STATEMENT OF J. L. ROBERTSON, MEMBER OF
THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
BEFORE THE HOUSE BANKING AND CURRENCY COMMITTEE
ON H.R. 6504, ON JUNE 24, 1952

Mr. Chairman and Members of the Committee:

The subject of bank holding company legislation has had a long history. In 1933, Congress enacted provisions for the purpose of regulating bank holding companies; but it soon became apparent that those provisions did not adequately and effectively deal with certain problems in this field, and it has been generally recognized that some additional legislation is necessary.

Over the past 15 years Congress has considered numerous bills on this subject, ranging all the way from so-called "death sentence" legislation to "freeze" bills and bills designed only to regulate and restrict the operations of bank holding companies. One bill of a regulatory nature, S. 829, was favorably reported by the Senate Banking and Currency Committee in the 80th Congress. A somewhat similar bill, S. 2318, was recommended by the Board of Governors two years ago. The Senate Banking and Currency Committee held hearings on that bill and also on a shorter substitute bill, S. 3517, proposed by Senator Robertson. The bill which is now under consideration by your Committee, H. R. 6504, is in many respects similar to S. 2318, although there are some important differences.

Then the Board of Governors was requested by your Committee to express its views regarding the current bill, the Board felt that the time was opportune to undertake a complete re-examination of the bank holding company situation and to determine exactly what the problems are and what legislation is necessary to meet these problems. After intensive study of the matter, the Board reached conclusions which were set forth in the letter which the Board's Chairman addressed to your Committee on April 11, 1952, and in the memorandum which was enclosed with that letter. I hope that letter and its enclosures will be made a part of the record, since what I have to say here today will be for the most part simply an elaboration and expansion of the approach there outlined.
Before proceeding to a discussion of the Board's proposal, I should like to make it clear that the Board does not consider bank holding companies to be necessarily undesirable. On the contrary, we are fully aware that in many instances they have performed a valuable service in improving the management and condition of the banks controlled by them and in providing adequate banking facilities in the areas in which they operate. However, the fact remains that the very nature of the holding company mechanism makes certain abuses possible and gives rise to certain problems which, we believe, should be considered and dealt with by Congress. The key to our approach to this matter has been a desire to determine what new legislation is necessary not as a maximum, but as a minimum, in order to meet these problems.

NATURE OF THE PROBLEM

For a clear picture of the situation with which we are dealing, it should be recognized at the outset that bank holding companies represent but one of three types of multiple-office banking. One of these is branch banking, which needs no description and which is already covered by both Federal and State legislation. Another is chain banking, through which a number of independently incorporated banks are controlled by the same individual or individuals. The third, of course, is holding company banking; and, briefly stated, a bank holding company is a corporation or similar organization which owns or controls one or more independently incorporated banks.

The Board's proposals do not include regulation of chain banking; and question might be raised as to why chain banking should not be restricted as well as holding company banking, since both may involve the bringing together of several banks under single management and control. The answer lies in the fact that in chain banking there are certain inherent limitations upon the extent to which expansion is possible. In the first place, expansion is limited by the personal financial means of a single individual or a relatively small group of individuals. In the second place, control by individuals either ceases automatically upon the death of those individuals or else control is ultimately diffused among their heirs.

These inherent limitations do not exist in the case of bank holding companies. Through the corporate device, control of banks may be acquired either with funds derived from sale of capital to the public or by exchange of the holding company shares for the stock of individual banks; and the corporate device also makes possible a perpetuation of control. In the circumstances, the Board has concluded that, on the basis of present facts, there is no pressing need for legislation dealing with chain banking.
What, then, are the reasons for which we believe bank holding companies should be subjected to regulations and restrictions in addition to those provided by existing law?

A table showing figures for 28 bank holding company groups as of the end of 1950 was submitted with the Board's letter of April 11 to your Committee. Since the date of the Board's letter, we have been able to obtain figures as of the end of 1951, and I am submitting hereewith for the Committee's information a copy of the revised table. The revised table indicates that there are in the United States today 31 groups of banks which are of the type generally regarded as involving holding company banking. These 31 groups, as of December 31, 1951, included 388 banks located in 29 States and the District of Columbia, with 1,070 branches and deposits aggregating $20-1/2 billion. In some of these bank holding company groups there has been considerable expansion in the number of their banking offices since 1933. Also, in some of the groups, the bank holding companies controlled not only banks but other types of businesses such as life insurance, automobile financing, installment financing, real estate, and manufacturing.

The mere statement of these facts immediately suggests the two major problems, actual or potential, which arise from the existence of bank holding companies. One of these is the unlimited ability of such a company to expand its banking operations by acquiring additional banking offices. Obviously, this means that a large part of the commercial banking facilities in a particular area, which may cover several States, can be concentrated under the management and control of a single corporation.

The other problem arises from the fact that a bank holding company may, without restriction under present law, control not only banks but also various other types of enterprises wholly unrelated to the banking business. Our banking laws have long recognized the desirability of prohibiting banks from engaging in extraneous business. The usual type of nonbanking business enterprise requires a managerial attitude and involves business risks of a kind entirely different from those involved in the banking business. Banks, which operate to such a great extent with their depositors' funds, should finance other businesses rather than operate them. Moreover, it is not difficult to visualize the danger which would result from the improper use of the credit facilities of banks for the benefit of nonbanking enterprises where both the banks and such enterprises are controlled by the same corporation.
These two possibilities of abuse are in our judgment the only serious problems in the bank holding company field. Existing provisions of law relating to bank holding companies do not cover these problems.

Under present law, a bank holding company is subject to regulation only if it controls a member bank and only if it desires to vote the stock of such bank. If the holding company wishes to vote such stock, it must apply to the Board of Governors for a voting permit and, as a condition to obtaining such permit, it must agree to submit itself and its controlled banks to examination, to establish reserves of readily marketable assets, to dispose of all interests in securities companies, and to declare dividends only out of actual net earnings. Essentially, that is all that present law requires. In effect, it makes regulation entirely voluntary on the part of bank holding companies; they are free from all restriction if they do not choose to vote the stock of the member banks controlled by them. Even if they apply for voting permits — and 20 bank holding company groups now hold such permits — the restrictions to which they are subject are largely supervisory in nature and are aimed primarily at protecting the member banks in the groups. There are other provisions of existing law which provide for examinations and reports of affiliates of member banks and which limit loans made by member banks to their affiliates and holding company affiliates. Nowhere in existing law, however, is there any provision which prohibits bank holding companies from adding to the number of their banks or which precludes their having extensive interests in enterprises not related to the banking business.

If these facts are recognized, the extent of the need for legislation on this subject becomes clear. All that appears necessary is legislation which, without changing existing law, would directly and effectively provide means for limiting or regulating the acquisition of additional banking offices by bank holding companies and would require such companies, with reasonable exceptions, to divest themselves of nonbanking interests.

The Board's letter to the Committee outlined six principles or points which, in its opinion, should be embodied in minimum legislation of this kind. Briefly, those principles relate to coverage, limitation on expansion, divestment of nonbanking interests, supervision, enforcement, and the administering agency. I should like to elaborate a little on each of these points in an effort to make entirely clear the approach which we have in mind.
One of the principal stumbling blocks in the past has been the matter of coverage or definition. Under present law, a company is a "holding company affiliate" (1) if it owns or controls a majority of the shares of stock of a member bank, or (2) if it owns or controls more than 50 per cent of the number of shares voted in the last election of directors of a member bank, or (3) if it controls in any manner the election of a majority of the directors of a member bank, or (4) if all or substantially all of the stock of a member bank is held by trustees for the benefit of the shareholders or members of the company. The Board of Governors is specifically authorized to exempt from regulation any company which it determines is not engaged, directly or indirectly, as a business in holding the stock of, or managing or controlling banks.

This definition has been in the law for nearly 19 years. For purposes of the proposed new legislation, we believe that the same definition should be applied except to such extent as it may need to be broadened in order to cover all companies which ought to be subjected to the new legislation. Our study of the bank holding company situation has led us to the conclusion that a definition of "bank holding company" similar to that in existing law would, with but a few changes, be entirely adequate.

In the first place, it seems clear to us that the definition should not be limited to companies which control member banks. The problem raised by the unlimited ability of bank holding companies to expand in the banking field with resulting concentration of economic power exists whether or not the banks controlled are member or nonmember banks. There are today certain holding companies which control only nonmember banks and are therefore not covered by the definition in the present law. As a matter of fact, there have been instances in which a member bank acquired by such a holding company has immediately withdrawn from membership in the System and consequently the holding company did not become subject to existing bank holding company law. We would propose, therefore, that, for purposes of the new legislation, the definition of bank holding company be expanded to cover a company which owns or controls any bank, whether or not a member of the Federal Reserve System.

Insofar as the definition in present law applies a majority ownership test, we believe that that test would be adequate to cover all companies which now need to be regulated. At the present time, so
far as we know, every company which normally should be con-
sidered to be a bank holding company owns or controls a majority of
the stock of at least one bank. If it should later develop that there
are some companies which do not own more than 50 per cent of the stock
of any one bank, but which should be subjected to regulation, amend-
ments to the law for that purpose would, of course, be possible. How­
ever, on the basis of presently known facts, we believe that the majority
ownership test would be sufficient to meet the minimum requirements of
legislation dealing with the two major problems which I have mentioned.

If the definition were based primarily on ownership of
15 per cent of stock, as proposed by H. R. 6504, it would include
companies which would not need to be subjected to regulation in order
to achieve the basic purposes of the legislation. Its effect would be
to cover an unknown number of concerns in order to catch a very few, if
any, so-called fringe organizations or organizations which only po­
tentially and theoretically might be expected to embark upon a program
of controlling banks.

In two respects, a definition based on majority stock own­
ship would have to be qualified in order to prevent possible evasions.
First, we would propose that any company which falls within the definition
as of a specified date prior to passage of the new law would continue
to be regarded as a bank holding company as long as it continues to own
any bank stock whatsoever. In other words, a company which owns 50 per
cent or more of the stock of a single bank at the time specified in the
legislation would be a bank holding company within the proposed defini­
tion; and it could not escape regulation by subsequently reducing its
stock ownership to less than a majority. In the second place, the
definition should cover any successor organization so that there could
be no escape from regulation merely by transferring the holding company's
ownership of bank stocks to some other organization which would not itself
technically fall within the definition.

In addition to the majority ownership test, we would also suggest
retention of that feature of the definition in present law which limits the
coverage of bank holding companies to corporations, business trusts, asso­
ciations, or similar organizations. Again, if it should subsequently
develop that there are other forms of organizations, such as, for
example, partnerships or nonbusiness trusts, which ought to be covered
by the legislation, an appropriate amendment to cover such organiza­
tions could, of course, be enacted by Congress.
As an administrative matter, it would be desirable for the administering agency to have a severely limited authority to exempt from the definition of "bank holding company" any company which is determined not to be engaged as a business in holding bank stocks or in managing or controlling banks and which need not be covered in order to accomplish the purposes of the legislation. If such authority is given, the administering agency should be permitted to exercise it only in accordance with standards prescribed in the law itself and it should be made clear that any such exemption would be subject to revocation.

As distinguished from authority to make exemptions from the definition, we feel that the administering agency would not need to have any discretion in bringing under coverage of the legislation companies which may exercise some measure of controlling influence over banks even though they do not meet the majority ownership test. In the first place, it should be borne in mind that the definition in present law which we would retain, with the modifications above mentioned, would cover any company which controls "in any manner" the election of the majority of directors of a bank; and, if it should become important, the exercise of such control would be a question of fact for determination by the courts in criminal proceedings for the enforcement of the legislation. Furthermore, as previously indicated, we believe that the majority ownership test would cover all companies normally regarded as bank holding companies; if that should be found not to be the case, the law would of course be subject to further amendment.

LIMITATION OF EXPANSION

The second principle of the approach recommended by the Board is that there should be authority in some agency of the Federal Government to regulate and restrict the acquisition of additional banks by bank holding companies. For this purpose, we would propose that bank holding companies be required to obtain the prior consent of the administering agency before acquiring stock of any bank.

In determining whether to give that consent, the administering agency should be required to take into consideration certain standards or factors. These standards, which should be specified in the law, would be: (1) the financial history and condition of the bank holding company applying for such consent and of the banks controlled by that company; (2) the prospects of the holding company and its controlled banks; (3) the character of the management of the bank holding company and of its controlled banks; (4) the convenience, needs, and welfare of the communities and of the area concerned; and, finally, (5) whether
or not the proposed acquisition would have the effect of expanding the
bank holding company system beyond limits consistent with the policy
of Congress, which would be stated in the law, in favor of local owner-
ship and control of banks and competition in the banking field or with
adequate and sound banking or the public interest.

Once the administering agency grants consent to any such
acquisition of bank stocks on the basis of these factors, there should
be some assurance that the financial and management factors which in-
duced such consent will continue in the future. Accordingly, in grant-
ing its consent, the administering agency should be authorized to pre-
scribe such conditions as it deems necessary in order to assure the main-
tenance of the relative financial status and character of management of
the bank holding company and of its controlled banks — conditions, for
example, such as the maintenance of adequate capital and reserve funds.

It will be observed that we do not propose that the legislation
cover acquisitions of bank assets, as distinguished from bank stocks.
Our reasons for this should be explained. If a bank acquires the assets
of another bank, ordinarily it is for the purpose of converting such
other bank into a branch of the acquiring bank. In such cases, of course,
the consent of one of the bank supervisory agencies generally would be
required under existing law. In those few cases in which the acquisi-
tion of assets would not result in the establishment of a branch but
would have the effect of eliminating the bank whose assets are acquired,
the matter should be covered, not by bank holding company legislation,
but by provisions of Federal law already on the books which make acqui-
sitions of bank assets by banks subject to approval by the appropriate
supervisory agency, that is, the Comptroller of the Currency, the Federal
Deposit Insurance Corporation, or the Board of Governors. Those provi-
sions are contained in the Federal Deposit Insurance Act which was
enacted in 1950.

We would suggest, therefore, that any further restrictions
on the acquisition of bank assets, as distinguished from bank stocks,
should be made in the form of amendments to section 18(c) of the Federal
Deposit Insurance Act rather than in legislation directed at the ex-
pansion of bank holding companies. In this connection, I believe that
that section would provide adequate authority for restricting the ex-
pansion of bank holding company groups through acquisitions of bank
assets if the section were amended to require the consent of the ap-
propriate supervisory agency where the total capital structure
of the acquiring bank would not be equal to the combined amounts of
the capital structures of the banks concerned; and by "capital structure" I mean not only capital and surplus but also undivided profits and other capital accounts. Present law requires such consent only where the capital and surplus of the acquiring bank would be less than the aggregate amounts of the capital and surplus, respectively, of the banks involved; and this makes it possible for a large bank to take over a small bank, without obtaining the consent of the supervisory agency, merely by transferring undivided profits to capital and surplus.

While such an amendment to section 18(c) of the Federal Deposit Insurance Act would take care of the situation I have just mentioned, it may be that your Committee would wish to consider an amendment of somewhat broader scope which would make the section applicable to all mergers and consolidations of banks and acquisitions of bank assets, irrespective of the capital structure of the resulting bank. Your Committee might also wish to consider the addition of a provision which would require the appropriate supervisory agencies, in determining whether to give their consent, to take into consideration certain specific standards, including, not only capital adequacy, but also whether the transaction would tend unduly to lessen competition or to create a monopoly.

To return now to our proposals for regulation of bank holding companies, we feel that the administering agency, before giving its consent to any acquisition of bank stocks by a bank holding company, should be required to consult all interested bank supervisory authorities, State and Federal, and obtain the benefit of their views. This brings me to an important point on which I should like to expand, namely, the question of States' rights insofar as bank holding company legislation is concerned.

H. R. 6504 would prohibit any bank holding company or any of its subsidiaries from acquiring bank shares or bank assets across State lines or in any State in which the operation of branch banks is not authorized by the State law. Presumably, the intent of these "freeze" provisions is to protect the rights of the States. We believe, however, that such provisions are not only unnecessary to accomplish the purposes of the legislation but also that they would in effect constitute an interference with the rights of the States.

By prohibiting a bank holding company from acquiring bank shares or assets in a State which prohibits branch banking, these provisions would compel a State to apply to bank holding companies rules
at least as restrictive as those which it has seen fit to apply to branch banking. This would seem neither logical nor desirable. The policy of a State embodied in its branch banking laws may not at all be the same as it would wish to apply to bank holding company groups. As a matter of fact, there are now certain States in which branch banking is prohibited, but in which bank holding companies have freely operated for many years.

Likewise, the prohibition against expansion across State lines would mean that a State would be deprived of any right to express its policy as to the operation within its borders of a bank holding company having its principal office in another State. Under the Board's approach to this matter, the administering agency, in passing on the proposed acquisition of bank shares in such a case, would be required to obtain and give consideration to the views of the State authorities of the State in which the holding company proposes to operate. Under the freeze provisions of H. R. 650h, however, the bank holding company could not operate in such a State even though both the administering agency and the State authorities would be disposed to raise no objection and, as a matter of fact, even though the State might welcome the assistance which could be rendered to its banks by the out-of-State holding company.

In our opinion, the States should be left entirely free to deal with bank holding company operations on a basis different from that on which they deal with branch banking operations and to express their policy as to the operation of out-of-State holding companies within their borders. Consequently, it would be our recommendation that, in lieu of the "freeze" provisions of H. R. 650h, the legislation should specifically reserve to the States the right to impose such further restrictions and limitations upon bank holding companies as they may deem necessary. This would mean, of course, that if a State wishes to prohibit the operations of bank holding companies, it would be free to do so as it is today; and the administering agency under this legislation could not, therefore, grant effective consent to the acquisition by a bank holding company of any offices in that State.

**Nonbanking Interests of Bank Holding Companies**

The third point in our approach is that all bank holding companies should be required, after a reasonable time and with such exceptions as may be appropriate, to divest themselves of ownership of shares of stock and other equity interests in nonbanking enterprises.
As far as the exceptions are concerned, it would seem reasonable to permit bank holding companies to hold stocks of companies whose businesses are closely related or incidental to the business of banking, such as safe deposit companies or companies engaged solely in a fiduciary business. They should be permitted to retain shares acquired in a fiduciary capacity, and also, at least for a limited period, shares or securities acquired in the process of collecting debts previously contracted in good faith. Aside from specific exceptions such as these, it would not seem desirable to complicate legislation on this subject with numerous exceptions.

As in previous bills and as in H. R. 6504, it would be desirable to give appropriate tax relief to bank holding companies which would be required to divest themselves of their nonbanking assets under the legislation.

**SUPERVISION AND ENFORCEMENT**

Once provision is made for meeting the two major problems in this field—restrictions on expansion and divestment of nonbanking interests—it is our view that provisions with respect to supervision of bank holding companies should be kept to a minimum. We would recommend the inclusion of only two provisions of this kind.

First, it would seem desirable to require all bank holding companies to register with the administering agency within a certain time. Secondly, in order to enable the administering agency to exercise its best judgment in determining whether to consent to proposed acquisitions of bank shares by a bank holding company, the administering agency should be authorized to obtain whatever information it may need for this purpose by means of reports and, if deemed necessary, by examinations of bank holding companies. Such reports and examinations should also contain information sufficient to enable the administering agency to determine whether the law is being complied with and to keep Congress informed with respect to the administration and effectiveness of the legislation.

In the past, proposals with respect to legislation on this subject have sometimes included so-called "sanctions" or enforcement measures under which the administering agency would have been authorized, in the event of violations of the statute, to prohibit the payment of salaries to holding company officers, to prohibit dividends by the holding company or the payment of fees by subsidiary
banks to the holding company, or to prohibit the holding companies from voting their stock in the banks controlled by them. We doubt, however, that sanctions of this kind would be either desirable or effective.

Bearing always in mind the desirability of keeping the legislation to a minimum, it is our feeling that the only essential measure of enforcement, and the most effective one, would be a provision for criminal penalties for violation of the statute or of conditions prescribed by the administering agency in granting consent to acquisitions of bank stocks. This would place complete responsibility for enforcement of the law in the Department of Justice. The administering agency would not be placed in a position in which it would be required to institute proceedings for enforcement.

**ADMINISTERING AGENCY**

As was stated emphatically in the Board's letter to this Committee, the Board makes no suggestion as to what agency of the Government should be vested with the responsibility for administering the legislation. We feel that this is a matter solely for determination by Congress.

At the same time, we feel strongly that the administration of the legislation should be vested in a single agency of the Government. The reasons for this belief are twofold.

In the first place, under the simplified approach which the Board is recommending, the authority of the administering agency would be a very limited authority which would not conflict or interfere with any authority now exercised by the three bank supervisory agencies. Its only purely regulatory function would be to give or withhold its consent to the acquisition of bank stocks directly or indirectly by a bank holding company. If the bank holding company is a bank, it and its subsidiary banks would normally be prohibited by existing laws from acquiring bank stocks in any event.

In the second place, distribution of authority would mean that a bank holding company frequently would be obliged to file applications for consent to the acquisition of bank stocks with two or more different agencies of the Government, thereby resulting not only in a certain amount of duplication but in possible conflicts in policies between the several agencies in acting on such applications. It would also mean that each of the agencies involved would
be called upon to obtain substantially the same information from bank holding companies; and obviously it would be preferable for all such information to be centralized in a single agency. We believe, therefore, that any arguments that might be advanced for a distribution of authority between the several bank supervisory agencies would be far outweighed by the desirability of uniform policies and procedures and by the economy and efficiency resulting from administration by a single agency.

**RELATION TO EXISTING LAW**

An important feature of the Board's approach is that it would add to, but make no specific change in, provisions of existing law on this subject. It would leave on the books those provisions enacted in the Banking Act of 1933 which define holding company affiliates and require them to obtain voting permits from the Board of Governors if they desire to vote the stock of member banks owned by them. It would also leave untouched the provisions of the Federal Reserve Act which place certain limitations upon the amount which may be loaned by member banks to their affiliates and holding company affiliates and upon the collateral for such loans. These provisions of the present law are of value in protecting the soundness of member banks in holding company groups, even though they do not, as I have pointed out, meet the problems which we are now discussing.

Under our proposed definition of "bank holding company", all companies which are now holding company affiliates under existing law would also be bank holding companies subject to the provisions as to expansion and divestment of nonbanking interests which would be contained in the new legislation. The converse would not, however, necessarily be the case, since there would be some companies which would fall within the definition of "bank holding company" but which would not be "holding company affiliates" under present law. In other words, some companies would be subject to both the old and the new law while others would be subject only to the new.

In such circumstances, it would be possible that a company covered by both laws would be required to obtain the consent of the administering agency before acquiring the stock of a bank and would then be obliged, if the bank is a member bank, to obtain a voting permit under provisions of present law if it should desire to vote such stock. Theoretically, this could result in some possibility of conflict of policies and duplication of functions, but I firmly believe that in practice it would not present a serious problem.

The important point to bear in mind is that the legislation now being considered is aimed at matters which are not covered by present law and would not, therefore, require any revision of existing law. In the interest of simplicity, we believe that the legislation should not be complicated and confused by detailed modifications of the present law which, after all, is designed primarily for safeguarding the soundness of member banks rather than the restriction or regulation of bank holding companies. Of course, if it should later develop that present law requires amendments or that it might properly be repealed, legislation for that purpose could then be considered.
CONCLUSION

By way of summary and emphasis, let me repeat that, after very careful consideration, the Board believes that the major problems in the bank holding company field would be satisfactorily met by legislation limited to the following provisions:

1. A definition of "bank holding company" similar to the definition of "holding company affiliate" in present law, but expanded to cover companies controlling only nonmember banks as well as companies controlling member banks and phrased to include continued coverage of companies which may reduce their holdings of bank stocks after a date specified in the law;

2. Requirement for the consent of the administering agency to acquisitions of additional bank stocks by bank holding companies, with the right reserved to the States to impose further restrictions if they desire;

3. Requirement for divestment of nonbanking interests by bank holding companies, with reasonable exceptions and appropriate tax relief;

4. Requirement for registration of all bank holding companies and authority in the administering agency to obtain such information as may be necessary through reports and examinations;

5. Criminal penalties for violation of the law; and

6. Administration by a single agency of the Government selected by Congress.

We have been advised by the Bureau of the Budget that enactment of legislation incorporating the principles above outlined would be in accord with the program of the President.

In the past, as the Committee knows, proposals for legislation relating to bank holding companies have usually failed of enactment because of differences of viewpoint with respect to matters of detail. We believe that this difficulty can be largely eliminated if agreement can be reached by all concerned as to the fundamental objectives and if legislation can be confined to the few matters outlined above in order to accomplish those objectives. By the same token, it should be possible to make the legislation relatively simple, brief, and uncomplicated.

In conclusion, I should like to thank the Committee on behalf of the Board for this opportunity to present the Board's views with respect to a matter which it considers important.