

INTERPRETATION

X-9322

BANKING ACT OF 1935

(Copies to be sent to all Federal Reserve Banks)

September 11, 1935

Mr. J. H. Case,  
Federal Reserve Agent,  
Federal Reserve Bank of New York,  
New York, New York.

Dear Mr. Case:

Reference is made to your letter dated November 23, 1934 and inclosures contained therein, requesting an expression of the Board's views as to whether "A" Trust Company, \_\_\_\_\_, New York, may lawfully continue to hold certain \_\_\_\_\_ Corporation notes either as "investment securities", under the provisions of paragraph Seventh of section 5136 of the Revised Statutes and section 9 of the Federal Reserve Act, or in the bank's loan account. As you have already been advised, the Board communicated with the Comptroller of the Currency with regard to the question whether these notes are to be regarded as investment securities and, after his views were received, a further reply to your letter was delayed pending the enactment of the Banking Act of 1935 which contains provisions affecting this question.

From the information submitted in your letter, it appears that on or about November 5, 1934, "A" Trust Company, a State member bank, purchased \_\_\_\_\_ Corporation  $2\frac{1}{2}$  per cent Serial Notes in the amount of \$900,000, such notes being a part of a \$9,000,000 issue, one-third of which matures annually on November 1, 1935, 1936, and 1937. It also appears that the notes purchased by "A" Trust Company consist of \$300,000 of each of the three maturities. It is understood that all the

notes were originally issued in denominations of \$100,000 and \$50,000 but are interchangeable for notes of smaller denominations. You state that "A" Trust Company paid for the notes by check payable to \_\_\_\_\_ Corporation.

It is also understood that "A" Trust Company and the other 18 purchasers of the issue stated that they purchased the notes for their own account for the purpose of investment and not for distribution and that, since the securities were offered to not in excess of 25 purchasers, the securities were not registered under the Securities Act of 1933. It appears that the notes are not actively dealt in on any market although other securities of \_\_\_\_\_ Corporation are actively traded in and are widely held.

An examination of the form of the definitive notes and of the printed trust agreement discloses that the notes are in the usual form of a corporate note or bond and are issued pursuant to the terms of a trust agreement under which \_\_\_\_\_ Corporation obligates itself to the trustee, "B" Trust Company, to pay the interest on and the principal of the notes. The notes may be registered as to principal or payable to bearer, and the notes carry interest coupons payable to bearer. Although the notes are unsecured, the trust agreement contains covenants limiting the right of \_\_\_\_\_ Corporation and its subsidiary companies to make mortgages, pledges or other incumbrances while the notes remain unpaid.

The first question presented by your letter is whether the notes in question are "investment securities" as defined in paragraph

Seventh of section 5136 of the Revised Statutes and the regulations of the Comptroller of the Currency issued pursuant thereto on February 25, 1927 and December 27, 1934. In response to the Board's inquiry to the Comptroller he stated that, in his opinion, the notes were not "investment securities" within the meaning of his regulation on the subject because of the fact that they do not have such public distribution as to insure the marketability of the issue. The Board agrees with the opinion of the Comptroller of the Currency upon this point and, accordingly, it will be appreciated if you will advise "A" Trust Company that the notes may not lawfully be held as "investment securities" under the provisions of paragraph Seventh of section 5136 of the Revised Statutes and section 9 of the Federal Reserve Act.

You also request an expression of the Board's views as to whether the notes may be held by "A" Trust Company in its loan account as evidence of a loan by the bank to \_\_\_\_\_ Corporation. The notes in question appear to constitute securities, but as above stated are not "investment securities" within the meaning of that term as used in section 5136 of the Revised Statutes. Under the provisions of that section as amended by section 308 of the Banking Act of 1935, it is clear that a national bank may not purchase for its own account notes such as those under consideration which are securities but not "investment securities", and the provisions of section 9 on this subject are clearly intended to place State member banks on a basis of equality with national banks with respect to investments in securities. Accordingly, it is the view of the Board that a State member bank may not, since the

enactment of the Banking Act of 1935, purchase for its own account notes of the type here under consideration.

In view of the amendment to the law the Board believes that it is unnecessary for it to determine the question presented in your letter under the provisions of the law as it existed prior to the enactment of the Banking Act of 1935, and the Board will raise no objection to the continued holding by "A" Trust Company of the notes in question which were purchased prior to the enactment of that Act.

It will be appreciated if you will advise "A" Trust Company of the Board's views in this matter.

Very truly yours,

(Signed) Chester Morrill

Chester Morrill,  
Secretary.