October 2, 1917.

SUBJECT: Right of the Federal Reserve Board to grant to national banks in New York permission to act as trustee, executor, administrator, and registrar of stocks and bonds.

My dear Governor:

The Federal Reserve Board has heretofore declined to grant to national banks in New York permission to exercise any of the powers enumerated in Section 11 (k) of the Federal Reserve Act except the right to act as registrar of stocks and bonds.

Section 11 (k) authorizes the Federal Reserve Board -

"To grant by special permit to national banks applying therefor, when not in contravention of State or local law, the right to act as trustee, executor, administrator, or registrar of stocks and bonds under such rules and regulations as the said board may prescribe".

In acting upon applications filed under authority of this section, the policy of the Board has been to refuse the application of any bank which is located in a state the laws of which expressly or by necessary implication prohibit a national bank from exercising any of the powers enumerated in the statute.

Section 223 of the New York Banking Laws provides as follows:

"No corporation other than a trust company organized under the laws of this State shall have or exercise in this State the power to receive deposits of money, securities or other personal property from any person or corporation in trust, or have or exercise in this State any of the powers specified in subdivisions one, four, five, six, seven and eight of section one hundred eighty-five of this article (viz. to act as fiscal or transfer agent, as trustee under any corporate mortgage, as trustee or agent for married women, as guardian, receiver or trustee of the estate of any

"minor and as depositary of any moneys paid into court, to act under court appointment as trustee guardian, receiver or committee of the estate of a lunatic, etc , or as receiver of any person in insolvency or as executor or trustee under a will or as administrator, or to act as trustee of any estate), nor have or maintain an office in this state for the transaction of, or transact, directly or indirectly, any such or similar business, except that a federal reserve bank may exercise the powers conferred by subdivision one of such section (fiscal or transfer agent) if authorized so to do by the laws of the United States and any domestic corporation legally exercising any of the powers conferred by such subdivision at the time this act takes effect may continue to exercise such powers, and a trust company incorporated in another state may be appointed and may accept appointment and may act as executor of, or trustee under, the last will and testament of any deceased person in this state, provided trust companies of this state are permitted to act as such executor or trustee in the state where such foreign corporation has his domicile * * * * * * * * * ".

It is because of this statute that the Federal Reserve Board has declined to grant to national banks the right to exercise any of the powers specified in Section 11 (k) except the power to act as registrar of stocks and bonds. This action of the Board was predicated upon the assumption (1) that Section 11 (k) vested in the States the right to determine by appropriate legislation whether or not national banks should exercise such powers, and (2) that it was the intention of the legislature of New York to prohibit all corporations (including national banks) other than trust companies organized under the laws of New York, from exercising such powers.

At the time that the Board adopted the policy above referred to the language of Section 11 (k) had not been construed by the courts. Since then it has been construed by the Supreme Courts of Illinois and Michigan and by the United States Supreme Court. In the case of Grant Fellows, Attorney General, vs. the First National Bank of Bay City, Michigan, the Supreme Court of Michigan held that since no statute of Michigan prohibited national banks from exercising trust powers the laws of that State would not be contravened by the exercise by a national bank of such powers but that the Act of Congress giving national banks this right was unconstitutional and void. This case was appealed

to the United States Supreme Court which held that the Michigan Court had erred in holding that Section 11 (k) was unconstitutional, and the judgment of the lower court was reversed.

In discussing the opinion of the Michigan Supreme Court the United States Supreme Court, through Mr. Chief Justice White, said:

> "In view of the express ruling that the enjoyment of the powers in question by the national bank would not be in contravention of the state law, it follows that the reference of the court below to the state authority over the particular subjects which the statute deals with must have proceed erroneous assumption that because a particular function was subject to be regulated by the state law, therefore Congress was without power to give a national bank the right to carry on such functions. But if this be what the statement signifies, the conflict between it and the rule settled in McCulloch v. Maryland and Osborn v. Bank, is manifest. What those cases established was that although a business was of a private nature and subject to state regulation, if it was of such a character as to cause it to be incidental to the successful discharge by a bank chartered by Congress of its public functions, it was competent for Congress to give the bank the power to exercise such private business in cooperation with or as part of its public authority. Manifestly this excluded the power of the State in such case, although it might possess in a general sense authority to regulate such business, to use that authority to prohibit such business from being united by Congress with the banking function, since to do so would be but the exertion of state authority to prohibit Congress from exercising a power which under the Constitution it had a right to exercise. From this it must also follow that even although a business be of such a character that it is not inherently considered susceptible of being included by Congress in the powers conferred on national banks, that rule would cease to apply if by state law state banking corporations, trust companies, or others which by reason of their business are rivals or quasi-rivals of national banks are permitted to carry on such business This must be since the state may not by legislation create a condition as to a particular business which would bring about actual or potential competition with the business of national banks and at the same time

"deny the power of Congress to meet such created condition by legislation appropriate to avoid the injury which otherwise would be suffered by the national agency. Of course as the general subject of regulating the character of business just referred to is peculiarly within state administrative control, state regulations for the conduct of such business if not discriminatory or so unreasonable as to justify the conclusion that they necessarily would so operate, would be controlling upon banks chartered by Congress when they came in virtue of authority conferred upon them by Congress to exert such particular powers. And these considerations clearly were in the legislative mind when it enacted the statute in question. This result would seem to be plain when it is observed (a) that the statute authorizes the exertion of the particular functions by national banks when not in contravention of the state law, that is, where the right to perform them is expressly given by the state law or what is equivalent is deducible from the state law because that law has given the functions to state banks or corporations whose business in a greater or less degree rivals that of national banks, thus engendering from the state law itself an implication of authority in Congress to do as to national banks that which the state law has done as to other corporations; and (b) that the statute subjects the right to exert the particular functions which it confers on national banks to the administrative authority of the Reserve Board giving besides to that Board power to adopt rules regulating the exercise of the functions conferred, thus affording the means of coordinating the functions when permitted to be discharged by national banks with the reasonable and non-discriminating provisions of state law regulating their exercise as to state corporations,- the whole to the end that harmony and the concordant exercise of the national and state power might result".

It therefore, becomes necessary for the Federal Reserve Board to reconsider, in the light of this decision of the United States Supreme Court the question whether national banks in New York should be granted the powers specified in Section 11 (k).

It will be observed that while the Court recognizes the right of a State to regulate the conduct of trust business, it holds that such regulations must not be "discriminatory or so unreasonable as to justify the conclusion that they necessarily would so operate".

Upon reconsideration of the question of the right of the Federal Reserve Board to grant permits to national banks in New York to exercise trust powers, the Board must not, in view of this decision, assume that Section 11 (k) vests in the States the unqualified right to determine by appropriate legislation whether or not a national bank may exercise such powers. The power of the State to enact such legislation is clearly subject under the opinion of the United States Supreme Court, to the qualification that such legislation must not be discriminatory against national banks. The court expressly holds that a "state may not by legislation create a condition as to a particular business which would bring about actual or potential competition with the business of national banks and at the same time deny the power of Congress to meet such created condition by legislation appropriate to avoid the injury which otherwise would be suffered by the national agency."

It is manifest, therefore, that in determining whether the exercise of trust powers by national banks will contravene State laws, the Board must consider whether the State law is one which discriminates against national banks.

The United States Supreme Court has in terms prescribed the rule by which such laws must be tested. In discussing Section 11 (k) the Court says -

> "the statute authorizes the exertion of the particular functions by national banks when not in contravention of the state law, that is, where the right to perform them is expressly given by the state law, or what is equivalent is deducible from the state law because that law has given the functions to state banks or corporations whose business in a greater or less degree rivals that of national banks, thus engendering from the state law itself an implication of authority in Congress to do as to national banks that which the state law has done as to other corporations".

Applying this test to Section 223 of the New York Banking Laws it is apparent that the legislature of New York has granted to trust companies organized under the laws of New York the right to exercise these powers and it is only necessary for the Board to consider whether such trust companies come into actual or potential competition with national banks. If the Board concludes that such companies are "rivals or quasi-rivals of national banks", it must interpret Section 223 of the New York Banking Laws as permitting national banks to exercise these powers. In other words, it

must construe that part of Section 223 which provides that "no corporation other than a trust company organized under the laws of this state shall have or exercise in this state the power to receive deposits of money, securities or other personal property from any person or corporation in trust etc " as relating to corporations other than national banks

In view of the fact that the records before the Board are sufficient to show that trust companies organized under the laws of New York compete with national banks in commercial deposits and loans, and in many other activities engaged in by national banks, it is respectfully recommended that no application of a national bank located and doing business in New York for permission to exercise the power of trustee, executor or administrator be refused by the Board on the ground that the exercise of such powers will contravene the laws of New York

Respectfully,

M C Elliott,

Counsel

Hon W P G Harding,
Governor