March 14, 1928

To Federal Reserve Board.

SUBJECT: Revision of the Clayton Act Regulation.

From Mr. Wyatt, General Counsel.

Due to the enactment of the amendment to the Clayton Act, which was signed by the President on March 9th, it is necessary to revise the Board's Regulation, pertaining to interlocking directorates under the Clayton Act; and I respectfully submit herewith for the Board's consideration a proposed draft of a revised regulation in such form as to show the exact textual changes proposed to be made in the Regulation.

Most of these changes are technical and are designed to make the Regulations conform to the provisions of the law as amended. There is one question, however, which is of considerable importance and to which, I believe, the Board should give especial attention, viz: What facts should the Board take into consideration in determining whether it will be "compatible with the public interest" to permit interlocking directorates between particular banks?

Heretofore, the Board has had only one question to consider in granting interlocking directorates, i.e., whether the banks were "in substantial competition". If the banks were in substantial competition the Board had no authority to permit interlocking directorates and could do nothing but refuse its permission. If the banks were not in substantial competition, the Board had discretionary authority to grant the application, and usually granted it without considering any other question.

As amended, however, the statute provides that the Federal Reserve Board may issue a permit "if in its judgment it is not incompatible with the public interest". This clearly gives the Board much broader authority than it previously had, and it would seem that such increased authority carries with it an increased responsibility. Moreover, the question whether it is compatible with the public interest for a person to serve as director of two or more banks coming within the prohibitions of the Clayton Act would seem to be a broader question than the mere question whether such banks are in substantial competition.

Every time the Board grants permission for interlocking directorates under the law as amended the issuance of such a permit will be equivalent to an expression of the Board's opinion that it is compatible with the public interest for the applicant to serve as director of all the banks involved and for such banks to have interlocking directorates. In passing upon each application, therefore, it is the Board's duty to take into consideration every fact which would have a bearing upon the question whether it is compatible with the public interest to grant a permit, and it would seem that the applicants should be advised in advance as to the facts which the Board will consider in formulating its judgment on this question.

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In revising the regulation, therefore, I have stricken out all reference to substantial competition; and, in lieu of the old definition of that term, have inserted, as Section IV(d), a proposed statement of what the Board will take into consideration in determining whether the issuance of such a permit would be compatible with the public interest. This is a difficult question and I am not prepared definitely to recommend the adoption of the statement which I have drafted. I submit it, however, for the Board's consideration and shall discuss below my reasons for suggesting these various points. In deciding whether it would be compatible with the public interest for a person to be permitted to serve as director of two or more banks coming within the prohibitions of the Clayton Act, it is obvious that the Board should consider (1) whether the banks are natural competitors, and (2) whether the existence of such an interlocking directorate would tend to lessen competition between such banks; since the main purpose of the original Clayton Act was to prevent a lessening of competition and a restriction of credit.

It seems to me that it would also be proper for the Board to consider whether the banks involved have conflicting interests and whether the applicant will be able faithfully to serve both of them. In other words, it would seem to be incompatible with the public interest for the Board to sanction a person serving as director of a bank when he has interests adverse to that bank. Thus, it might be considered incompatible with the public interest for a director of a large bank with branches to serve also as director of a small independent bank which is resisting absorption into the branch system of the larger bank.

It may also be appropriate for the Board to consider whether the service by the applicant as officer, director or employee of more than one of the banks involved would prevent him from giving proper attention to the affairs of all of the banks involved or from properly discharging his duties to all of them. It seems obvious that the public is vitally concerned with the proper management of banks, since bank failures always affect the public adversely, and one of the most frequent causes of bank failures is poor management, which usually is due to the lack of proper attention to the bank's affairs by the directors thereof. Conceivably, a person might make an excellent director for one bank, but would be unable to give proper attention to the affairs of three banks, especially if such banks are located in widely different parts of the country. The Supreme Court has said that a person should not accept the position of director of a bank, unless he is able to attend the directors' meetings regularly and faithfully to discharge his duties by acquainting himself with the bank's affairs and intelligently participating in the supervision of its management by the Board of directors.

It would also seem that the Board should take into consideration any other facts having a bearing upon the interest of the public in the banks involved, in so far as such interest is affected by their having the same directors, officers or employees.

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While I am not prepared to recommend unqualifiedly the statement on this subject which I have drafted, therefore, I submit it for the Board's consideration and believe that it is worthy of careful attention.

Respectfully,

Walter Wyatt,
General Counsel.

Draft attached.

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