June 6, 1916.

MEMORANDUM ON SECTION 8 OF THE CLAYTON ACT.

To All Federal Reserve Agents:

The provisions of Section 8 of the Clayton Anti-Trust Act which relate to interlocking bank directorates go into effect on October 15, 1916. As originally enacted by Congress, this Section provided in substance

(a) That no person shall at the same time be director or other officer or employee of more than one bank or trust company organized or operating under the laws of the United States, provided either of such banks or trust companies has resources aggregating more than $5,000,000.

The phrase "organized or operating under the laws of the United States," has been construed to apply not only to national banks, but also to State banks and trust companies which are members of the Federal Reserve System.

(b) That no private banker or person who is a director in any State bank or trust company whose resources aggregate more than $5,000,000 shall be eligible to serve at the same time as a director in any bank or banking association organized or operating under the laws of the United States. It will be noted that this particular provision applies only to directors and not to officers and employees.

(c) That no bank or trust company organized or operating under the laws of the United States located in any city of more than 200,000 inhabitants shall have as a director or other officer or employee any private banker or any director or other officer or employee of any other bank or trust company located in the same place.

The Act makes certain exceptions to these provisions:

(a) They do not apply to mutual savings banks not having a capital stock represented by shares.

(b) They do not in any way prohibit a person who is a Class "A" director of a Federal reserve bank from being an officer or director or both an officer or director in one member bank.

(c) They do not apply to banks or trust companies where the entire capital stock of one is owned by stockholders in the other.

On May 15, 1916, Congress passed an amendment to Section 8 of the Clayton Act which is intended to make further exceptions to its restrictions, provided the consent of the Federal Reserve Board is first obtained. This amendment provides that nothing in Section 8 of the Clayton Act shall prohibit any officer, director or employee of any member bank or Class "A" director of a Federal Reserve Bank who shall first procure the consent of the Federal Reserve Board from being an officer, di-

director or employee of not more than two other banks, banking associations, or trust companies, whether organized under the laws of the United States or any State, if such other bank, banking association or trust company is not in substantial competition with such member bank.

This amendment, which is in the form of a proviso, does not affect or alter the classes of ineligible directors, officers, etc., as defined by Section 8 before amendment. It merely provides that a person who is an officer or director of a member bank may, with the approval of the Federal Reserve Board, be an officer or director of not more than two other banks or trust companies, whether State or national, in which he otherwise would have been ineligible to serve, provided such other banks or trust companies are not in substantial competition with the member bank of which he is andirector or officer.

Under the provisions of this amendment it will be necessary for every director, officer, or employee of a member bank to apply for the approval of the Federal Reserve Board to serve as a director, officer, or employee of any other bank or trust company which comes within the inhibitions of Section 8 of the Clayton Act and which is not in substantial competition with his own bank. In this connection it may be mentioned that if a director of a member bank desires to serve as a director of

two State banks or trust companies which are not members of the Federal Reserve System, the sole test is whether such other State banks or trust companies are in competition with the member bank and it is immaterial whether they are in competition with each other.

The Federal Reserve Board, before passing upon these applications, will in each case call upon the Federal reserve agents for a report. It will, therefore, be necessary to lay down for the Federal reserve agents certain broad lines that will be observed in dealing with these applications.

The most important task will be to define what the Board will consider "substantial competition".

Perhaps it may be the easiest way of approach to consider and decide first what shall not constitute "substantial competition".

Answering this question, it should be said that the mere fact that two banks ("bank" hereinafter will include national banks, trust companies or State banks) are in the same locality or of similar size, or that they both belong to the same class of "banks" or that they both are buying commercial paper or securities, or take deposits, or are doing a trust company business, does not constitute "substantial competition". If the mere fact that two banks are taking deposits or are buying commercial paper or bonds should be considered to be "substantial competition", it would be

paramount to excluding directors, officers or employees (hereinafter called "directors") from serving on any other "bank", because they all would be in "substantial competition".

The question is, then, not on the broad character of the functions exercised by these banks, but the determining point of criticism must be the extent and manner in which these functions are exercised.

Two men in the United States each wanting a glass of water can not be said to be competing with each other where they are standing on the banks of a stream affording sufficient water for all. If, on the other hand, two men in the desert need water, there will indeed be very substantial competition for a single glass of water, the supply being limited to that amount.

Two such extreme cases are fairly obvious. The question becomes more difficult of determination, however, as the facts in each case converge from those extremes. Take, for instance, a community supplied by a single reservoir of water, Though there may be an ample amount for all, it is apparent that severe competition or a tendency to monopolize may result from an effort on the part of one to succeed in supplying himself plentifully at the expense of the others, securing thereby a stronger position either for fixing the market price of the water or for arbitrarily discriminating in offering or permitting its enjoyment. In dealing then, first with the object competed for it is clear that if it is

of such broad and general nature and existing in such generous supply that it may be considered a general commodity with a wide market, the mere fact that two banks require such commodity would not make them competing. It would make them competing only if the commodity which they both desire and can reach were of so restricted a nature that, in trying to acquire it, they would materially affect each other's supply. In other words, where both banks take the same kind of deposits, buy the same kind of paper and securities they must for a substantial portion of their regular business be tapping the same limited or individual field in order to be considered as substantially competing.

This test should apply irrespective of the location of the two banks in question, though the distance from each other may be an important factor in determining how much each depends upon the same sources of supply. There may be the same class of banks not remote from each other - conceivably in the same city - which do not compete because the main business carried on by them may be of an entirely different character. The one may be in the business center, taking business accounts and making business loans and not paying interest on deposits; the other may be an up-town bank, having private accounts, not making business loans and paying interest on deposits of individuals. It is well conceivable that such two banks may be considered as not in substantial competition, even though, for certain investments, they

might have to resort to the same class of investments, but find them in broad market, such as call loans, time loans or commercial paper.

It is possible, on the other hand, that banks of the same class, even though remote from each other, might be doing substantially the same kind of business, and might, therefore, be competing in precisely the same fields and for the same commodities. Such banks are those whose business are so important in scope that they reach into far-distant territories. To illustrate, certain large banks in Chicago and New York, for instance, have ceased to be local institutions. They are banks that have their connections all over the country, that compete with one another in dealing with the deposits of large corporations in purchasing their securities, and it is conceivable that such large banks with such ramifications may be considered as competing even though geographically remote from each other, while two smaller banks in the same cities doing substantially the same character of business would not be held as competing. The degree of such competition must depend upon the facts of each case, and whether the banks in question are "in substantial competition" must be decided by the Federal Reserve Board after a review of such facts and the recommendations or report of the Federal reserve agent.

The Board proposes to adopt the method of advising each Federal reserve bank of the applications made by each director. To illustrate, if a Philadelphia director should wish to retain a directorship in New York and, at the same time, one in Chicago, all three Federal reserve agents will be advised of the three directorships involved in the case. They will be requested particularly to investigate the local concern involved in the application and will all three receive copies of the reports of their fellow Federal reserve agents, so that they will be in a position to study the entire case before making their recommendations. The Federal Reserve Board's special committee, after having heard from all Federal reserve agents involved in the application, will make its final recommendation to the Board.

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