a few.

It seems to me that if I were in the position of Congress, I would be reluctant to take these cases out of court. The testimony before your Subcommittee, including that of the Attorney General, indicates that the cases will be very few. I am not persuaded that there is any compelling reason, from the point of view of the banks involved or the communities they serve, to grant a special immunity from the antitrust laws for bank mergers in these cases. In the absence of some general principle justifying such an immunity, questions of

fairness to the parties and feasibility of divestiture plans may properly be left to courts of equity familiar with the facts of each case.

While I have been pleased to give my views on this particular bill, it should be clear that I believe the problem which your Subcommittee faces is broader. More is needed than merely the single proposed improvement of the administrative procedures for regulation of competition in banking which this bill proposes. I believe that other serious shortcomings exist in our current guidelines and procedures.

Attachments 2

TABLE 1

Change in Number of Banks and Branches
by Type of Change:
1950 to 1964

	U. S.			California			New York			Illinois		
	1950 to 1954	1955 to 1959	1960 to 1964	1950 to 1954	1955 to 1959	1960 to 1964	1950 to 1954	1955 to 1959	1960 to 1964	1950 to 1954	1955 to 1959	1960 to 1964
Beginning of period:												
Number of banks	14,205	13,881	13,486	206	171	115	640	560	415	890	910	955
Number of branches	4,665	6,443	9,790	949	1121	1556	759	966	1303	3	3	
Total number of offices	18,870	20,324	23,276	1155	1292	1671	1399	1526	1718	893	913	9
New banks organized	342	538	1,065	27	17	57	6	5	15	28	50	63
Losses from mergers, consolidations, etc.	666	933	776	62	73	17	86	150	70	8	5	9
Branches and facilities beginning operations, total	1,909	3,559	5,250	192	464	601	227	373	426	1	1	--
Branches and facilities ceasing operations, total	131	212	269	20	29	30	20	36	27	1	--	--
End of period:												
Number of banks	13,881	13,486	13,775	171	115	155	560	415	360	910	955	1009
Number of branches	6,443	9,790	14,771	1121	1556	2127	966	1303	1702	3	4	4
Total number of offices	20,324	23,276	28,546	1292	1671	2282	1526	1718	2062	913	959	1

Note: The number of banks and branches includes all commercial banks, insured and non-insured, in the United States and possessions. Facilities on military bases are included as branches.

TABLE 2

States with the Smallest Per Cent of Banks Holding
Over 50 Per Cent of Total Deposits
As of December 31, 1964

State	Number of Banks	Per Cent of All Banks in State	Average Number of Banking Offices per Bank in this Group	Average Deposits in Millions of $ per Bank
California	2	1.0%	611.5	8,590
Illinois	11	1.1	1.0	1,079
Michigan	5	1.4	51.2	1,241
New York	4	1.2	136.8	7,542
Pennsylvania	9	1.5	48.7	1,049