

X-7859

## INTERPRETATION OF BANKING ACT OF 1933

(Copies to be sent to all Federal Reserve Banks)

April 13, 1934

\_\_\_\_\_,  
\_\_\_\_\_,  
\_\_\_\_\_.

Dear Sir:

Receipt is acknowledged of your letter of January 25, 1934, with inclosure, in regard to the question whether the \_\_\_\_\_ National Company of \_\_\_\_\_, \_\_\_\_\_, an affiliate of \_\_\_\_\_ National Bank of \_\_\_\_\_, is a "securities company" within the purview of Section 20 of the Banking Act of 1933, which provides in part that after one year from June 16, 1933, no member bank shall be affiliated in any manner described in Section 2(b) thereof with any " \* \* \* corporation \* \* \* engaged principally in the issue, flotation, underwriting, public sale, or distribution \* \* \* of stocks, bonds, debentures, notes, or other securities". In the opinion of counsel for the bank inclosed with your letter, there was raised the additional issue whether the company could be considered as being engaged primarily in the business of "purchasing, selling or negotiating securities" within the meaning of Section 32 of the Act, which provides in part that from and after January 1, 1934, no officer or director of any member bank shall be an officer, director or manager of any " \* \* \* corporation \* \* \* engaged primarily in the business of purchasing, selling or negotiating

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securities \* \* \* ".

From the information submitted it appears that the activities of the \_\_\_\_\_ National Company consist principally in its making loans secured by mortgages or deeds of trust on real estate, and in its acting as trustee under deeds of trust on large tracts of land or oil properties. It is understood that the agreements under which the company acts as trustee secure the payment of obligations in the form of notes or bonds, but that such obligations are negotiated before the instruments securing the obligations are executed, and that the company does not participate in the "issue, flotation, underwriting, public sale, or distribution" of such obligations. Apparently the company merely agrees to make collections of the loans and to distribute the moneys collected to the holders of the various obligations secured by the deeds of trust.

One of the principal purposes of the Banking Act of 1933 was to effect a separation of commercial and investment banking, and it appears that Sections 20 and 32 of that Act were designed to aid in the accomplishment of this purpose. Although there may be mortgage notes of a kind which should be classified as "notes or other securities" for the purposes of Section 20, the Federal Reserve Board is of the opinion that mortgage notes arising out of the ordinary type of direct loans on real estate are not "notes or other securities" within the intendment of Section 20, and that neither such notes nor the mortgages securing the same should be classified as "stocks, bonds, debentures, notes or other securities" in determining whether

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an organization engaged in dealing in such obligations comes within the scope of said Section 20. Accordingly, the Board is of the opinion, on the basis of the facts submitted, that the \_\_\_\_\_ National Company cannot be considered as engaged principally in the "issue, flotation, underwriting, public sale or distribution \* \* \* of stocks, bonds, debentures, notes or other securities" within the meaning of Section 20.

Similarly, the Board is of the opinion that neither mortgages nor ordinary mortgage notes are "securities" within the intentment of Section 32 and that such obligations should not be classified as securities for the purposes of that section. On the basis of the facts submitted, therefore, the Board concurs in the opinion of your counsel that the \_\_\_\_\_ National Company does not come within the purview either of Section 20 or of Section 32 of the Banking Act of 1933.

The views expressed above should not be construed as an expression of opinion by the Board that mortgage notes and mortgages should not be considered "stocks, bonds, debentures, notes, or other securities" within the meaning of Section 21(a) of the Banking Act of 1933. Said Section 21 provides a penalty of fine or imprisonment for violation of its provisions and the interpretation of the provisions of that section is a matter entirely within the jurisdiction of the Department of Justice. Since an expression of opinion by the Federal Reserve Board as to what would constitute a violation

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of that section would not afford protection from criminal prosecution if the Department of Justice, upon consideration of the matter, should take a contrary position and determine to prosecute for a violation thereof, the Federal Reserve Board does not feel that it would be appropriate to undertake to express an opinion on the question whether mortgage notes or mortgages should be considered "stocks, bonds, debentures, notes, or other securities" within the meaning of that section.

Very truly yours,

(Signed) Chester Morrill  
Chester Morrill,  
Secretary.