

FEDERAL RESERVE BOARD

WASHINGTON

ADDRESS OFFICIAL CORRESPONDENCE TO
THE FEDERAL RESERVE BOARD

X-6692

September 4, 1930.

SUBJECT: Topic for Fall Conference - Revision of
Membership Condition re Purchase of Bank Stocks.

Dear Sir:

The replies to the Board's letter of June 27, 1930, (X-6646) relative to the advisability of a revision of the condition of membership regarding the purchase of stock in other institutions by State member banks, disclose a considerable variance of opinion on the question and accordingly the Board has decided to refer the matter to the Conferences of Governors and Federal Reserve Agents which convene on October 6.

For your information there is enclosed copy of a memorandum prepared by the Board's Assistant Counsel summarizing the replies to the circular letter referred to above.

Very truly yours,

E. M. McClelland,
Assistant Secretary.

Enclosure.

TO ALL GOVERNORS AND FEDERAL RESERVE AGENTS.

August 9, 1930.

The Federal Reserve Board Proposed revision of condition No. 3,
Mr. Wingfield, Assistant Counsel. Section IV, of Board's, Regulation H.

Under the present provisions of condition No. 3 of Section IV of the Board's Regulation H, a State member bank subject to such condition may not purchase any of the stock of another bank or trust company unless it obtains in each case the permission of the Federal Reserve Board. Recently the Board considered the advisability of revising this condition so as to permit State member banks subject to it to purchase a limited percentage of the capital stock of other banks and trust companies without being under the necessity of obtaining the Board's permission to make such purchases. This office was requested to prepare a draft of a revision of condition No. 3 along this line. The following revision of this condition was accordingly prepared and submitted to the Board:

"(3) Such bank or trust company, except after applying for and receiving the permission of the Federal Reserve Board, shall not acquire more than 50 per cent of the capital stock of any other bank or trust company; and, except with the Board's permission, its total investments in the stock of other banks and trust companies shall not exceed 20 per cent of its own capital stock and surplus."

Before reaching a determination as to whether this revision of condition No. 3 should be adopted, however, the Board decided to submit it to the Governors and Federal Reserve Agents of all Federal reserve banks for their suggestions. The Board accordingly on June 27, 1930, addressed a letter (X-6646) to all Governors and Federal reserve agents and requested them to advise the Board whether in their opinion a revision of this condition of membership No. 3 was advisable and as to whether the percentages contained in the revision above quoted with reference to the amount of stock of other banks and trust companies, which might be purchased by a member bank were appropriate and advisable. Replies to the Board's letter have now been received from all of the Governors and Agents and these replies will be summarized for the Board's information.

It appears that six of the Governors and Agents are of the opinion that it is not desirable for the Board at this time to make any change in the condition No. 3 contained in Section IV of the Board's Regulation H. In this connection, the Board's special attention is called to the letters received from Governor Black of Atlanta, Governor Harrison of New York, and Mr. Heath of Chicago, which set out in some detail the objections to a change in the present provisions of this condition. These letters discuss the question whether it is advisable for the Board to retain any condition of membership with reference to

the purchase of bank stocks. They point out, however, that group and branch banking is being investigated with a view to possible legislation on the subject and that the Board itself has appointed a committee to investigate group and branch banking. Under these circumstances, they suggest that any change in condition No. 3 should be deferred until a later date.

All of the other Governors and Federal reserve agents seem to feel that some change in this condition is desirable. Three of this latter group believe that it is advisable for the Board to eliminate from its Regulations entirely the condition No. 3. The others believe it is desirable for the provisions of this condition to be revised so as to permit a member bank to purchase limited amounts of the stock of other banks and trust companies without obtaining specific permission from the Board. Various percentages with reference to the amount of stock which should be purchased without the Board's permission are suggested by these Governors and Federal Reserve Agents. One Governor and two Federal Reserve Agents think that the percentages contained in the revision above quoted are appropriate. The great majority, however, feel that these percentages are too liberal and in most cases suggest considerably lower percentages of varying amounts. In this connection the particular attention of the Board is called to the letters of Governor Norris of Philadelphia, Governor Martin of St. Louis, and Mr. Walsh of Dallas.

The replies of each of the Governors and Federal Reserve Agents will be summarized for the Board's information in greater detail below:

SUMMARY OF REPLIES

BOSTON.

Deputy Governor Paddock.— Deputy Governor Paddock believes that condition No. 3 might well be eliminated entirely because it does not provide satisfactory control of group banking. If condition is to be retained, however, he suggests that a member bank be not permitted to purchase more than 40 per cent of the capital stock of any other bank or trust company without the Board's permission and that the limit of its total investments in bank stocks should be 40 per cent of its own capital and surplus.

Mr. Curtiss - Mr. Curtiss believes that it would be desirable to eliminate condition No. 3 entirely because this condition is not effective in giving the Board control over group banking. If the condition is to be retained, however, he suggests that the purchase without the Board's permission by a member bank of stock of any other bank or trust company be limited to 40 per cent of the capital of such other bank or trust company. It is not clear what limit with reference to total investments in the stock of other banks and trust companies he believes is desirable.

NEW YORK.

Governor Harrison.- Governor Harrison suggests the desirability of eliminating entirely the condition of membership No. 3. He further suggests, however, that any amendment of this condition of membership be deferred until after the committee appointed by the Board to investigate group and chain banking has made its report. Governor Harrison appears to feel that condition of membership No. 3 would not be effective in controlling group and chain banking and that investment in bank stocks by State member banks is not inadvisable, unless the aggregate amount of such investments by any one member bank is such as to indicate that the member bank's general investment policy is unsound.

Mr. Case.- Mr. Case has advised the Board that he concurs in Governor Harrison's letter.

PHILADELPHIA.

Governor Norris.- Governor Norris believes that a revision of the Board's condition of membership No. 3 is desirable. He suggests that the purchase by a member bank of stock of any other bank or trust company without the Board's permission be limited to 20 per cent of the capital stock of such other bank or trust company and that the total amount of bank stock a member bank may purchase be limited to 5 per cent of its own capital and surplus, or at the most to 10 per cent of its own capital and surplus.

Mr. Austin.- Mr. Austin believes that a change in the Board's condition of membership No. 3 is desirable. He suggests that the purchase by a member bank of stock in any other bank or trust company be limited to 20 per cent of such other bank's capital stock without the Board's permission and also suggests that the total investment by a member bank in bank stocks be limited to 20 per cent of its own capital and surplus. Mr. Austin also suggests that if this condition is revised, it be so framed that it is applicable to member banks which are now subject to this condition in its present form or in the form in which it was applied prior to the Board's Regulations, Series of 1928.

CLEVELAND.

Governor Fancher and Mr. DeCamp.- Governor Fancher and Mr. DeCamp have replied to the Board's letter (X-6646) in a joint letter.

They seem to feel that if the Board's condition of membership No. 3 is revised as proposed, group banks will be able to evade the spirit of this condition by reason of the fact that several member banks which are members of a particular group might hold the permitted amount of stock in a particular bank and the aggregate amount so held by all members of the group would constitute control of the bank. They suggest, however, that the total amount of bank stock which a member bank might purchase should not without the Board's permission exceed 20 or 25 per cent of its own capital and surplus. They seem to feel that a revision of the condition so as to permit a member bank without the Board's specific permission to purchase up to 50 per cent of the capital of any one bank or trust company is not inadvisable.

RICHMOND.

Governor Seay and Mr. Hoxton. - Governor Seay and Mr. Hoxton have also made a joint reply to the Board's letter (X-6646). They suggest that the revision of the Board's condition of membership No. 3 contained in this letter is extremely liberal and goes much further than could be reasonably expected. They suggest that the amount of stock of any bank which a member bank may purchase without the Board's permission be placed at 25 per cent of the capital of such other bank or trust company. They further suggest that the total amount of bank stock which a member bank may purchase without the Board's permission be fixed at 20 per cent of the capital and surplus of the member bank.

ATLANTA.

Governor Black. - Governor Black feels that there should be no change in the present provisions of the Board's condition of membership No. 3. He feels that this condition should not be liberalized because (1) national banks are not permitted to purchase bank stock, (2) the Board might be accused of fixing in its regulation the wrong percentage, since what would be a proper limitation in one case might be obviously improper in another, and (3) that a change in this condition, while legislation on the subject of group banking is being considered, might be politically construed either as an aid or an obstacle to group, chain or branch banking.

Mr. Newton. - Mr. Newton feels that no change in the Board's condition of membership No. 3 is desirable because a particular bank might not be justified in purchasing any number of shares of the stock of another bank and each case should stand upon its own merits.

CHICAGO.

Governor McDougal. - Governor McDougal suggests that the Board's condition of membership No. 3 be eliminated entirely from the Board's conditions of membership. It appears that he does not feel that the Board should, by retaining this condition, attempt either to restrain or encourage group banking.

Mr. Heath. - Mr. Heath suggests that the Board's condition of membership No. 3 should remain unchanged or should be eliminated from the Board's conditions of membership entirely. He points out that if a member bank is permitted without the Board's permission to purchase up to 50 per cent of the capital of any one bank and purchase an aggregate amount of bank stock up to 20 per cent of its own capital and surplus, a large member bank could actually control a considerable number of smaller banks and thus become a holding company for a group banking system of considerable size. Mr. Heath feels, therefore, that the proposed revision of condition of membership No. 3 with the percentages contained in this provision, as set out in the Board's letter (X-6646) would constitute virtual approval of the principle of group banking. Mr. Heath further suggests that the Board has appointed a committee to investigate all phases of group, chain and branch banking and that it would not be advisable to liberalize the provisions of condition of membership No. 3 in advance of the report of this committee, which may possibly make an adverse report on the principle of group banking.

ST. LOUIS.

Governor Martin. - Governor Martin suggests that condition of membership No. 3 be revised so as to limit the purchase by a member bank without the Board's permission of stock in any other bank or trust company to 20 per cent of capital of such other bank or trust company and to limit the total investments in bank stock by a member bank, to 20 per cent of its own capital stock and surplus.

Mr. Wood. - Mr. Wood suggests that the condition of membership No. 3 be revised so as to limit the right of a member bank to purchase stock either directly or indirectly through an affiliated corporation or otherwise in any other bank or trust company, without the Board's permission, to 20 per cent of the capital of such other bank or trust company. Mr. Wood does not suggest any limitation on the aggregate amount of bank stock which a member bank may purchase without the Board's permission.

MINNEAPOLIS.

Governor Geery. - Governor Geery feels that a revision of the Board's condition of membership No. 3 is desirable and he suggests that a member bank should be authorized to purchase without the Board's permission not more than 25 per cent of the stock of any other bank or trust company and to invest not more than 20 per cent of its own capital and surplus in the stocks of all other banks and trust companies.

Mr. Mitchell. - Mr. Mitchell states that he thinks the amount of bank stock that a member bank should be permitted to hold should be limited to the smallest possible amount, since a national bank is not permitted to invest in any bank stock, he feels that a State bank or trust company should not be permitted to do so. It appears, therefore, that Mr. Mitchell is of the opinion that no change should be made in the present provisions of the Board's condition of membership No. 3.

KANSAS CITY.

Governor Bailey. - Governor Bailey feels that it is desirable to liberalize the present provisions of the Board's condition of membership No. 3. He suggests that a member bank be authorized to purchase not more than 25 per cent of the capital stock of any other bank or trust company without the Board's permission and that such a member bank be authorized to make aggregate investments in the stocks of all banks and trust companies not in excess of 25 per cent of its own capital and surplus.

Mr. McClure. - Mr. McClure feels that a liberalization of the present provisions of the Board's condition of membership No. 3 is advisable and he feels that the percentages of 50 per cent and 20 per cent, respectively, contained in the revised condition set out in the Board's letter (X-6646) are reasonable limitations on the amount of stock of any one bank which may be purchased by a member bank and on the aggregate amount of bank stock which may be purchased by a member bank.

DALLAS.

Governor Talley. - Governor Talley feels that a revision of the Board's condition of membership No. 3 is desirable, but suggests that a member bank should not be permitted to purchase more than 20 per cent of the capital stock of any one bank or trust company except with the Board's permission, and that the total investments in bank stocks by a member bank should be limited to 10 per cent of the capital and surplus of the member bank.

Mr. Walsh. - Mr. Walsh believes that the revision of the Board's condition of membership No. 3 is desirable, but believes that the percentages of 50 per cent and 20 per cent contained in this revision as set out in the Board's letter (X-6646) should be reduced to 25 per cent and 10 per cent, respectively.

SAN FRANCISCO.

Governor Calkins. - Governor Calkins approves the proposed revision contained in the Board's letter (X-6646) including the percentages of 50 per cent and 20 per cent contained therein. He states that he would be in favor of a limitation upon the purchase of stock of any one bank below the 50 per cent contained in the Board's proposed revision, if such condition was practically enforceable. He believes, however, that it can be evaded, and, therefore, approves the condition as set out in the Board's letter.

Mr. Sargent. - In the absence of Mr. Newton, Mr. Sargent, Assistant Federal Reserve Agent at San Francisco, advises that a revision of the Board's condition of membership No. 3 is desirable. He approves the revision of this condition contained in the Board's letter (X-6646) containing the percentages contained therein of 50 per cent and 20 per cent, respectively.

For the Board's information, percentages the various Governors and Federal Reserve Agents have suggested the proposed revision of condition of membership No. 3 should contain may be briefly set out as follows:

		Per cent of stock of any one bank	Per cent of capital and surplus of member bank may be invested in bank stock
BOSTON -	Deputy Governor Paddock	40%	40%
	Mr. Curtiss	40%	--
NEW YORK -	Governor Harrison	0%	0%
	Mr. Case	0%	0%
PHILADELPHIA -	Governor Norris	20%	5% or 10%
	Mr. Austin	20%	20%
CLEVELAND -	Governor Fancher	50%	20% or 25%
	Mr. DeCamp	50%	20% or 25%

Per cent of stock : Per cent of cap-
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: of member bank may
: be invested in bank
: stock

RICHMOND	- Governor Seay	25%	20%
	Mr. Hoxton	25%	20%
ATLANTA	- Governor Black	0%	0%
	Mr. Newton	0%	0%
CHICAGO	- Governor McDougal	---	---
	Mr. Heath	0%	0%
ST. LOUIS	- Governor Martin	20%	20%
	Mr. Wood	20%	---
MINNEAPOLIS	- Governor Geery	25%	20%
	Mr. Mitchell	0%	0%
KANSAS CITY	- Governor Bailey	25%	25%
	Mr. McClure	50%	20%
DALLAS	- Governor Talley	20%	10%
	Mr. Walsh	25%	10%
SAN FRANCISCO	- Governor Calkins	50%	20%
	Mr. Sargent	50%	20%

Respectfully,

B. M. Wingfield,
Assistant Counsel.

BMW: vbr - omc