Statement of
Wm. McC. Martin, Jr., Chairman,
Board of Governors of the Federal Reserve System
before the
Subcommittee on Commerce and Finance of the
House Committee on Interstate and Foreign Commerce
on H.R. 8499 and H.R. 9410

June 10, 1964

For several decades, a number of larger banking institutions throughout the country have maintained collective investment funds of the type known as "common trust funds". Such funds have provided diversification and economy that could not otherwise be achieved for relatively small fiduciary accounts administered by the bank. This is accomplished by placing the funds of such small trusts in a "pool", and investing the resources of the pool, which customarily aggregate many millions of dollars, as a single account.

The typical account participating in a common trust fund has been a small trust - perhaps for charitable purposes or for the benefit of a decedent's widow or children. In recent years, however, some banks have felt that their successful experience justifies expansion of common trust funds to constitute an investment vehicle - for example, to enable salaried individuals or professional people to accumulate a competence for retirement years and for disposition upon death.

If a bank established a "collective investment fund" for this purpose, and the fund was opened to participation by any person who wished to invest funds in this way in a pool of corporate stocks and other securities, the arrangement might be similar in general effect
to the operation of an open-end investment company, generally referred to as a mutual fund.

This development raised the question whether participation in such a collective investment fund, established and operated principally as an investment vehicle, would involve the issuance of "securities" within the purview of the Federal securities laws, particularly the Securities Act of 1933 and the Investment Company Act of 1940. Recognizing the existence of this question, the bills now before the committee would answer it by excluding all collective investment funds of banks from the coverage of the Federal securities laws, and subjecting such funds to the provisions of this "Bank Collective Investment Fund Act" and "the rules and regulations . . . of the Comptroller of the Currency pertaining to collective investments by national banks."

Up to this point I have attempted simply to outline the origin of the problem and to place it in perspective. The principal interest of your committee, of course, is the relative merit of each of the several ways in which the problem may be dealt with through legislation.

H.R. 8499 and H.R. 9410 do not purport to dispose of the question whether it is in the public interest for banks to establish and operate collective funds to serve as investment media, competing with mutual fund shares and similar securities. These identical bills would leave that question for resolution under existing banking laws. In effect,
the bills say: If banks are permitted to, and do enter this field and, in so doing, sell interests in an investment entity that would constitute "securities" subject to the Federal securities laws, such securities are to be exempted from those laws and, instead, are to be governed by the provisions of this Act and regulations of the Comptroller of the Currency.

The proposals for legislation along the lines of these bills have been supported mainly as a means of avoiding "duplicative Federal regulation" and "overlapping claims of jurisdiction". The impression is thereby conveyed that, unless Congress takes action along these lines, banks that engage in this activity will be subject to overlapping and perhaps conflicting requirements under the banking laws and the securities laws, administered respectively by the bank supervisory agencies and the Securities and Exchange Commission.

The Board of Governors of the Federal Reserve System believes that this view of the matter is based upon a fundamental misapprehension and that its implementation through enactment of either of these bills would not be in the public interest. The misapprehension to which I refer results from a failure to keep in mind the different objectives and methods of bank supervision, on the one hand, and the regulation of sale of securities, on the other.

The principal purpose of bank supervision is to assure that this vital sector of the economy operates in a safe, sound, and serviceable manner and in accordance with laws and regulations.
adopted with those objectives in mind. Among other functions, bank examination attempts to safeguard bank deposits, to evaluate the quality of bank management, and to learn whether the bank is rendering satisfactory service to its community and whether its capital structure is adequate in view of the nature of its business. In other words, bank supervision enforces banking laws and regulations and evaluates the operations of banks, principally to protect and benefit bank depositors and other customers.

The Federal securities laws with which we are concerned have an entirely different aim and focus. Their purpose is to protect and benefit investors, and to accomplish this by making available to them relevant information regarding securities that they hold or contemplate acquiring. The keynote of these laws is disclosure of information to the public, rather than regulation and control of enterprises, banking or otherwise.

If this fundamental distinction is kept in mind, it becomes apparent that (1) regulation of banking by supervisory agencies and (2) disclosure to investors of information regarding securities issued by banks are entirely different, and that no significant danger of duplication of effort or conflict of jurisdictions should result merely because banks continued to be supervised by the Federal Reserve System and other supervisory agencies and securities issued by banks were subject to the disclosure and other provisions of the Federal securities laws.
A large proportion of our country's industry and commerce is presently regulated by agencies such as the Interstate Commerce Commission, the Federal Power Commission, the Civil Aeronautics Board, the Federal Communications Commission, and the public utilities commissions of the States, to mention only a few; but the securities issued by railroads, pipeline companies, airlines, telephone and telegraph companies, electric and gas companies, and the like, are nevertheless governed by the securities laws that we are considering here. As far as I know, it never has been contended that, because Triangle Airlines Company, for example, is subject to the jurisdiction of the Civil Aeronautics Board, there is "duplication of supervision" or "conflict of jurisdiction" because an offering of securities by that corporation is subject to the disclosure requirements of the Securities Act of 1933, in the interests of prospective investors.

In the opinion of the Board of Governors, this should be equally true in the case of banks and securities issued by banks. Through the securities laws, Congress has implemented its considered judgment that American investors should be furnished with information that is adequate to enable them to make intelligent decisions regarding the intrinsic and - even more important - the relative merits of securities competing for their investment dollars. The investing public is entitled to these benefits with respect to securities issued by banks as well as securities issued by enterprises in other fields.
The Federal securities laws embody and implement this salutary "disclosure philosophy", and the Securities and Exchange Commission, which administers those laws, has resources of personnel and experience, devoted to the administration of those laws, that would be difficult to duplicate. To exclude certain categories of securities from those laws and that administration, merely because such securities are issued by funds maintained by banks, would deny investors important protections and benefits without any adequate reason. The proposed exclusion of certain securities from the coverage of the securities laws, and the proposed transfer of jurisdiction in the securities field from the Securities and Exchange Commission to bank supervisors, would yield no benefits of which we are aware, but on the contrary would be injurious to investors and would require the Federal Reserve System and other bank supervisors to perform functions, at a substantial additional cost to the American people, that can be more efficiently performed by the Securities and Exchange Commission, whose facilities are devoted entirely to this complex and important subject.

For these reasons, the Board of Governors recommends against enactment of H.R. 8499 and H.R. 9410.