

The Papers of Eugene Meyer (mss52019)

117_11_001-

Subject File, Federal Reserve Board, Glass Bill (S. 3215), Comments on
Affiliates, 1932

EUGENE MEYER

SUBJECT FILE

FEDERAL RESERVE BOARD
GLASS BILL (S. 3215)
COMMENTS ON AFFILIATES 1932

GOVERNOR MEYER

CONFIDENTIAL

CONFIDENTIAL

COMMENTS AND RECOMMENDATIONS
ON SECTIONS OF
GLASS BILL (S-3215)
DEALING WITH AFFILIATES

February 29, 1932

810 Eighteenth Street, N. W.
Washington, D. C.
February 29, 1932

Honorable Carter Glass
United States Senate
Washington, D. C.

Dear Senator Glass:

We are transmitting herewith a further report upon the Glass Bill, S-3215, containing our recommendations with respect to those sections of the bill which deal with the general subject of affiliates. As was the case with our first report, the recommendations represent our own personal views and opinions and in no sense the views of our institutions.

We have been impressed in reviewing this portion of the bill with the technical character of the problems and the lack of adequate information bearing upon them. We hope, therefore, that our recommendations will be subjected to further careful scrutiny by persons experienced in this field. Particularly in the case of the definitions, which are crucial in the administration of the law, we feel that further study would be fruitful. It may be necessary in order to render the definitions effective to give the Comptroller of the Currency and the Federal Reserve Board authority to extend their application to cover cases where there may clearly be affiliations in fact, even though they may be technically excluded by the wording of the law.

Honorable Carter Glass - #2

February 29, 1932

It has seemed to us desirable to preface our detailed recommendations as to changes in the bill with a general statement of principles that have formed the basis for our recommendations.

Respectfully yours,

W. Randolph Burgess E. A. Goldenweiser

CONTENTS

	Page
General principles governing legislation as to nonbanking affiliates.....	1 - 5
Specific provisions of S-3215 Sections 2, 4, 6, 11, 20-24, 31-32.....	6 -31
Additional New Sections:	
<u>Borrowing by bank officers and employees.</u>	32-33
<u>Branches of State member banks.....</u>	34

GENERAL PRINCIPLES GOVERNING LEGISLATION

AS TO NONBANKING AFFILIATES

We understand that the Senate Committee has considered whether it would be better to attempt to abolish affiliates altogether or to allow them to continue under supervision, and has decided to adopt the latter course. We interpret this decision to imply that no attempt will be made at present to effect a complete divorce of affiliates from their parent institutions.

There are several reasons why the present is not an auspicious time to attempt the abolition or divorce of affiliates from banking institutions. In the first place, the amount of information available as to affiliates is restricted--there has never been a comprehensive survey of the field, and any action taken now should be tentative in view of the paucity of information.

In the second place, under present conditions any vigorous attempt to bring about such a divorce would result in a general liquidation of affiliates.

Finally, too rigorous legislation at this time might be expected to have a disturbing effect upon the general situation. In the case of securities companies, for example, the unhappy consequences which followed the excessive issuance of securities in 1928 and 1929 have already reacted upon the machinery of securities distribution. Many banks have already taken steps to liquidate their securities companies or to reduce their capital and volume of operations. The market for new securities is disorganized and any action tending to disrupt the existing machinery still further would tend to retard recovery, since new enterprise is in a measure dependent upon the sale of

securities to investors.

Certain forms of affiliates, furthermore, appear to be legitimate and useful adjuncts to a commercial bank. Safe deposit companies have long been recognized as serviceable, and the same may be said of agricultural loan companies and bank building corporations. It is also true that holding companies have in several instances definitely strengthened the banking situation in certain areas. Even in respect to security affiliates there are certain advantages in having a part of the business of issuing securities done by institutions which are under supervision by the authorities rather than having all of it done by agencies over which there is no supervision whatever.

For these reasons our recommendations are confined to (1) supervision over affiliates, one of the results of which will be to make available information with regard to their operations; and (2) certain restrictions over the operations of affiliates or of banks in relation to their affiliates.

It may develop when sufficient information acquired under the provisions of this bill becomes available that, in order to make supervision effective, in regard to affiliates as in regard to banks, it may be necessary to find a way to require all institutions having to do with the initiating or marketing of securities, as well as bank holding companies, to have their power to engage in business originate from a national authority.

Nonbanking affiliates may be classified for convenience under two general types: subsidiary affiliates and holding company affiliates. These are so different in character and legal status as to require separate legislative treatment.

SUBSIDIARY AFFILIATES

There are from 15 to 20 distinguishable types of subsidiary affiliates in addition to banks and trust companies, the four most common nonbanking types being:

- securities companies
- real estate companies
- bank building companies
- safe deposit companies

In addition the following occur frequently:

- mortgage companies
- liquidating companies
- agricultural loan companies
- personal or small loan companies
- investment trusts
- building and loan associations
- insurance agencies
- finance and acceptance corporations
- guaranty and mortgage guaranty companies
- foreign banking corporations

Some affiliates carry on more than one of these various types of business. The character and function of subsidiary affiliates are so diverse that it is difficult to adopt any uniform regulation which will apply to all of them.

Our proposals, therefore, in regard to subsidiary affiliates are made with a view, first, to subjecting these companies to some type of supervision which, without destroying the existing machinery, will be helpful in safe-guarding the relations with the parent bank, and, secondly, to assembling over a period additional information about affiliates and their operations which shall form a basis for such further methods of control as may later appear to be desirable.

We therefore recommend limitations upon the loans of banks to their subsidiaries; also that subsidiary affiliates be subject to examination at the same time as their parent institutions, and that the call reports made by these

institutions be accompanied by reports for their affiliates, as of the same date, showing their balance sheets and profit and loss statements. These examinations and reports would have the double advantage of bringing the organizations under scrutiny and of accumulating information as to their organization and operations.

An important difference between our recommendation on this subject and the original bill is that we have followed the principle that all limitations enacted should be uniformly applicable to all member banks rather than to national banks alone.

HOLDING COMPANY AFFILIATES

Numerically, holding companies are a smaller problem than subsidiary companies. The number of domestic holding company affiliates of member banks probably does not exceed 100 as compared with some 1,200 domestic subsidiary company affiliates.

Supervision of holding companies is complicated by the dual banking system, for most holding companies control some national banks and some State banks. Too drastic regulation of holding companies of national banks would impel them to convert all their banks into State institutions. For this reason suggestions for regulations made in succeeding pages are confined to those which may be applied alike to holding companies for both national and State member banks.

This and a number of other holding company problems may be expected to be diminished by the extension of branch banking proposed in the Glass bill with the amendment we have suggested, because many holding company groups

would then be likely to become branch systems.

It seems clear that the Comptroller of the Currency and the Federal Reserve Board should be given authority to examine every holding company controlling a member bank and should receive current reports from such companies. There should also be means of assurance that the stockholder's liability upon stock held by a holding company should be at least as enforceable as the liability of independent individual shareholders. Loans to holding company affiliates upon their stock should be prohibited. We believe also that it would be desirable and practicable to have holding companies bring all the banks under their control into the Federal reserve system, if they are eligible, and thus make these banks, which benefit from the strength of their member bank associates in the group, assume the full responsibilities of membership in the system.

SPECIFIC PROVISIONS OF S-3215

On the basis of these general principles, the following specific suggestions are made with respect to the provisions of S-3215 relating to affiliates:

SECTION 2 Continued

surety on the obligations of others, or in any similar business or undertaking:

"(1) In which any national bank or member bank directly or indirectly owns or controls a majority of the voting shares, or a lesser number of such shares if such lesser number is more than 50 per centum of the number of shares voted for the election of directors, trustees, or other managing officers at the preceding election; or

"(2) In which any national bank or member bank in any other manner directly or indirectly controls the election of a majority of its directors, trustees, or other managing officers; or

"(3) All or substantially all of the shares of which are held by trustees for the benefit of the shareholders of any national bank or member bank; or

"(4) The control of which is held directly or indirectly, through ownership of shares or in any other manner, by shareholders of any national bank or member bank who own or control a majority of the stock of such national bank or member bank.

"(c) The term 'holding company affiliate', except where otherwise expressly defined, shall include any corporation, business trust, association, or other similar organization:

"(1) Which directly or indirectly owns or controls a majority

SECTION 2 -- Definitions

These suggestions supersede our recommendations in the memorandum submitted on February 8.

The definitions relating to affiliates have been further revised to distinguish more precisely between subsidiary affiliates and holding company affiliates. It is suggested that the following be substituted for subsections (b) and (c) of Section 2 of the Bill:

"(b) The term 'subsidiary affiliate', except where otherwise expressly defined, shall include any corporation, business trust, association or other similar organization engaged in the business of acting as trustee, executor, administrator, or in any other fiduciary capacity, or in the business of receiving deposits, making loans, or discounting notes, drafts, bills of exchange or other evidences of indebtedness, or in the business of underwriting, purchasing, selling, dealing in, holding, or acting as a broker of stocks, bonds, or other investment securities, or in the business of purchasing, selling, holding, dealing in, making loans on, or acting as a broker of, real estate or real estate loans, or in the business of renting safe deposit boxes, or in any kind of insurance business, either as insurer, broker, or agent, or in the business of granting bankers' acceptance credits, or in the business of examining, guaranteeing, or insuring titles to real estate, or in the business of acting as guarantor or

SECTION 2 Continued

of the shares of capital stock of a national bank or member bank, or a lesser number of shares if such lesser number shall amount to more than 50 per centum of the shares voted for the election of directors at the preceding annual meeting of such national bank or member bank; or

"(2) Which in any other manner directly or indirectly controls the election of a majority of the board of directors of any national bank or member bank; or

"(3) For the benefit of the shareholders of which all or substantially all of the stock of any national bank or member bank is held by trustees."

SECTION 4

This section was also discussed in the previous report. It is suggested that it be omitted on the ground (1) that the introduction of branch banking may be expected to reduce sufficiently the holding company problem so that no such provisions will be necessary, and (2) the provision as drawn appears to discriminate against well organized and more responsible groups in favor of looser and less responsible affiliations.

SECTION 6

We suggest the following substitute for this provision making a few minor modifications to bring the practice in accord with Federal reserve practice as to member bank reports:

SECTION 6 Continued

"Section 9 of the Federal Reserve Act, as amended, is further amended by inserting between the fifth and sixth paragraphs thereof the following new paragraph:

"Each bank admitted to membership under the provisions of this section shall obtain and furnish to the Federal reserve bank of which it becomes a member such reports of the condition of any or all of its subsidiary affiliates as the Federal Reserve Board, in its discretion, may require. Such reports shall be in such form as the Federal Reserve Board may prescribe, shall be verified by the oath or affirmation of the president or such other officer as may be designated by the Board of Directors of the affiliate to verify such reports, and shall disclose the financial condition of the affiliate on dates fixed by the Federal Reserve Board. Each such report shall be transmitted to the Federal reserve bank at the time required by the Federal Reserve Board and shall exhibit in detail and under appropriate heads all assets of the affiliate in question, their cost and present value, all liabilities of such affiliate, its earnings and expenses, and such other information as the Federal Reserve Board may require. Any member bank which fails to furnish any report of a subsidiary affiliate to the Federal reserve bank, when required by the Federal Reserve Board shall be subject to a penalty of \$100 for each day during which such failure continues. Such penalty

SECTION 6 Continued

may be assessed by the Federal Reserve Board, in its discretion and, when assessed, may be collected by the Federal reserve bank by suit or otherwise.' "

We also suggest the following additional paragraph under Section 6 to put subsidiary affiliates of State member banks on the same status as those of National banks with respect to examinations:

"Section 9 of the Federal Reserve Act, as amended, is further amended by adding at the end thereof new paragraphs to read as follows:

'Examiners selected or approved by the Federal Reserve Board shall examine any subsidiary affiliate of a bank admitted to membership under the provisions of this section, when directed to do so by the Federal Reserve Board, in its discretion, or by the Federal reserve bank of the district in which such member bank or subsidiary affiliate is located, in its discretion. The examiner making the examination of any such affiliate shall have power to make a thorough examination of all the affairs of the affiliate, and in doing so he shall have power to administer oaths and to examine any of the officers, directors, employees, and agents thereof under oath, and shall make a full and detailed report of the condition of the affiliate to the Federal Reserve Board or to the Federal reserve bank which directed the examination to be made. Copies of the report of any such examination may, in the discretion of

SECTION 6 Continued

the Federal Reserve Board, be furnished to the State authorities having supervision of State member banks, to officers, directors, or the receiver of the affiliate examined, or to the officers, directors, or the receiver of the member bank with which it is affiliated, and to any other proper persons. The expenses of any examination made under the provisions of this paragraph may, in the discretion of the Federal Reserve Board, be assessed against the affiliate examined and, when so assessed, shall be paid by the affiliate examined. If the officers, directors, or stockholders of any affiliate of a bank admitted to membership under the provisions of this section shall refuse to permit an examiner to make an examination of the affiliate which the Federal Reserve Board or the Federal reserve bank has directed to be made, refuse to give any information required in the course of any such examination, or refuse to pay the expenses of any such examination, the Federal Reserve Board after a hearing, in its discretion, may require the member bank with which it is affiliated to surrender its stock in the Federal reserve bank and to forfeit all rights and privileges of membership. The Federal Reserve Board may restore membership upon due proof of compliance with the conditions imposed by this section.

SECTION 11

Provisions relating to the restriction of loans to affiliates are contained in Section 11 and also in Section 29. Section 11 relates to all member banks but includes only certain specified types of affiliates and is much less drastic than Section 29, which relates to National banks only and to all types of affiliates. We believe it is undesirable to enforce more drastic restrictions as to affiliates upon National banks than upon State member banks, and for this reason recommend that provisions in regard to loans to subsidiary affiliates should be covered in a single section applicable to all member banks and to all types of subsidiary affiliates. Loans to holding companies are treated in another section.

In accordance with this general principle, the following substitute is suggested for Section 11:

SECTION 11

The Federal Reserve Act as amended is hereby further amended by inserting between Sections 20 and 21 the following new section:

"Section 21A. No National banking association and no member bank shall (1) make any loan or any extension of credit to, or purchase securities under repurchase agreement from, any of its subsidiary affiliates, or (2) invest any of its funds in the capital stock, bonds, or other obligation of any such affiliate, or (3) accept the capital stock, bonds, or other obligations of any such affiliate as collateral security for advances made to any

SECTION 11 Continued

person, co-partnership, or corporation; if in the case of any such affiliate the aggregate amount of such loans or extensions of credit, repurchase agreements, investments, and advances against such collateral security will exceed 10 per centum of the unimpaired capital stock and surplus of such National banking association or member bank, or if in the case of all such affiliates the aggregate amount of such loans, extensions of credit, investments, and advances against such collateral security will exceed 20 per centum of the unimpaired capital stock and surplus of such National banking association or member bank; Provided, however, that in computing such aggregate amounts, either in the case of a single affiliate or of all affiliates together, there shall be excluded the investment of such National banking association or member bank in (1) the capital stock and obligations of an affiliate organized for the sole purpose of holding its banking house or houses and the site or sites thereof, (2) the capital stock of a corporation organized to conduct a safe deposit business, (3) the capital stock of any corporation in which such bank has been authorized to invest pursuant to Section 25 of the Federal Reserve Act, and (4) the capital stock of a corporation organized under Section 25-A of the Federal Reserve Act.

"Each loan or extension of credit made to a subsidiary

SECTION 11 Continued

affiliate within the foregoing limitations shall be secured by collateral having market value at the time of making the loan or extension of credit of at least 20 per centum more than the amount of such loan; except that such loans or extensions of credit on the security of obligations of the United States Government, Reconstruction Finance Corporation, Federal land banks, and of notes, drafts, bills of exchange, or acceptances eligible for rediscount at the Federal reserve banks, may be made in an amount equal to the ascertained market value of these securities, and that a loan made on the security of obligations of any State or political subdivision or agency thereof shall be secured by collateral having an ascertained market value at the time of making the loan of at least 10 per centum more than the amount of such loan. A loan or extension of credit to a director, officer, clerk, or other employee or nominee of any such affiliate shall be deemed a loan to the affiliate to the extent that the proceeds of such loan are transferred to the affiliate."

SECTION 20

The second half of this section relates to affiliates and it is suggested that it be omitted, in accordance with the general principle previously discussed that no attempt should be made at this time to divorce affiliates from the banks with which they are connected.

SECTION 21

It is suggested that this section be omitted also on the principle that no attempt should be made at this time to divorce affiliates from the banks with which they are connected.

As previously noted in our first report, the last part of this section would make it impossible for a member bank to clear checks or do the other ordinary banking business of a correspondent for a foreign banking house or any out-of-town investment house.

SECTIONS 22, 23, AND 24

It is recommended that Section 23 be omitted since it is directed toward divorcing and destroying affiliates. For Sections 22 and 24 we suggest a revision. The principal change is that an additional section has been prepared to place holding companies of State member banks under the same supervision and restriction as holding companies for National banks.

The provision for free assets to guarantee stockholders' liability has been modified to make it more practicable.

A provision has been added designed to bring into the reserve system eligible nonmember banks controlled by holding companies coming under the

SECTIONS 22, 23, AND 24 Continued

provisions of this section.

We have not assigned numbers to these sections, because they take the place of several sections in the bill, and, if accepted by the Subcommittee, can be numbered continuously.

SECTION

Section 5144 of the Revised Statutes, as amended, is amended to read as follows:

"Sec. 5144. In all elections of directors and in deciding all questions at meetings of shareholders, each shareholder shall be entitled to one vote on each share of stock held by him, except that shares of its own stock held by any National bank as trustee shall not be voted, and shares owned or controlled by any holding company affiliate, as defined by the Banking Act of 1932, or by any officer, director, or employee thereof, shall not be voted unless there is in effect at the time a voting permit issued to such holding company affiliate as hereinafter provided. Shareholders may vote by proxies duly authorized in writing; but no officer, clerk, teller, or bookkeeper of such association shall act as proxy; and no shareholder whose liability is past due and unpaid shall be allowed to vote.

"Any holding company affiliate may make application to the Comptroller of the Currency for a voting permit entitling it and its officers, directors and employees to cast one vote at all

meetings of shareholders of such National banking association on each share of stock actually owned or controlled by it or by its officers, directors, or employees. The Comptroller of the Currency may, in his discretion, grant or withhold such permit as the public interest may require; and every holding company affiliate which applies for and receives such a permit shall be subject to, and shall comply with, all of the applicable provisions of this section, so long as such permit shall remain in force.

"Every such holding company affiliate and each bank owned or controlled thereby shall be subject to examination by examiners representing and acting for the Comptroller of the Currency, who shall have the same powers and duties with respect to such examinations as they have with respect to examinations of National banks. The expenses of each such examination shall be assessed against, and paid by, such holding company affiliate or the bank examined. The report of the examiner shall set forth all facts ascertained by the examination and shall include the name, location, capital, surplus, and undivided profits of each bank in which the applicant owns stock and the number of shares so owned.

"Each holding company affiliate and each bank owned or controlled thereby shall file with the Comptroller of the

Currency reports of condition (including consolidated reports of such holding company and all banks controlled thereby) at such times and in such form as the Comptroller may prescribe, in his discretion, and shall publish in such manner as the Comptroller shall prescribe such reports of condition or such parts thereof as he may require.

"Within a period of one year from the issuance of any such voting permit, each nonmember State bank owned or controlled by such holding company affiliate which is eligible for membership in the Federal reserve system shall apply for membership therein in the manner prescribed by, and subject to the terms of, Section 9 of the Federal Reserve Act. If such application is approved by the Federal Reserve Board, such bank shall become a member of the Federal reserve system and shall comply with all of the provisions of law applicable to member banks. If such application is not approved by the Federal Reserve Board, or if any such bank shall fail to become, or shall cease to be, a member of the Federal reserve system at any time while such voting permit remains in effect, such holding company affiliate shall divest itself of all stock ownership or other interest in, or control of, such bank.

"Except as otherwise provided herein, every such holding company affiliate, (1) shall possess on January 1, 1934, or at the time of the issuance of such voting permit, and shall

thereafter continue to possess during the existence of such permit, free and clear of any lien, pledge or hypothecation of any nature, readily marketable assets other than bank stock, which shall not amount to less than 15 per centum of the aggregate par value of bank stocks held or owned by such holding company affiliate, and (2) shall reinvest in readily marketable assets other than bank stock all net earnings over and above six per centum per annum on the book value of its own shares outstanding, until its readily marketable assets other than bank stocks shall amount to 25 per centum of the aggregate par value of bank shares held or owned by it; Provided, however, That, in computing the amount of readily marketable assets, other than bank stock, which any holding company affiliate is required to possess at any given time, credit shall be given to such holding company for all contributions which such holding company has made during the preceding three years to any bank owned or controlled by such holding company at the time such computation is made. The term 'contribution,' as herein used, shall include all gifts of money, assets or other things of value to any such bank, all amounts paid for worthless or doubtful assets purchased from any such bank, and such other similar amounts as the Comptroller of the Currency, in his discretion, may permit to be treated as contributions. No holding company affiliate, whose shareholders are

liable by the law of the State in which such holding company affiliate is incorporated for the liabilities of such corporation to an amount not less than the par value of the shares of stock held by any such shareholder, in addition to the amount invested in such shares, shall be required to comply with the provisions of this paragraph.

"There is hereby created a board composed of the Secretary of the Treasury, Governor of the Federal Reserve Board and the Comptroller of the Currency, who may, in their discretion, revoke any such voting permit after giving sixty days' notice of their intention to the holding company affiliate by registered mail. Whenever such board shall have revoked any such voting permit, no member bank whose stock is owned in whole or in part by the holding company affiliate whose permit is so revoked shall receive United States Government deposits, nor shall any such member bank pay any further dividend to such holding company affiliate upon any shares of such bank owned or controlled by such holding company affiliate.

"When any holding company affiliate has obtained a voting permit from the Comptroller of the Currency in accordance with the provisions of this section, any officer, director, agent or employee of such holding company affiliate, who shall make any false entry in any book, report or statement of such holding company affiliate with intent in any case to injure or defraud

such holding company affiliate, any member bank or any other company, body politic or corporate, or any individual person, or with intent to deceive any officer of such company or of any member bank, or the Comptroller of the Currency, or any agent or examiner appointed to examine the affairs of such holding company affiliate, shall be deemed guilty of a misdemeanor and upon conviction thereof in any district court of the United States shall be fined not more than \$5,000 or shall be imprisoned for not more than five years, or both, in the discretion of the court.

"No National bank shall, (1) make any loan on the stock of any holding company affiliate which owns or controls such National bank directly or indirectly, (2) make any loan to any holding company affiliate which owns or controls such National bank directly or indirectly on the security of any shares of stock of any affiliate of such holding company affiliate, (3) be the purchaser or holder of the stock of such holding company affiliate; unless such security or purchase shall be necessary to prevent loss upon a debt previously contracted in good faith; and any stock so purchased or acquired shall be sold or disposed of at public or private sale within two years from the date of its acquisition.

"Unless there is in effect at the time a permit issued pursuant to the terms of this section authorizing such stock to be voted, any person, firm, corporation, association, business trust,

or other organization, which shall vote, or cause, direct, authorize, or permit to be voted, the stock of any National bank owned or controlled by any holding company affiliate, or by any officer, director or employee thereof, shall be deemed guilty of a misdemeanor and, upon conviction thereof in any district court of the United States, shall be fined not more than \$5,000 for each such offense. Each vote cast shall constitute a separate offense within the meaning of this paragraph."

SECTION

The Federal Reserve Act, as amended, is further amended by inserting therein immediately after Section 9 thereof a new section reading as follows:

"Section 9A. No State bank or trust company shall be permitted to become a member of the Federal Reserve System unless each holding company affiliate of such State bank or trust company, as defined in the Banking Act of 1932, shall have filed with the Federal Reserve Board an agreement in such form as may be prescribed by said Board accepting, and agreeing to submit to, and comply with, all of the provisions of this section; and no State bank or trust company shall remain a member of the Federal Reserve System after one year from the date of the enactment of this act unless each holding company affiliate of such State bank or trust company shall have filed such an agreement with the Federal Reserve Board.

"Every such holding company affiliate and each bank owned or controlled thereby shall be subject to examination by examiners selected or approved by the Federal Reserve Board and acting under the direction of the said Board, who shall have the same powers and duties with respect to such examinations as they have with respect to examinations of member banks. The expenses of each such examination shall be assessed against, and paid by, such holding company affiliate or the bank examined. The report of the examiner shall set forth all facts

SECTION Continued

ascertained by the examination and shall include the name, location, capital, surplus and undivided profits of each bank in which such holding company affiliate owns stock and the number of shares so owned.

"Each such holding company affiliate and each bank owned or controlled thereby shall file with the Federal Reserve Board reports of condition (including consolidated reports of such holding companies and all banks controlled thereby) at such times and in such form as the said Board may prescribe, in its discretion, and shall publish in such manner as the said Board shall prescribe such reports of condition or such parts thereof as the said Board may require.

"Within a period of one year from the date of any such agreement filed with the Federal Reserve Board by any holding company affiliate, each nonmember State bank owned or controlled by such holding company affiliate which is eligible for membership in the Federal Reserve System shall apply for membership therein in the manner prescribed by, and subject to the terms of, Section 9 of this Act. If such application is approved by the Federal Reserve Board, such bank shall become a member of the Federal Reserve System and shall comply with all of the provisions of law applicable to member banks. If such application is not approved by the Federal Reserve Board, or if any

SECTION Continued

such bank shall fail to become, or cease to be, a member of the Federal Reserve System at any time while such agreement remains in effect, such holding company affiliate shall divest itself of all of the stock ownership or other interest in, or control of, such bank.

"(b) Except as provided herein, every such holding company affiliate (1) shall possess on January 1, 1934, and at all times thereafter during the membership in the Federal Reserve System of any State bank or trust company of which it is a holding company affiliate, free and clear of any lien, pledge or hypothecation of any nature, readily marketable assets other than bank stock, which shall not be less than 15 per cent of the aggregate par value of bank stocks held or owned by such holding company affiliate; and (2) shall reinvest in readily marketable assets other than bank stock all net earnings over and above 6 per centum per annum on the book value of its own shares outstanding, until its readily marketable assets, other than bank stocks, shall amount to 25 per centum of the aggregate par value of bank shares held or owned by it; Provided, however, That, in computing the amount of readily marketable assets, other than bank stock, which any holding company affiliate is required to possess at any given time, credit shall be given to such holding company for all

SECTION Continued

contributions which such holding company has made during the preceding three years to any bank owned or controlled by such holding company at the time such computation is made. The term 'contribution,' as herein used, shall include all gifts of money, assets or other things of value to any such bank, all amounts paid for worthless or doubtful assets purchased from any such bank, and all such other similar amounts as the Federal Reserve Board, in its discretion, may permit to be treated as contributions. No holding company affiliate whose shareholders are liable by the law of the State in which such holding company affiliate is incorporated for the liabilities of such corporation to an amount not less than the par value of the shares of stock held by any such shareholder, in addition to the amount invested in such shares, shall be required to comply with the provisions of this paragraph.

"If any holding company affiliate shall fail to comply with the provisions of this section or with the provisions of any agreement with the Federal Reserve Board made pursuant thereto, the said Board, in its discretion, may require any State member bank to which said company is a holding company affiliate to surrender its stock in the Federal reserve bank and to forfeit all rights and privileges of membership in the Federal Reserve System as provided in Section 9 of this Act.

SECTION Continued

"Any officer, director, agent or employee of any holding company affiliate which has filed an agreement with the Federal Reserve Board, as provided in this section, who shall make any false entry in any book, report or statement of such holding company affiliate with intent in any case to injure or defraud such holding company affiliate, any member bank or any other company, body politic or corporate, or any individual person, or with intent to deceive any officer of such company or of any member bank, or the Federal Reserve Board, or any agent or examiner appointed to examine the affairs of such holding company affiliate, shall be deemed guilty of a misdemeanor, and upon conviction thereof in any district court of the United States, shall be fined not more than \$5,000 or shall be imprisoned for not more than five years, or both, in the discretion of the court.

"No State member bank or trust company shall, (1) make any loan on the stock of any holding company affiliate which owns or controls such State member bank or trust company directly or indirectly, (2) make any loan to any holding company affiliate which owns or controls such State member bank or trust company directly or indirectly on the security of any shares of stock of any affiliate of such holding company affiliate, (3) make loans to any holding company affiliate amounting in the aggregate to more than 10 per cent of the unimpaired capital and

SECTION Continued

surplus of such member bank, or (4) be the purchaser or holder of the stock of such holding company affiliate; unless such security or purchase shall be necessary to prevent loss upon a debt previously contracted in good faith; and any stock so purchased or acquired shall be sold or disposed of at public or private sale within two years from the date of its acquisition."

SECTION 29

Paragraphs (b) and the first part of (c) are discussed under Section 11. Paragraph (a) appears to be too sweeping as it would include with a borrowing corporation all of its "subsidiaries or affiliates," terms which have not been defined in relation to industrial or other corporations. Therefore, we suggest omission.

The second part of Section 29 (c) is not clear, and appears to contemplate an undue control over an individual's use of funds obtained as dividends on bank stock. We suggest omission.

SECTION 31

In place of this provision as it stands we suggest the following substitute:

"Section 5211 of the Revised Statutes of the United States, as amended, is further amended, by adding at the end thereof the following new paragraph:

'Each national bank shall obtain and furnish to the Comptroller of the Currency such reports of the condition of any or all of its subsidiary affiliates as the Comptroller of the Currency, in his discretion, may require. Such reports shall be in form as the Comptroller of the Currency may prescribe, shall be verified by the oath or affirmation of the president or such other officer as may be designated by

SECTION 31 Continued

the board of directors of the affiliate to verify such reports, and shall cover the condition of the affiliate on dates fixed by the Comptroller of the Currency. Each such report shall be transmitted to the Comptroller of the Currency at the time required by the Comptroller of the Currency, and shall exhibit in detail and under appropriate heads all assets of the affiliate in question, their cost and present value, all liabilities of such affiliate, its earnings and expenses, and such other information as the Comptroller of the Currency may require. "

SECTION 32

In place of this provision as it stands, we suggest the following substitution:

"Section 5240 of the United States Revised Statutes, as amended, is further amended by adding at the end thereof a new paragraph reading as follows:

1 Examiners appointed under the provisions of the first paragraph of this section may examine any subsidiary affiliate of a national bank, when directed to do so by the Comptroller of the Currency. The examiner making the examination of any subsidiary affiliate of a national bank shall have power to make a thorough examination of all the affairs of the affiliate, and in doing so

SECTION 32 Continued

he shall have power to administer oaths and to examine any of the officers and agents thereof under oath and shall make a full and detailed report of the condition of the affiliate to the Comptroller of the Currency. The expense of examinations provided for in this paragraph shall be assessed by the Comptroller of the Currency upon the affiliates examined in proportion to assets or resources held by the affiliates upon the dates of examination of the various affiliates. If the officers, directors, or stockholders of any affiliate of a national bank shall refuse to permit an examiner to make an examination of the affiliate which the Comptroller of the Currency has directed to be made, refuse to give any information required in the course of any such examination, or refuse to pay the expense of any such examination, the national bank with which it is affiliated shall be subject to a penalty of not more than \$1,000 for each day that any such refusal shall continue. Such penalty may be assessed by the Comptroller of the Currency, in his discretion and, when assessed, may be collected by the Comptroller of the Currency by suit or otherwise. All sums of money collected for penalties under this paragraph shall be paid into the Treasury of the United States. 1"

ADDITIONAL NEW SECTIONS

Borrowing by bank officers and employees

Borrowing by officers and employees of banks has in some cases caused serious complications and difficulties. It would seem to us proper that persons connected with banks should not borrow money from brokers or dealers in securities and should not borrow either from their own bank or from another bank without approval of a properly constituted committee. This would not prevent legitimate borrowing, but would act as a check on speculative borrowing by bankers and their employees.

Section _____. Section 22 of the Federal Reserve Act, as amended, is amended by adding the following paragraph after paragraph (e) and renumbering paragraph (f) as paragraph (g).

"(f) No Federal reserve agent nor any of his assistants or employees and no officer or employee of any Federal reserve bank or of any member bank shall hereafter borrow money from, or otherwise become indebted to, any broker or dealer in stocks, bonds, or other investment securities. No Federal reserve agent nor any of his assistants or employees and no officer or employee of any Federal reserve bank or of any member bank shall hereafter borrow from any bank or banker upon collateral consisting of stocks, bonds, or other investment securities, or upon an unsecured note, without the written consent of a committee consisting

SECTION _____ Continued

of not less than three of the directors of the bank of which he is an officer or employee. Such committee shall be appointed at a regular meeting of the directors of such bank; and not more than one of its members shall be an officer of the bank. It shall be the duty of such committee to require written financial statements of all officers and employees of such bank desiring to borrow upon the security of stocks, bonds, or other investment securities, or upon an unsecured note and to determine whether such borrowing is contrary to the interests of such bank; and such committee shall maintain records of its proceedings which, together with the financial statements of such officers and employees, shall be open to inspection by authorized examiners examining such banks.

"No member bank shall hereafter make any loan or advance on the security of stocks, bonds, or other investment securities, or upon an unsecured note to any Federal reserve agent nor to any of his assistants or employees or to any officer or employee of any Federal reserve bank or of any member bank without the written consent of a committee of directors of the bank of which the person obtaining such advance is an officer or employee, appointed in accordance with the provisions of this subsection."

Branches of state member banks

In our earlier report we recommended extension of the branch banking privilege of national banks, but by inadvertence did not provide for a similar extension for state member banks. The following section corrects this omission by placing state member banks on an equality with national banks in so far as the state laws will permit.

Section _____. The second paragraph of Section 9 of the Federal Reserve Act, as amended, is amended and reenacted to read as follows:

"No bank admitted to membership pursuant to the provisions of this section shall establish any branch beyond the corporate limits of the city, town, or village in which its head office is located unless it has a paid-up and unimpaired capital of not less than \$1,000,000 and first obtains the permission of the Federal Reserve Board: Provided, however, That no such bank shall be permitted to establish any branch beyond the territorial limits within which national banks are permitted by law to establish branches at the time. The term 'branch', as used in this section, shall be held to include any branch, branch office, branch agency, additional office, or any branch place of business at which deposits are received, or checks paid, or money lent."