Washington, D. C., July 20, 1916.

MEMORANDUM FOR THE BOARD SUBMITTED THROUGH COUNSEL'S OFFICE

By Breckinridge Jones.

One prime objection on the part of State banks and trust companies to becoming member banks is while a national bank has its rights fixed by Federal statutes and a change can come only by an Act of Congress, a State bank or trust company becoming a member bank is subject to the discretion of the Federal Reserve Board as expressed from time to time in rules and regulations passed by the Federal Reserve Board.

It appears that under the construction placed by the Federal Reserve Board on the Reserve Act this latter statement is true. It seems clear that under the circulars relating to the admission of State banks and trust companies issued by the Board the Board has so construed the Act. The result is that State banks and trust companies have found this one of the main causes that has led them to refrain from becoming member banks - the fear being that the State institution might be deprived of some of its charter powers.

A trust company might come in under rules and regulations that do not deprive it of some of its charter powers; and, yet being in, if, the Board has the power to make such rules and regulations subsequent changes might be made so as to so restrict the trust company operations as to deprive it of an essential part of its business.

This objection is fundamental.

When a State bank or trust company becomes a member bank its status and rights, so far as the Federal Reserve Act is concerned, should be as crystallized and definite as are those of the national bank - that is, to be subject to change only by an Act of Congress.

My contention is that this is true under the Federal Reserve Act and that a contrary view has obtained only because of error on the part of the Federal Reserve Board in construing the Federal Reserve Act.

Under the National Bank Act and the Federal Reserve Act the status and rights of a national bank are clearly set out yet thereunder the Comptroller has the right to make "rules and regulations" but these relate only to the modus operandi

and are administrative only in their features.

So I contend that the Federal Reserve Act expressly fixes the requirements to be met by a State bank or trust company in being admitted as a member bank and the right of the Federal Reserve Board to make rules and regulations was intended by Congress to relate only to the modus operandi, or merely to be administrative features.

(A brief on this subject was filed by me with the Federal Reserve Board some months ago and copy of it is handed herewith to Judge Elliott)

My plea is that the Board pass a resolution adopting this construction of the Federal Reserve Act. If it will do so then the subsequent changes in the circulars and forms relating to the admission of State banks and trust companies as heretofore issued by the Board become matters of detail easily made to harmonize.

There is nothing in this suggestion tending to weaken the Reserve System or to impair the right of examination and supervision on the part of the Board.

If a State bank applies to become a national bank the Comptroller has the power to examine and see that the bank is sound and if it is admitted as a national bank the Comptroller has ample power under his rules and regulations to see that it obeys the laws of its being. So when a State bank or trust company applies to become a member bank the Federal Reserve Board, through its proper agencies, has power to examine and see that the applying institution is sound, and if it is admitted the Board has ample power to see that it remains sound and that it obeys the laws of its being.

But some one objects. Suppose a bank or trust company has under its charter the right to do certain kinds of business not ordinarily incidents of banking?
For example -

(1) Acting as executor or administrator.
(2) Becoming surety on the bond of an individual acting in such capacity.
(3) Insuring lives and granting annuities.
(4) Doing a farm loan business.
(5) Issuing debentures against real estate loans.
(6) Buying, selling and investing in bonds, stocks, and other investment securities, etc., etc.

My answer is that when Congress expressly provided for State banks and trust companies, when incorporated under general laws or special charters, coming into the System under the express limitations set out in the Act, it had in view that such State institutions were different from national banks, having powers beyond the powers of national banks.

Moreover, what difference does it make to the Federal Reserve Board what powers the States have given these institutions so long as the Board has ample power to see that these institutions are safe and sound and comply with the laws of their being. If they come in they must buy stock in a regional bank, must keep reserve there, and can get Federal reserve notes only to the extent that they have paper eligible for discount.

As a practical conclusion, unless a State bank or trust company has business of a kind that will enable it to avail itself of the benefits of the Reserve System it will not ask to come in.

One of the provisions of the Federal Reserve Act is objected to by nearly every national bank and has been and is a prime cause in keeping out of the System State banks and trust companies.

I refer to Section 22.

The objections to that Section have been urged so often by so many that I need not repeat them. Judge Elliott is familiar with them.

It is not difficult to suggest an amendment that will fairly answer objections and yet leave the Section effective to prevent the faults hit at by its authors. Judge Elliott has the form of such an amendment.

It would be easy to get hundreds of petitions for this change but such a public campaign would be unwise at this time. The Currency Committees in the Senate and House would readily understand the proposition. If the amendment could be recommended by the Board and put through this session of Congress and the Board would construe the Act as indicated in the first paragraph of this memorandum, I believe a large number of State banks and trust companies would promptly come into the System, and the popularity of the System would be established.

BRECKINRIDGE JONES.

7/24/16.