FEDERAL RESERVE BOARD

WASHINGTON

ADDRESS OFFICIAL CORRESPONDENCE TO
THE FEDERAL RESERVE BOARD

X-7287

November 7, 1932.

SUBJECT: Glass Bill, S. 4412.

Dear Sir:

The Federal Reserve Board has previously forwarded to you copies of the so-called Glass Bill, S. 4412, which was reported to the Senate by the Banking and Currency Committee of that body on April 18, 1932, as well as copies of the accompanying majority and minority reports of the Committee. You have also been furnished with copies of the hearings on the bill which were held before the Senate Committee in March when the bill was under consideration as S. 4115. The Board's report to the committee was printed in connection with Governor Meyer's testimony in these hearings and was also included in the Federal Reserve Bulletin for April, 1932. There are inclosed herewith two copies of a memorandum (X-7139) which presents a comparison of the more important features of S. 4412 and S. 4115 with the changes recommended by the Federal Reserve Board.

As the bill may be taken up again at the forthcoming

session of Congress, the Federal Reserve Board will be glad to receive any suggestions regarding its provisions which you desire to submit for the Board's consideration, together with your reasons for such suggestions.

Very truly yours,

Chester Morrill,
Secretary.

Inclosures.

TO ALL CHAIRMEN AND GOVERNORS.

S. 4412, INTRODUCED APRIL 18, 1932.

PROVISIONS OF THIS BILL COMPARED WITH S. 4115 WITH CHANGES RECOMMENDED BY FEDERAL RESERVE BOARD.

There is set forth below a comparison of the more important features of S. 4412, which was introduced in the Senate and reported by the Committee on Banking and Currency on April 18, 1932, and S. 4115 with the changes recommended by the Federal Reserve Board in its letter to Senator Norbeck of March 29, 1932.

S. 4115 is referred to herein as the "old bill" and S. 4412 as the "new bill". Section numbers and page numbers refer to the sections and pages of the new bill, unless otherwise indicated. Certain sections of the old bill which have been omitted entirely from the new bill are treated at the end of this memorandum.

SECTION 1.

Title. - (p. 1)

This section merely provides that the short title of the act shall be the "Banking Act of 1932."

SECTION 2.

Definitions. - (pp. 1, 2 and 3)

The definitions contained in section 2, including those of an affiliate and of a holding company affiliate, are, in the new bill, made applicable not only to the provisions of this act but to any pro-

visions of law amended by this act.

The several classes of institutions defined as affiliates in the old bill are subdivided in the new bill so as to make a distinction between "affiliates" generally and "holding company affiliates".

With these exceptions, the definitions contained in the new bill are substantially in the same form as in the old bill with the changes recommended by the Board.

SECTION 3.

(a) Control of Federal reserve bank credit by Federal Reserve Board.(pp.3,4)

On this subject the recommendation of the Federal Reserve Board is adopted in Section 3 (a) of the new bill.

(b) Voting by groups or chains in elections of Federal reserve bank directors. (p. 5)

Section 4 of the old bill prohibited banks that belong to a group or chain from voting for Federal reserve bank directors, and the Board recommended the omission of the provision. The new bill provides (in Section 3(b) that when two or more member banks are affiliated with the same holding company affiliate only one of such banks may participate in the nomination or election of Federal reserve bank directors.

SECTION 4.

Distribution of earnings of Federal reserve banks. (p. 5)

The old bill provided (in Section 5) that net earnings of Federal reserve banks after payment of dividends and expenses should be paid to the Federal Liquidating Corporation. The Board recommended that no

changes be made in the present method of the distribution of earnings of Federal reserve banks but that the Secretary of the Treasury be authorized in his discretion to use the franchise tax received from Federal reserve banks for investment in obligations of the Liquidating Corporation. The new bill provides (in Section 4) that all net earnings of a Federal reserve bank, after payment of dividend claims and expenses, shall be paid into the surplus fund of the Federal reserve bank.

SECTION 5.

(a) Branches of State member banks. (pp. 5, 6)

In connection with Section 21 of the old bill, the Board recommended a new provision to the effect that nothing contained in the bill shall prevent State member banks from establishing branches either in the United States or elsewhere upon the same terms and conditions as those applicable to branches of national banks. This provision as recommended is contained in Section 5(a) of the new bill.

(The provisions of the new bill with reference to branches of national banks are contained in Section 19.)

(b) Reports of affiliates of State member banks. (pp. 6, 7)

The old bill (in section 6) required each affiliate of a State member bank to make three complete reports of condition annually through the president of the bank to the Federal Reserve Board. The Board's recommendation was that such reports be required only when deemed necessary by the Federal Reserve Board. The new bill provides in Section 5(b) that a State member bank shall obtain from each of its affiliates and furnish to the Federal reserve bank and to the Federal Reserve Board not less than

three reports of condition each year and such additional reports as the reserve bank or the Board may deem necessary. The provision requiring such reports to be made is mandatory; but they are required to contain only such information as, in the judgment of the Federal Reserve Board, shall be necessary to disclose fully the relations between such affiliate and such bank and to enable the Board to inform itself as to the effect of such relations upon the affairs of such bank.

(Substantially the same provisions are contained in Section 23 of the new bill with reference to reports of affiliates of national banks.)

Dealings in stocks and investment securities by State member banks. (p. 8)

Section 5(b) of the new bill contains a provision to the effect that State member banks shall be subject to the same limitations and conditions as are national banks with respect to the purchase, sale, underwriting and holding of investment securities and stock. There was no such provision in theold bill; and the Board recommended that Section 15 of the old bill, which restricted dealings in investment securities by national banks, be omitted entirely.

(The provisions on this subject regarding national banks are in Section 14 of the new bill.)

Divorce of stock of State member banks from stock of other corporations. (p. 8)

Section 5(b) of the new bill contains a provision to the effect that, after three years from the passage of the act, no certificate of stock of a State member bank shall represent the stock of any other corporation, except a member bank, nor shall the ownership or transfer of a stock cer-

tificate of such a bank be conditioned upon the ownership or transfer of a certificate of stock of another corporation, except a member bank.

A similar provision regarding stock of national banks is found in Section 16 of the new bill.

The old bill contained no such provision regarding the stock of State member banks; but Section 17 contained a similar provision regarding the stock of national banks, which would have become effective immediately, and the Board recommended that it be retained but that it be made effective after three years.

Right of an affiliate of a State member bank to vote stock held by it in such bank. (pp. 8 and 9)

Section 5(b) of the new bill provides that the holding company affiliates of State member banks shall be subject to the provisions of Section 5144 of the Revised Statutes (which contains the conditions under which affiliates may vote stock held in national banks) and also provides for the forfeiture of the membership of a State member bank, in the discretion of the Federal Reserve Board, where a voting permit of a holding company affiliate of such a bank is revoked. Under the new bill, therefore, substantially the same provisions are applicable to holding company affiliates of national banks and holding company affiliates of State member banks.

The Board recommended that the provisions of the old bill with reference to the conditions under which holding company affiliates of national banks might obtain permits to vote stock owned by them in such

banks be revised in a number of particulars and also recommended that substantially the same provisions as those suggested for national banks be made applicable to affiliates of State member banks, suggesting a new section of the bill for this purpose. The provisions applicable to affiliates of national banks in this connection are contained in Section 17 of the new bill and are discussed hereafter with reference to that section; but it may be stated briefly at this point that the recommendations of the Board regarding affiliates of national banks have not been adopted in the new bill.

Examination of affiliates of State member banks. (p. 9)

The new bill in Section 5(b) requires such examinations of affiliates of State member banks as shall be necessary to disclose fully the relations between such banks and their affiliates and the effect of such relations upon the affairs of the bank; the expense of such examinations may, in the discretion of the Federal Reserve Board, be assessed against the bank examined, (instead of against the affiliates as recommended by the Board); and, in the event of the refusal of the affiliate to give information requested or to permit such an examination, or in the event of the failure of the bank to pay the expenses of such an examination, the membership of any State member bank affiliated with such an affiliate may be forfeited in the discretion of the Federal Reserve Board.

The old bill contained a provision (in Section 28) requiring examinations of affiliates of a State member bank. The Federal Reserve Board recommended that such examinations be authorized to be made only when deemed necessary.

(Provisions of a somewhat similar character are contained in Section

24 of the new bill with reference to examinations of affiliates of national banks.)

SECTION 6.

Membership of the Federal Reserve Board. (pp. 10-12)

The old bill (in Section 7) contained a provision omitting the Secretary of the Treasury from the membership of the Federal Reserve Board and omitting the provision of the Federal Reserve Act authorizing the Secretary to assign quarters to the Federal Reserve Board. The Board recommended certain minor amendments to this section and suggested that authority be given the Board to purchase or erect a building for its offices. In Section 6 of the new bill the provisions of the old bill are repeated with the minor changes recommended by the Board; but the authority for the Federal Reserve Board to purchase or erect a building is omitted.

SECTION 7.

Open Market Committee. (pp. 13, 14)

Section 7 of the new bill adds a new Section 12A to the Federal Reserve Act, which provides for a Federal Open Market Committee along the lines of the existing Open Market Policy Conference.

The Board recommended that the similar provisions of the old bill (Section 10) on this subject be stricken out, and that there be substituted certain amendments to Section 14 of the Federal Reserve Act clarifying the Board's powers over open market operations and containing in revised form one of the provisions of the old bill. The Board's recommendations were not adopted in the new bill.

The chief differences between the new bill and the old bill are: In lieu of the statement in the old bill that no Federal reserve bank may engage in open market operations "except after approval and authorization

by the Committee", there is a provision in the new bill that no Federal reserve bank shall engage in such operations "except in accordance with resolutions adopted by the Committee and approved by the Federal Reserve Board". This applies to all purchases and sales on the open market under Section 14 of the Federal Reserve Act, whether for system account or for the account of an individual Federal reserve bank. The old bill provided that the Governor of the Federal Reserve Board should be a member of the committee in addition to the twelve members appointed by the directors of the Federal reserve banks, but in the new bill the Governor is not made a member of the committee. The new bill also omits the provision of the old bill that the Board's annual report to Congress should include a review of the decisions of the committee with an explanation thereof.

Federal Liquidating Corporation. (pp. 14-27).

Section 7 of the new bill also contains the proposed new Section 12B of the Federal Reserve Act providing for a Federal Liquidating Corporation to expedite the payment of dividends to depositors and creditors of closed member banks. The provisions of the new bill on this subject are a compromise between the provisions of the old bill and the Board's proposed substitute.

The old bill provided (in Section 10) for the creation of a Federal Liquidating Corporation for the purpose of purchasing and liquidating the assets of closed member banks. The Board recommended a number of changes in the provisions with reference to this proposed corporation, and in the new bill some of these changes have been adopted and some have been omitted. Without setting forth all of the detailed differences between the old bill, the recommendations of the Board, and the new bill,

there are stated below the more important of these differences.

In accordance with the recommendation of the Federal Reserve Board, the new bill provides for a board of directors of five members, (the Comptroller of the Currency, a member of the Federal Reserve Board, and three members selected annually by the Governors of the Federal reserve banks), instead of a board of fourteen members (the Comptroller of the Currency and the 13 members of the Federal Open Market Committee) as provided in the old bill.

The old bill provided for two classes of capital stock of the corporation: class A stock, to be subscribed by member banks in an amount equal to one-half of one per cent of their deposits, and class B stock, to be subscribed by Federal reserve banks in an amount equal to one-fourth of their surplus; with an additional provision for annual subscriptions by Federal reserve banks in amounts equal to one-fourth of the annual increase in their surplus accounts. The Board recommended that the capital stock consist of $100,000,000 to be subscribed by the United States. The new bill provides for the appropriation by the United States to the corporation of the sum of $125,000,000, but also provides for two classes of stock: class A stock, to be subscribed by member banks in an amount equal to one-fourth of one per cent of their deposits, and class B stock to be subscribed by Federal reserve banks in an amount equal to one-fourth of their surplus. One-half of each class of stock is apparently to be paid in upon the organization of the corporation, and the remainder is subject to call. The new bill, however, omits the provision for additional annual subscriptions by the Federal reserve banks.

The old bill authorized the Liquidating Corporation to purchase

and liquidate the assets of closed nonmember State banks and to make loans to such banks, for a limited number of years; and also authorized an appropriation of $200,000,000 from the United States Treasury for this purpose. In accordance with the recommendation of the Board, this provision is omitted from the new bill and its provisions are limited to member banks.

The old bill provided for the issuance of debentures by the Liquidating Corporation in amounts aggregating not more than four times its capital. The Federal Reserve Board recommended that debentures be authorized up to twice the amount of capital and that Federal reserve banks be given authority to purchase these debentures up to one-fourth of their surplus. The new bill authorizes the issuance of debentures in an amount aggregating not more than twice the amount of the capital of the corporation and the $125,000,000 appropriation from the Treasury of the United States. The provision recommended by the Board, however, that such debentures be guaranteed by the United States is omitted from the new bill.

The new bill (p. 20, lines 24, 25; p. 21, lines 1-4) contains in a different form the provision for a valuation committee, the elimination of which was recommended by the Board. Loans on and purchases of, assets of closed member banks are to be made "on the basis of" valuations of such assets made by this committee, which includes the receiver, a representative of the insolvent bank, and a third member selected by those two, but does not include any representative of the corporation.

A number of provisions recommended by the Federal Reserve Board of a prohibitive or penal character in connection with the proposed Federal Liquidating Corporation and its operations have been adopted in the new bill and certain unnecessary steps regarding the organization of the corporation and increases and decreases in its capital have been eliminated.

SECTION 8.

Loans on member banks' collateral notes (pp. 27-28)

The old bill (Section 11) provided that the rate at which a Federal Reserve Bank might make advances to its member banks on their 15-day promissory notes should be at a rate 1% higher than the rediscount rate, and also provided that if a member bank, while indebted to a Federal reserve bank on such a 15-day note and despite a warning of the Federal reserve bank or the Federal Reserve Board, should increase its loans made for the purpose of purchasing or carrying investment securities (except obligations of the United States), the note should be immediately due and payable and the member bank should be ineligible to borrow on such 15-day notes for such periods as the Federal Reserve Board might determine. The old bill also provided that the Federal Reserve Board might suspend the provisions of law with reference to loans to member banks on their 15-day notes for periods of 90 days.

In light of these provisions of the old bill, the Federal Reserve Board recommended an amendment increasing the maximum maturity of advances to member banks on their promissory notes secured by eligible paper from 15 to 90 days.

Section 8 of the new bill (pp. 27,28) does not adopt the recommendation of the Board on this point and contains substantially the same provisions as those in the old bill, except that there have been omitted the discriminatory rate of 1% on such 15-day advances to member banks and the provisions for the suspension by the Board of the provisions of law on this subject.

SECTION 9.

Foreign transactions of Federal reserve banks (p. 29)

The Federal Reserve Board suggested certain changes in the provisions of Section 12 of the old bill with reference to the supervision of the Board over foreign transactions of Federal reserve banks, and the more important of these changes have been adopted in the corresponding provisions contained in Section 9 of the new bill. The provisions of the new bill on this subject, which are substantially those of the old bill with the Board's suggested changes, provide that all relationships and transactions by Federal reserve banks with foreign bankers shall be subject to special supervision and regulation by the Federal Reserve Board; that negotiations with foreign bankers shall not be conducted without the permission of the Board; that the Board may be represented in any such negotiations; and that a full report of all such negotiations shall be made to the Board in writing.

SECTION 10.

Reserves of member banks and restrictions on dealings in "Federal Funds" (p. 30).

Section 13 of the old bill contained a complete revision of Section 19 of the Federal Reserve Act with reference to the reserves required of member banks. Chief among its provisions was the requirement that the percentages of reserve against time deposits be increased over a period of years to the same percentages as those required against demand deposits. Another important provision of the old bill prohibited the transfer of balances with a Federal reserve bank from one bank to

another without the authority of the Federal Reserve Board and except upon payment of a fee for the privilege. The Board was also authorized to suspend all dealings in reserve balances for such periods as it might deem best.

The Federal Reserve Board recommended, in lieu of the provisions of the old bill on this subject, a revision of section 19 of the Federal Reserve Act in accordance with the recommendations of the System Committee on Reserves with some modifications; and recommended the omission of the limitations on the use of balances standing to the credit of member banks on the books of the Federal Reserve Banks.

The new bill (in Section 10) omits entirely any revision or amendment of the reserve requirements of member banks, and also omits the restrictions of the old bill on the transfer of balances in Federal reserve banks.

Member banks as mediums in making loans on collateral. (p. 30)

In accordance with a recommendation of the Federal Reserve Board, Section 10 of the new bill adds a new paragraph to Section 19 of the Federal Reserve Act forbidding a member bank to act as the medium or agent of any non-banking corporation or individual in making loans on the security of stocks, bonds and other investment securities to brokers or dealers in such securities, and providing a fine for violation thereof.

The old bill contained a provision for a similar purpose but in different form.

SECTION 11.

Loans to or investments in stock of affiliates. (pp. 30-32)

On this subject the new bill (in Section 11) adopts substantially the recommendations of the Federal Reserve Board and provides that no member banks shall make any loan or extension of credit to, or purchase

securities under repurchase agreements from, any of its affiliates, or invest in the stock or obligations of such affiliates, or accept such stock or obligations as security for advances, if the aggregate amount thereof, in the case of any one affiliate, will exceed ten per cent of the capital stock and surplus of the member bank, or if, in the case of all such affiliates, the aggregate amount thereof will exceed twenty per cent of the capital stock and surplus of such member bank. Each loan or extension of credit to an affiliate shall be secured by collateral, in the form of stocks, bonds, debentures or other such obligations, having a market value of at least twenty per cent more than the amount of the loan or extension of credit or at least ten per cent more than the amount thereof if secured by State or municipal obligations. Loans or extensions of credit secured by obligations of the United States, Federal intermediate credit banks, Federal land banks or paper eligible for rediscount by Federal reserve banks are excepted from the requirement as to marginal collateral (but the suggestions of the Federal Reserve Board that those secured by obligations of the Reconstruction Finance Corporation be also excepted was not adopted). The provisions of this section do not apply to an affiliate engaged solely in holding the bank premises of the affiliated member bank or conducting a safe-deposit business or the business of an agricultural credit corporation or live stock loan company, or to an affiliate in the capital stock of which a national bank is authorized to invest under Section 25 of the Federal Reserve Act, or an affiliate organized under Section 25(a) of the Federal Reserve Act.

The old bill (in Section 9) contained some of the provisions of the new bill on this subject, but the limitations prescribed were applicable only as to affiliates engaged in buying and selling stocks, bonds, real estate or real estate mortgages or organized to hold title to any such property. The old bill did not include the twenty percent limit in the case of all affiliates, on the aggregate of loans, investments and advances, nor did it include any of the above-mentioned exceptions to the limitations prescribed. The old bill required marginal collateral of twenty per cent in all cases except where the security for the loan consisted of paper eligible for rediscount or obligations eligible for investment by savings banks.

SECTION 12.

Real estate loans and investments in bank premises (pp. 32, 33)

The old bill (in Section 14) contained a number of provisions with reference to real estate loans and investments of member banks. It would have required a bank to revise the valuations on which such loans were based at the time of each examination and also, in effect, at the time of each report of its condition. The limitations on the amount of such loans would have been changed, and all unsecured loans whose eventual safety depends upon the value of real estate would have been classified as real estate loans. Time depositors would have been given a preferred claim on all real estate loans and other assets acquired under this section of the old bill.

The Federal Reserve Board recommended that these provisions of the old bill be omitted and that there be substituted therefor a provision that no national bank, without the permission of the Comptroller of the Currency, and no State member bank, without the permission of the Board, shall invest in bank premises, or in the stock or obligations of, or in loans to, any corporation owning or holding its bank premises a sum exceeding the amount of the capital stock of such bank.

The new bill omits the provisions of the old bill in accordance with the recommendation of the Board, and adopts in substance the provision suggested by the Board, although the language of the provision is somewhat changed, and loans upon the security of the stock of any such corporation holding bank premises are included within the investments to which the limitation applies.

SECTION 13.

Jurisdiction of Federal Courts over cases involving foreign banking transactions. (pp. 33,34)

This provision, which was not contained in the old bill and which was not the subject of a recommendation by the Federal Reserve Board, confers upon the district courts of the United States jurisdiction over any case to which a corporation organized under the laws of the United States is a party and which arises out of transactions involving international or foreign banking, either directly or through the agency, ownership or control of branches or of local institutions in foreign countries.

It is understood that the rule in the Federal courts with reference to the valuation of foreign currency in transactions of this kind is more favorable to banks than in the State courts, and it is apparently for this reason that the bill contains the above provision.

SECTION 14.

National banks granted all powers of State banks. (p. 34)

In the old bill (Section 15) national banks were granted power to engage in all forms of banking business permitted by the laws of the State in which they are located to "banks of deposit and discount" organized under such State laws, except to the extent that the exercise of such powers is forbidden by the laws of the United States.

The Board recommended that this provision be omitted; but it is contained in the new bill in substantially the same form in which it appeared in the old bill.

Dealings in investment securities (pp. 34-36)

The old bill (in section 15) contained a number of provisions with reference to dealings in investment securities by national banks and the Board recommended that all these provisions be omitted. They are, however, repeated in the new bill, with certain changes and additions, and with the provision (in Section 4) that the same provisions shall be applicable to State member banks. The new bill provides in effect that:

Dealings in investment securities are limited to the purchase and sale of such securities, without recourse, solely upon the order

and for the account of customers, except that member banks may purchase and hold for their own account investment securities under limitations and restrictions prescribed by regulation of the Comptroller of the Currency.

No member bank shall underwrite any issue of securities.

The total amount of any one issue of investment securities of any one obligor hereafter purchased and held by a member bank for its own account shall not exceed 10 per cent of the total amount of such issue outstanding, but this limitation does not apply to any issue not in excess of $100,000 and not in excess of 50 per cent of the capital of the bank; and the total amount of investment securities of any one obligor hereafter purchased and held shall not exceed 15% of the capital of the bank and 25 per cent of its surplus. (The latter limitation in the old bill was stated in ambiguous terms and might have been construed to apply to the aggregate amount of all investment securities held by the bank.)

No member bank may purchase or hold the stock of any corporation, except as otherwise permitted by law, and except that a bank may invest not more than 15 per cent of its capital and surplus in the stock of safe deposit companies.

These limitations do not apply to obligations of the United States, to general obligations of any State or any subdivision thereof, or to obligations issued under the authority of the Federal Farm Loan Act.

The definition of investment securities contained in existing law would apparently have been stricken out by the old bill and the Comptroller of the Currency given unlimited powers to prescribe his own definition, except that stocks could not be included. The new bill, however, in effect restores the definition contained in the existing law.

SECTION 15

(a) Capital required for organization of national banks. (pp. 36, 37)

The old bill (in section 16) contained an amendment to Section 5138 of the Revised Statutes to provide that no national bank may be organized with a capital of less than $50,000, except that a national bank may be formed, in the discretion of the Comptroller of the Currency, for the purpose of succeeding to the business of an existing bank with a capital of not less than $25,000. The old bill also eliminated the existing requirement that the organization of national banks with a capital of less than $100,000 shall be subject to the approval of the Secretary of the Treasury.

The Board recommended the elimination of the exception in the old bill which permitted the formation of national banks with a capital of less than $50,000 to take over the business of an existing bank. This recommendation was adopted and with this change the provisions of the old bill on this subject are repeated in the new bill.

(b) Capital requirements of State member banks. (p. 37)

Section 15(b) of the new bill contains a provision, not appearing in the old bill and not recommended by the Federal Reserve Board, which amends Section 9 of the Federal Reserve Act so as to eliminate the provision of existing law under which a State bank is permitted to become a member of the Federal Reserve System with a capital equal to only 60% of the amount required for the organization of a national bank in the place in which it is situated. The capital required of State member banks hereafter admitted to the System, therefore, would be required in all cases to be equal to that required of national banks located in places of like size.

SECTION 16.

Shares of stock of $100 each.

The old bill (in Section 17) would have amended section 5139 of the Revised Statutes so as to provide that the capital stock of national banks should be divided into shares of $100 each, thus repealing the provision of the present law for shares of a lesser amount. In accordance with the recommendation of the Federal Reserve Board, however, this provision is omitted in the new bill.

Divorce of stock of national bank from stock of other corporations. (p. 37)

The new bill provides (in Section 16) that, after three years from the date of its passage, no certificate of stock of a national

bank shall represent the stock of any other corporation except a member bank, nor shall the ownership or transfer of a stock certificate of a national bank be conditioned upon the ownership or transfer of a certificate of stock of another corporation except a member bank.

Substantially the same provision was included in the old bill (in Section 17), except that the prohibition apparently was to take effect immediately and no exception was made as to the stock of another member bank. The Board recommended that this provision be made effective three years after enactment and, as stated, the new bill includes this change.

Similar provisions regarding certificates of stock of State member banks are included in section 5(b) of the new bill.

SECTION 17.

Shares of its own stock held by a national bank as trustee. (p. 38)

The old bill (in Section 19) provided that no shareholders of national banks who shall become such through nominal transfer or ownership on behalf of another shall vote at meetings of shareholders of such banks. The Board recommended that shares of its own stock held by any national bank as trustee shall not be voted. The Board's recommendation was adopted in the new bill, and the provision of the old bill was not retained.

Right of an affiliate of a national bank to vote stock held by it in such bank. (pp. 38-43)

The old bill (in Sections 19 and 20) contained provisions requiring an affiliate of a national bank to obtain a voting permit from the Federal Reserve Board before voting any stock held by it in such national bank. Such a voting permit might be issued only upon compliance by the holding company affiliate with a number of detailed provisions. The Federal Reserve Board recommended a number of changes in these provisions of the old bill, but the Board's recommendations on this subject have not been adopted in the new bill.

The salient features of the Board's recommendations on this subject were as follows: Shares owned or controlled by an affiliate shall not be voted unless such affiliate has filed an agreement with the Comptroller of the Currency to comply with the provisions of this section. Within one year from the date of any such agreement each nonmember State bank owned or controlled by such affiliate shall apply for membership in the Federal Reserve System and if not admitted such affiliate shall divest itself of all interest in such bank. Each such affiliate shall hold readily marketable assets, other than bank stocks, equal to 15 per cent of bank stocks held by it and shall reinvest its net earnings above 6 per cent in such assets until they amount to 25 per cent of bank shares held by it; with a proviso that credit shall be given for contributions made during the preceding three years to banks owned or controlled by the affiliate. Failure to comply with the agreement is ground for termination thereof by the Comptroller. No national bank shall make any loan to, or on

the security of the stock of, or be the purchaser of the stock of, any affiliate which owns or controls such bank, unless necessary to prevent loss upon a debt previously contracted in good faith, and stock so acquired shall be disposed of within two years. Officers and employees of affiliates which have entered into an agreement with the Comptroller of the Currency, are made subject to certain criminal provisions, and a penalty is provided for voting the stock held by affiliates, unless such an agreement is in effect.

The provisions of the new bill on this subject, which follow along the lines of the old bill with certain changes and additions and which do not contain the provisions as recommended by the Board, are in brief form set forth in the following paragraphs. (As hereinbefore explained under Section 5, the provisions of the new bill on this subject are applicable also to holding company affiliates of State member banks.)

Shares of a national bank controlled by a holding company affiliate, including those held by a trustee for the benefit of the shareholders of such affiliate, shall not be voted unless such affiliate shall have obtained a voting permit from the Federal Reserve Board; and in acting upon an application for such permit, the Board shall consider the financial condition of the applicant, the general character of its management and the probable effect of the granting of the permit upon the affairs of such bank. No permit shall be granted except upon the following conditions:

(a) Each such holding company affiliate shall agree: to submit to examinations, at its own expense, disclosing fully the relationship

between such affiliate and such bank, that such examinations may be made of each bank owned or controlled by the affiliate, and that publication of statements of condition of such banks may be required.

(b) After January 1, 1935, every such holding company affiliate shall possess unpledged readily marketable assets other than bank stock in an amount not less than 12% of the par value of all bank stocks controlled by such affiliate, which amount shall be increased by not less than 2% annually up to 25% thereof and by reinvesting in such readily marketable assets net earnings in excess of 6% annually until the 25% requirement is reached. (The last of the requirements of this paragraph was recommended by the Board.)

(c) However, where the shareholders of the affiliate are themselves liable under the double liability provisions on the bank stock held by the affiliate, the latter shall be required only to establish, out of its net earnings in excess of 6%, a reserve of readily marketable assets equal to 12% of the par value of bank stocks controlled by it, and readily marketable assets required of such affiliate may be used for replacement of capital in banks affiliated with it; but any deficiency so incurred shall be made up within such period as the Federal Reserve Board may prescribe.

(d) That officers, directors, agents and employees of such a holding company affiliate shall be subject to the same penalties for false entries as officers and employees of member banks are subject to under Section 5209 of the Revised Statutes.

(e) That every such holding company affiliate shall show that it does not have any interest in and is not participating in the management of any securities company; that, if it has such an interest or participation it will, within three years, divest itself thereof; and that it will declare dividends only out of actual net earnings.

If any holding company affiliate violates any of the provisions of this act, the Federal Reserve Board may revoke its voting permit after notice, and thereafter no national bank whose stock is controlled by such affiliate shall receive Government deposits or pay any dividend to such affiliate.

Where such a voting permit of an affiliate has been revoked, the franchise of any national bank controlled by such an affiliate shall be subject to forfeiture.

SECTION 18.

Relationships between Member Banks and Securities Dealers or Corporations making collateral loans. (pp. 43, 44.)

The old bill (in section 18) provided that, after January 1, 1933, no director, officer or employee of a member bank should be an officer or employee of a corporation or association engaged primarily in the securities business and no such officer, director or employee of a member bank should be a director, officer or employee of a corporation making loans secured by collateral to any one except its own subsidiaries. The old bill also provided that no member bank should have correspondent relationships with associations or corporations of the kind mentioned.

The Board recommended that these provisions be omitted and suggested substitute provisions.

The new bill provides, in substantial accordance with the substitute provisions recommended by the Board, that, after three years, no member bank shall be affiliated with a securities corporation in the manner described in Section 2(b) of the bill (where the word "affiliate" is defined so as not to include holding company affiliates). Violations of this provision subjects the member bank to a penalty of $1,000 a day, in the discretion of the Federal Reserve Board, and, if the violations continue for six months after warning from the Board, the bank's franchise may be forfeited, if a national bank, or its membership in the Federal Reserve System may be forfeited, if a State bank.

SECTION 19.

Branches of National banks. (pp. 44,45).

The old bill (in Section 21) provided for State-wide branches of national banks in States where the State law permits State banks to have branches, with a proviso that, if the usual business of the bank extends into an adjacent State, the Federal Reserve Board may permit the establishment of a branch by the bank in such State not more than fifty miles from its head office. In order to have branches outside of the city of its head office, a capital of $500,000 was required. Furthermore, the aggregate capital of a bank and its branches was required to equal the capital required for an equal number of national banks situated where the bank and its branches are respectively located.

The Federal Reserve Board suggested that, if these provisions were to be retained, a change be made which would eliminate the limitations of the present law on the number of branches which may be established in cities of less than 100,000 inhabitants, and the limitation providing that no branch may be established in a city of less than 25,000 inhabitants. This recommendation of the Board was adopted in the new bill.

The provisions of the new bill on this subject are substantially the same as those contained in the old bill, with the change recommended by the Board; except that the establishment of State-wide branches is not limited to those States in which the State law permits State banks to have branches.

(The provisions of the new bill with reference to branches of State member banks are contained in Section 5(a).)

SECTION 20.

Consolidations of national banks with other banks in the same State.(p. 45)

The provisions of the Act providing for the consolidation of two or more national banks or for the consolidation of State banks with national banks would be amended by the new bill so as to permit such consolidations to take place between banks located anywhere in the same State. This section was contained in the same form in the old bill (in Section 22). No suggestion was made by the Board on this point.

SECTION 21.

Rate of interest on loans. (pp. 45,46)

The new bill would amend Section 5197 of the Revised Statutes so that national banks could charge on loans and discounts, (1) the rate of interest allowed by the State law (or 7% where the State law fixes no limit), or (2) a rate 1% in excess of the Federal reserve bank discount rate, which ever may be the greater.

The provision of the new bill on this subject is the same as that contained in the old bill (Section 23) with a minor change suggested by the Board.

SECTION 22.

Limitations on loans to affiliated corporations. (pp.46,47)

The new bill provides an amendment to the first paragraph of Section 5200 of the Revised Statutes, which provides that in computing the amount which a corporation can borrow from a national bank, the corporation and all of its subsidiaries in which such corporation owns or controls a majority interest would be treated as a single borrower.

This provision has been adopted from the old bill (Section 25(a)) with a clarifying amendment suggested by the Board.

In accordance with the Board's recommendations, the following provisions of section 25 of the old bill are omitted from the new bill:
(1) That the amount which any national bank might lend to any broker or member of any stock exchange or similar corporation or any finance company, securities company, investment trust or other similar organization would be limited to 10% of the capital and surplus of such national bank.
(2) that no national bank would be permitted to lend to "an affiliate" an amount exceeding 10% of the capital and surplus of such

national bank or exceeding the capital stock of such affiliate, whichever may be the smaller.

(3) that the aggregate amount which all affiliates of a national bank could borrow from such national bank (including repurchase agreements) would be limited to 10% of the national bank's capital and surplus except that loans secured by Government bonds or by bonds issued by the State in which such bank is situated or by any political subdivision of such State would be excluded altogether from the limitations of Section 5200 of the Revised Statutes, if actually owned by the borrower.

(4) that no national bank might establish or capitalize an affiliate through cash or stock dividend declarations made from its surplus or from undivided profits; and "within three years after this section as amended takes effect", every affiliate should be capitalized through the sale of its own stock which should be paid for in cash in the same manner as required in the case of a national bank.

(5) that for a period of three years, no affiliate of a national bank might hold, or lend upon, more than 10% of the shares of the capital stock of the parent institution.

SECTION 23.

Reports of affiliates of national banks (pp. 47, 48).

The old bill (in Section 27) required each affiliate of a national bank to make three complete reports of condition annually through the president of the bank to the Comptroller of the Currency, and also to make such special reports as the Comptroller might require. The Board's recommendation was that such reports be required only when deemed necessary.

The new bill provides that every national bank shall obtain from each of its affiliates, other than member banks, and furnish to the Comptroller of the Currency not less than three reports of condition each year and such additional reports as the Comptroller may deem necessary. The provision requiring such reports is still mandatory; but they are required to contain only such information as in the judgment of the Comptroller shall be necessary to disclose fully the relations between such affiliate and such bank and to enable the Comptroller to inform himself as to the effect of such relations upon the affairs of such bank. The bank is subject to a penalty for failure to render such reports.

Provisions of the old bill requiring an affiliate under certain stated conditions to publish its entire portfolio are omitted from the new bill.

(Substantially the same provisions are contained in Section 5(b) of the new bill with reference to reports of affiliates of State member banks).

SECTION 24.

Examinations of affiliates of national banks. (pp. 48-50)

The new bill requires such examinations of affiliates (other than member banks) of a national bank as shall be necessary to disclose fully the relations between such bank and such affiliates and the effect of such relations upon the affairs of such bank, and authorizes the forfeiture of the franchise of the bank in the event of refusal of the affiliate to give information or to permit such examination. Publication of the examination report of a national bank or of an affiliate is authorized if the bank or affiliate fails to comply with recommendations of the Comptroller of the Currency based on such examinations.

The old bill contained a provision (in Section 28) requiring examinations of affiliates of national banks and member banks. The Federal Reserve Board recommended that this section provide for examination of affiliates of national banks only (as examinations of affiliates of State member banks are provided for elsewhere in the bill) and that such examinations be authorized to be made only when deemed necessary.

In accordance with certain other suggestions of the Federal Reserve Board on this subject, the new bill has added certain provisions to authorize examiners making an examination of an affiliate of a national bank to administer oaths and to examine officers and employees under oath; to provide that the expenses of such examination may be assessed against the affiliate and, if not paid by the affiliate, then against

the bank; and to provide a penalty of $100 per day to be paid by the bank for refusal of the affiliate to give information required or to permit such an examination.

While examinations of affiliates of national banks in the old bill were limited to a period of three years after its passage, the new bill, in accordance with the Board's suggestion on this point, contains no limit of this kind.

(Provisions of a somewhat similar character with reference to examinations of affiliates of State member banks are contained in Section 5(b) of the new bill.)

SECTION 25.

Removal of bank directors or officers from office.(pp.50-52)

On this subject, the new bill follows substantially the recommendation of the Board and provides a procedure for the removal of a director or officer of a member bank who has continued to violate the law or has continued unsafe or unsound practices in conducting the business of the bank with which he is connected, after being warned by the Comptroller of the Currency (as to a national bank) or the Federal Reserve Agent of his district (as to a State member bank) to discontinue such violations or such practices. After a hearing by the Federal Reserve Board establishing such facts, the Board may order the removal of such director or officer and a copy of such order shall be served upon him and upon the bank with which he is connected. Such order and findings of fact may not be made public or disclosed except

to such director or officer and the directors of his bank, "otherwise than in connection with proceedings for a violation of this section." Participation by such officer or director in the management of such bank after having been removed is punishable by fine or imprisonment.

The old bill placed the power of removal in a committee consisting of the Governor of the Federal Reserve Board, the Comptroller of the Currency and the Federal Reserve Agent, instead of in the Federal Reserve Board as provided in the new bill. The old bill did not contain the provision prohibiting the making public or disclosing the order of removal or findings of fact.

SECTION 26.

Saving clause and reservation of right to amend. (p. 52).

Section 26 contains the usual provisions (which were also in the old bill) reserving the right to alter, amend or repeal the act and limiting decisions holding parts of the act to be invalid, to the specific sections dealt with in such decisions.

SECTIONS OF OLD BILL ENTIRELY OMITTED FROM NEW BILL.

In addition to a number of other provisions of the old bill which have been omitted from the new bill but which have been treated above in connection with certain related topics contained in the corresponding sections of the new bill, (such as the provisions regarding reserves and regarding real estate loans and investments of member banks), there have also been omitted from the new bill the following provisions, each of which constituted an entire separate section of the old bill.

Limitation upon amount of loans on collateral security by member banks.

Section 8 of the old bill authorized the Federal Reserve Board to fix the percentage of the capital and surplus of a member bank which might be represented by loans on collateral security. The purpose of this section apparently was to prevent the undue use of bank loans for speculation in securities, which is fully covered in Section 3. In accordance with the recommendation of the Board, therefore, the provisions of Section 8 of the old bill have been omitted from the new bill.

Interest on deposits.

Section 24 of the old bill would have limited the rate of interest which national and State member banks would be permitted to pay on deposits as follows: (1) interest on balances due to banks would have been limited to 2 1/2% or "the current rate of discount of the Federal reserve bank", whichever is the smaller; (2) on all other deposit balances, the rate would have been limited to one-half the rate of interest which national banks are permitted to charge on loans.

In accordance with a recommendation of the Federal Reserve Board this section is omitted from the new bill.

Limitations on collateral loans to single borrowers.

Section 26 of the old bill provided that no member bank shall lend to any individual or corporation "upon collateral security" an amount exceeding 10% of its own capital and surplus, or an amount exceeding the percentage fixed by the Federal Reserve Board, whichever is the smaller.

In accordance with the recommendation of the Federal Reserve Board this section is omitted from the new bill (as was also Section 8 of the old bill which also provided for limiting collateral loans.)