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LEGISLATION TO PROHIBIT BANKS FROM PER-
FORMING CERTAIN NONBANKING SERVICES
AND FROM ENGAGING IN THE BUSINESS OF
PERSONAL PROPERTY LEASING

GOVERNMENT
Storage

HEARINGS
BEFORE THE
SUBCOMMITTEE ON BANK SUPERVISION
AND INSURANCE
OF THE
COMMITTEE ON BANKING AND CURRENCY
HOUSE OF REPRESENTATIVES
EIGHTY-EIGHTH CONGRESS

SECOND SESSION

ON

H.R. 9548

A BILL TO PROHIBIT BANKS FROM PERFORMING CERTAIN
NONBANKING SERVICES, AND FOR OTHER PURPOSES

AND

H.R. 9822

A BILL TO PROHIBIT BANKS FROM ENGAGING IN THE
BUSINESS OF PERSONAL PROPERTY LEASING

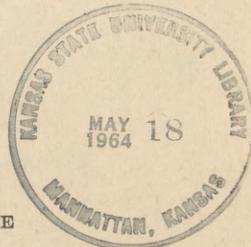
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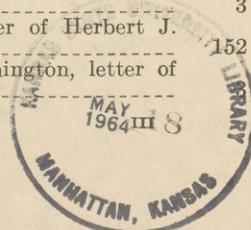
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LEGISLATION TO PROHIBIT BANKS FROM PERFORMING CERTAIN NONBANKING SERVICES AND FROM ENGAGING IN THE BUSINESS OF PERSONAL PROPERTY LEASING

TUESDAY, FEBRUARY 25, 1964

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON BANK SUPERVISION AND INSURANCE
OF THE COMMITTEE ON BANKING AND CURRENCY,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10 a.m., in the caucus room, Cannon House Office Building, Hon. Abraham J. Multer (chairman of the subcommittee) presiding.

Present: Representatives Multer, Moorhead, Minish, Grabowski, Halpern, Bolton, Lloyd, and Talcott.

Mr. MULTER. Good morning, gentlemen. The subcommittee will please come to order.

We have met this morning to take testimony on H.R. 9548, a bill to prohibit banks from performing certain nonbanking services, and H.R. 9822, a bill to prohibit banks from engaging in the business of personal property leasing. These bills were introduced and these hearings are being conducted in response to complaints that we have received from across the country against activities of banking institutions engaging in what are ordinarily known as nonbanking functions. We will hear the witnesses who have indicated a desire to be heard on either or both of these bills, as they are called.

Before calling the first witness, we will make part of the record at this point the two bills, and following that, we will put in the record the statements of Government agencies which submit such statements. These statements have not yet come in, but they will be made a part of the record at this point when they do come in from the Comptroller of the Currency, the Federal Reserve Board, the Federal Deposit Insurance Corporation, and in addition, statements from the National Association of Supervisors of State Banks, the American Society of Travel Agents, and the Independent Bankers Association.

(H.R. 9548 and H.R. 9822 follow:)

[H.R. 9548, 88th Cong., 1st sess.]

A BILL To prohibit banks from performing certain nonbanking services, and for other purposes

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That no bank of any type described in section 2 of this Act may perform any clerical, administrative, bookkeeping, statistical,

accounting, or other similar services for its depositors, borrowers, or other customers, except to the extent that such services are a necessary incident to the proper discharge of lawful functions of such bank as a depository, lender, trustee, or agent.

SEC. 2. This Act shall be administered and enforced in the case of—

(1) national banks or banks operating under the code of laws for the District of Columbia, by the Comptroller of the Currency;

(2) banks (other than banks described in paragraph (1)) which are members of the Federal Reserve System, by the Board of Governors of the Federal Reserve System; and

(3) banks (other than banks described in paragraph (1) or (2)) whose deposits are insured by the Federal Deposit Insurance Corporation, by the Board of Directors of the Federal Deposit Insurance Corporation.

The Federal banking agencies specified in this section are respectively authorized to make such rules and regulations as may be necessary to carry out the purposes of this Act.

[H.R. 9822, 88th Cong., 2d sess.]

A BILL To prohibit banks from engaging in the business of personal property leasing

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That no bank of any type described in section 2 of this Act may be the lessor of any personal property under any circumstances or by any means as a result of which such bank—

(1) performs or is compensated for any services other than the lending of money or advancement of credit with respect to such property, or

(2) acquires or may acquire any interest in such property other than as security for the repayment to such bank of money or credit advanced by it together with interest and other charges for exclusively financial services, or may realize from such property in the event of default more than such repayment and charges.

SEC. 2. This Act shall be administered and enforced in the case of—

(1) national banks or banks operating under the code of laws for the District of Columbia, by the Comptroller of the Currency;

(2) banks (other than banks described in paragraph (1)) which are members of the Federal Reserve System, by the Board of Governors of the Federal Reserve System; and

(3) banks (other than banks described in paragraph (1) or (2)) whose deposits are insured by the Federal Deposit Insurance Corporation, by the Board of Directors of the Federal Deposit Insurance Corporation.

The Federal banking agencies specified in this section are respectively authorized to make such rules and regulations as may be necessary to carry out the purposes of this Act.

(The letters from the Federal Reserve System, Federal Deposit Insurance Corporation, the Comptroller of the Currency, Independent Bankers Association, and the American Society of Travel Agents follow:)

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,
OFFICE OF THE CHAIRMAN,
Washington, February 24, 1964.

HON. ABRAHAM J. MULTER,
Chairman, Subcommittee on Bank Supervision and Insurance,
Committee on Banking and Currency,
House of Representatives,
Washington, D.C.

DEAR MR. CHAIRMAN: This is to confirm arrangements made between the counsel of your subcommittee and the Board's legislative counsel concerning tomorrow's hearing on H.R. 9548, to prohibit banks from performing certain non-banking services, and for other purposes, and H.R. 9822, to prohibit banks from engaging in the business of personal property leasing.

While I appreciate your extending an invitation for a witness to testify on the Board's behalf, the Board's position on these bills has not been decided. We are studying the proposals, and expect to present the Board's views by letter within 2 weeks.

Sincerely yours,

WM. MCC. MARTIN, JR.

FEDERAL DEPOSIT INSURANCE CORPORATION,
Washington, February 21, 1964.

HON. ABRAHAM J. MULTER,
Chairman, Subcommittee on Bank Supervision and Insurance,
House of Representatives,
Washington, D.C.

DEAR ABE: On February 19, 1964, Mr. Charles S. Beller, assistant counsel for the House Banking and Currency Committee, requested that we testify at your hearings on February 25, on H.R. 9548 and H.R. 9822.

Our General Counsel has discussed these proposals with Mr. Beller today and in view of the scope of this legislation and the limited notice, we would appreciate an opportunity to submit a report of our views by March 2 instead of testifying on February 25.

With best regards, I am,
Sincerely yours,

JOSEPH W. BARR, *Chairman.*

COMPTROLLER OF THE CURRENCY, U.S. TREASURY,
Washington, D.C., February 24, 1964.

HON. ABRAHAM J. MULTER,
Chairman, Subcommittee on Bank Supervision and Insurance,
Banking and Currency Committee,
House of Representatives,
Washington, D.C.

DEAR MR. CHAIRMAN: Due to the shortness of time of notification, we have been unable to complete reports on H.R. 9822 and H.R. 9548. We will do so as soon as possible and submit them for the record.

Sincerely,

JAMES J. SAXON,
Comptroller of the Currency.

INDEPENDENT BANKERS ASSOCIATION,
Washington, D.C., February 24, 1964.

HON. ABRAHAM J. MULTER,
House of Representatives,
Washington, D.C.

DEAR MR. CHAIRMAN: We are advised that your committee has scheduled hearings for Tuesday, February 25, to consider newly introduced measures, H.R. 9548, to prohibit banks from performing certain nonbanking services, and H.R. 9822, to prohibit banks from engaging in the business of personal property leasing.

We are interested in submitting a statement for the committee record on these matters, and request permission to file such a statement with your committee, to be introduced in the printed record. We will prepare and submit this statement, with your approval and concurrence.

Best regards.

Respectfully and sincerely,

C. HERSCHEL SCHOOLEY.

WILKINSON, CRAGUN & BARKER,
Washington, D.C., February 24, 1964.

Re H.R. 9548 and H.R. 9822.

HON. ABRAHAM J. MULTER,
Chairman of the Subcommittee on Bank Supervision and Insurance of the
Committee on Banking and Currency, House of Representatives, Wash-
ington, D.C.

DEAR CONGRESSMAN MULTER: This letter is written on behalf of the more than 1,650 active travel agency members of the American Society of Travel Agents (ASTA). ASTA is the only industrywide trade association of travel agents and its main offices are located at 360 Lexington Avenue, third floor, New York, N.Y.

It has recently come to our attention that your Subcommittee on Bank Supervision and Insurance will conduct hearings on February 25 concerning H.R.

9548 and H.R. 9822, bills to prohibit banks from performing certain nonbanking services.

As you may know, there has been a recent increase in travel agency activities among many banks throughout the country. Although we recognize that the two bills under consideration are confined to specific activities not related to the operation of travel agency activities, we thought that in view of the statement by Chairman Patman that the subcommittee will also consider "the advisability of enlarging these bills to exclude the performance of all nonbanking services by banks for depositors or others with or without compensation," that your subcommittee would find ASTA's views of interest.

Milton A. Marks, president of ASTA, is currently traveling abroad and is expected to return to this country during the first part of March. Because of the importance of this inquiry to the members of ASTA, we request the opportunity to formulate a detailed statement of the society's views in consultation with Mr. Marks and request that we be given the opportunity to file these views with your subcommittee no later than March 11, 1964.

Very truly yours,

WILKINSON, CRAGUN & BARKER,
GLEN A. WILKINSON.

(The statements from the Federal Reserve System, the Federal Deposit Insurance Corporation, the Comptroller of the Currency, the National Association of Supervisors of State Banks, the Independent Bankers Association, the American Society of Travel Agents, and the National Automobile Dealers Association follow:)

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM,
Washington, March 25, 1964.

HON. ABRAHAM J. MULTER,

Chairman, Subcommittee on Bank Supervision and Insurance, Committee on Banking and Currency, House of Representatives, Washington, D.C.

MY DEAR MR. CHAIRMAN: This is in response to your request for a report from the Board of Governors on H.R. 9548, a bill to prohibit banks from performing certain nonbanking services, and for other purposes.

The bill would prohibit every national bank, State member bank, and other insured bank from performing "any clerical, administrative, bookkeeping, statistical, accounting, or other similar services for its depositors, borrowers, or other customers, except to the extent that such services are a necessary incident to the proper discharge of lawful functions of such banks as a depository, lender, trustee, or agent."

The Board would not favor enactment of H.R. 9548. The Board does, however, share the misgivings that have been expressed concerning the tendency of some banks with modern data processing and other automated equipment to use it for the performance of services essentially unrelated to banking.

The problem arises in large part from the relatively high cost of such equipment and its adaptability to the performance of a wide range of data processing and related services. In order to utilize its equipment economically, a bank should not be prohibited some latitude in selling computer services, time, and capacity in excess of its own needs. Occasions for this may arise especially at the outset of a bank's computer operation and before some of the banking functions susceptible thereto have been automated. At the same time, the Board believes that, as nearly as practicable, a bank's computer installation should be used principally for the performance of normal banking functions, either for itself or for other banks, and that the size or capacity of the installation should be limited accordingly. Normal banking services should be regarded as excluding services for nonbank customers unless there exists a specific tie-in between the particular service and a banking transaction for the customer involved.

Voluntary adherence to the principles outlined above would adequately keep banks in the banking business, and we believe your hearings will help in minimizing the problems that have arisen as banks seek to find their proper role in furnishing data processing services. As indicated previously, the Board does not think that the situation warrants so severe a step as the adoption of the prohibition in H.R. 9548.

Public Law 87-856, approved October 23, 1962, permits banks to pool their efforts by joining in the ownership of data processing organizations. Section

4 of that act forbids such a cooperative service corporation to "engage in any activity other than the performance of bank services for banks." If a single bank owning data processing equipment is permitted to use its excess capacity for other than its own needs, these cooperative service corporations should likewise be authorized to do so and hence section 4 should be repealed.

Sincerely yours,

WM. McC. MARTIN, JR.

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM,
Washington, March 26, 1964.

HON. ABRAHAM J. MULTER,
Chairman, Subcommittee on Bank Supervision and Insurance, Committee on Banking and Currency, House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: This is in response to your request for the Board's views on H.R. 9822, a bill to prohibit banks from engaging in the business of personal property leasing.

From your remarks on January 31, 1964, on the floor of the House, it appears that introduction of H.R. 9822 was prompted by the views set out in a letter of March 18, 1963, to the presidents of all national banks from the Comptroller of the Currency. As reprinted in his "Manual for National Banks," paragraph 3400, the Comptroller's position on this matter is as follows:

"A national bank may become the owner and lessor of personal property acquired upon the specific request of and for the use of a customer and may incur such additional obligations as may be incident to becoming an owner and lessor of such property. These transactions do not result in obligations subject to the lending limits set forth in 12 U.S.C. 84."

In the opinion of the Board, "leasing" of personal property by banks divides, broadly speaking, into two quite different kinds of transactions. As explained hereinafter, one kind is unobjectionable, and in fact may be advantageous to the bank or its customers. The other type, in the Board's judgment, is not a suitable activity for banks and should be discouraged or prohibited. Accordingly, the practice of "leasing" by banks should not be either completely permitted or completely prohibited; the beneficial kind of lease arrangements should be permitted and the undesirable kind should be prevented.

As you know, banks frequently make loans on the security of personal property, the bank being protected either by a physical pledge of the property or by a security lien thereon, usually in the form of a recorded chattel mortgage. But in certain circumstances, it seems, banks have found that the protection afforded by a chattel mortgage may not be entirely effective in the event of the borrower's insolvency, for example. For this reason and perhaps to gain other benefits for the bank or its customers, banks have sometimes extended credit by purchasing personal property and "leasing" it to a customer for the full purchase price, instead of lending the customer the funds to purchase the property and then receiving a chattel mortgage thereon.

An illustration may clarify this procedure. A bank's customer wishes to acquire 10 trucks costing \$10,000 each. Ordinarily, the bank would lend the customer the needed \$100,000, and the customer would purchase the trucks and give the bank a chattel mortgage, to protect it in the event of the borrower's default. Occasionally, however, a bank may prefer to purchase the trucks and then to "lease" them to the customer, title being retained by the bank while the trucks are used by the customer. Under both arrangements, all other terms are substantially identical—for example, the customer might repay the bank \$25,000 semiannually, together with interest at 5 percent on the outstanding balance. In each case, at the end of 2 years the bank would have been repaid its \$100,000 advance with interest at the agreed rate, and the customer would then own the trucks free of any lien. In the case of the chattel mortgage, the lien of the mortgage would be released after full repayment; whereas in the case of the lease arrangement, the bank would transfer title to the customer in accordance with the lease/sale agreement.

In the opinion of the Board such uses of lease arrangements are unobjectionable. They may provide the bank with the strongest possible lien to protect its extension of credit or the borrower with a form of credit best suited to its needs. To prohibit banks from "leasing" property in this way would only deprive them of a useful security device.

The other kind of leasing, however, is quite different in purpose and effect and in its status with respect to sound banking principles. It may be best to illustrate this in a comparable situation.

In the case described above, the bank's customer might not wish to purchase the 10 trucks, but only to use them until the completion of a specific construction job, expected to take 6 months. In such a case, he might request the bank to purchase the trucks and to lease them to him for 6 months at a rental of \$40,000 for the 6-month period.

If a bank purchased and leased the trucks in these circumstances, the transaction would not be a secured extension of credit, as in the other case. The bank would not be advancing \$100,000 in reliance on the promise of its customer to reimburse that amount to the bank, with interest. Instead of a security title, as in the first case, the bank would acquire general ownership of the trucks, with all the opportunities for gain and risks of loss inherent in the ownership and leasing of property. After the first customer had used the trucks for 6 months and paid the bank \$40,000, as stipulated in the lease agreement, the bank would be the owner of 10 used trucks in which it still had an investment of \$60,000, and it would be compelled either to sell the trucks at the best available price or to seek to lease them to one or more successive lessees. Depending upon the bank's skill and enterprise, and economic conditions generally and in the secondhand truck field (or truck leasing business) specifically, the bank as an entrepreneur might emerge from the venture with a substantial loss or a substantial profit. In either event, however, the essence of the bank's operation would be the purchasing and leasing of equipment rather than the extension of secured credit, as in the case first described.

The ruling of the Comptroller of the Currency, set forth above, might be read as purporting to authorize national banks to engage in leasing of the second type. This interpretation of his ruling seems to be supported by the statement therein that the transactions referred to by the Comptroller are not subject to statutory lending limits, since true extensions of credit through the lease/sale mechanism, the Board presumes, would be subject to the same limitations as other loan transactions. (If the Comptroller should actually take the position that extensions of credit are exempt from statutory limits when handled through lease arrangements, the situation would call for legislative correction.)

The Board infers that H.R. 9822 was introduced with the purpose of preventing banks from engaging in leasing activities of the second type, as apparently approved by the Comptroller. The Board believes that such an objective would be sound. However, the provisions of the first section of the bill, read in connection with its title, might be construed as prohibiting not only the second type of transaction, but also the first, which the Board regards as an appropriate device for the extension of secured credit, as has been indicated.

The Board does not know how the Comptroller's ruling has been interpreted and applied by national banks or the extent to which national banks and State banks engage in purchasing and leasing equipment and other personal property in an unsafe and unsound manner. It is likely that few, if any, banks will engage in such activities, in which case prohibitive legislation would be unnecessary. If, however, Congress should decide that legislation along these lines is desirable in any event, the Board suggests that such legislation be so drafted as not to prevent banks from using lease arrangements as a form of security for legitimate extensions of credit.

Sincerely yours,

WM. McC. MARTIN, Jr.

FEDERAL DEPOSIT INSURANCE CORPORATION,

Washington.

HON. ABRAHAM J. MULTER,

Chairman, Subcommittee on Bank Supervision and Insurance, Committee on Banking and Currency, House of Representatives, Washington, D.C.

DEAR ARE: You have requested the views of this Corporation on H.R. 9548, a bill to prohibit banks from performing nonbanking services, and for other purposes. The bill places on the three Federal banking agencies the duty of regulating for banks under their individual jurisdiction what "clerical, administrative, bookkeeping, statistical, accounting, or other similar services" for bank depositors, borrowers, or other customers are "a necessary incident to the

proper discharge of lawful functions of such bank as a depository, lender, trustee, or agent."

Bank services of course have varied through the years and have increased as the needs of the banking business and the needs of the banks' customers and communities have grown. They have become an essential part of the banks' business. Regulated as to maximum interest rates on deposits and loans, banks must compete for business with added services. Such services to customers are generally in the area of the banks' own operation and supplement the banks' efficient use of their personnel and equipment.

Services have been rendered by banks for many years without question as to their legality or propriety, without hazard and with resulting benefit of efficient and reasonable services to the bank, its customers and the community. As we see it, this bill would only add to the costs of all concerned. If a bank can perform a service related to its business operation for anyone in its community at a lower cost than others and thereby operate more efficiently and economically, it should not, in our opinion, be barred from doing it.

When you introduced this bill you emphasized automatic data processing and other automated recordkeeping equipment and the need to prevent broadening of "service to bank customers during the course of their normal banking functions" to include "the taking over of bookkeeping and accounting functions for businessmen."

Presumably the purpose of this proposed legislation is to prevent banks from furnishing accounting and other data processing services to customers, unless these activities conform to the pattern that has always been characteristic of banking. Nevertheless, the language of the prohibitions is exceedingly broad in scope and it would seem to cloud the legality of many important banking services that banks have always performed for their customers.

These are changing times and banking cannot be insulated from the mainstream of technical progress. Hope is widespread that the application of electronic data processing equipment to the clerical work inherent in banking may enable the industry to master its ever-spiraling workload. Without the introduction of entirely new methods that greatly increase the effectiveness of the limited amount of human effort available for clerical routines it would be impossible for banking to pace the growth of economy at a reasonable cost.

Automatic data processing equipment can be introduced in the industry only on a bank-by-bank basis. The methods are novel, the equipment entails heavy capital investment, and their applications require much experimentation. There is good reason to believe that automation of clerical work will result in cost savings, and certainly it is the only way to prevent paperwork expenses from growing out of hand in the long run. It is reasonable, meanwhile, to expect that installations in some banks will have capacity in excess of the immediate needs. To prohibit the employment of such excess capacity not only increases the cost of such equipment in nonbanking installations but it also increases bank costs by denying the employment of otherwise idle facilities. Thus, any legislative proscriptions that handicap the introduction of new data processing facilities in banking prevent or delay the adoption of cost-savings measures that will eventually mean economies to bank customers.

Viewed objectively, this legislation has as a necessary consequence a slowing down of the efforts now widespread to automate paper processing activities. If that is the real objective, then its scope should be extended throughout all industry and not confined to banking. To be sure, automation in the clerical field will pose serious problems to accountants and others who also must adapt to new facilities. It is not in the public interest to preserve well-established patterns of economic activity when new and more efficient methods are available. Accountants will still be able to perform their professional duties for their customers and both would be assisted by more economical mechanical bank services. In fact, the full use of data processing equipment should enable accountants to more effectively serve the requirements of their bank clients.

Whether the management of a bank is devoting too much of its energy and funds to the performance of clerical services for customers who can use multi-purpose automated equipment is a question of fact to be answered in each case and can be controlled by bank supervision. The broad prohibition on service activities, contemplated by this legislation as a method to regulate data processing in banks, will be harmful to banking specifically and the business community generally.

For these reasons we do not recommend the enactment of H.R. 9548.

In 1962 Public Law 87-856 authorized banks to invest in corporations whose purpose is to provide bank services. Section 4 of this act provides that no bank service corporation may engage in any activity other than the performance of bank services for banks. The legislative proposal, enacted as Public Law 87-856, was originally intended to enable small banks to participate with other banks and business to avail themselves of efficient services at reasonable costs from bank service corporations. If these small banks can acquire these services on a more economical and efficient basis at lower costs to themselves and to others through the participation by other businesses in the services rendered by such a bank service corporation they should, in our opinion, be permitted to do so. We believe that the efficiency of the service corporations and the resulting benefits, through lower costs, to investing banks would be increased if the service corporations were not limited to serving banks exclusively. For these reasons, we believe section 4 of Public Law 87-856 imposes an unreasonable and costly burden on bank service corporations and should be removed by Congress. Accordingly, the Corporation recommends the repeal of section 4 of Public Law 87-856.

We have been advised by the Bureau of the Budget that it has no objection from the standpoint of the administration's program to the submission of this letter.

Sincerely yours,

JOSEPH W. BARR, *Chairman.*

FEDERAL DEPOSIT INSURANCE CORPORATION,
Washington, April 10, 1964.

HON. ABRAHAM J. MULTER,
Chairman, Subcommittee on Bank Supervision and Insurance, Committee on Banking and Currency, House of Representatives, Washington, D.C.

DEAR ABE: You have requested the views of this Corporation on H.R. 9822, a bill to prohibit banks from engaging in the business of personal property leasing.

Because of the few insured banks engaged in the practice of personal property leasing and the absence of any known bank supervision problems in this area, I might say that in the narrow sense the Corporation would have little interest in the proposed legislation. However, in the broader concern of the Corporation for all banks in the Federal deposit insurance system, I would like to express the Corporation's views on H.R. 9822.

This legislation is designed to prevent banks from engaging in the business of leasing equipment such as motor vehicles—passenger cars and trucks—to a series of users most of whose needs do not encompass the entire life of the machine. Typically, the pieces of equipment are rather costly. They are useful for a number of years and the users comprise a rather broad and diversified market. The need for the equipment is intermittent, often related to a specific job with relatively short duration. Finally, a lease arrangement is used to protect the capital investment.

Specialized equipment leasing companies are intermediaries who render essentially a financing service. With a minimum amount of ownership equity, these enterprises in turn are heavy borrowers from the banks to finance the acquisition of equipment. Only to a very limited extent do firms engaged in the rental of equipment customarily engage in property management activities.

The use of a lease on equipment to facilitate the employment of bank funds is far from new. For many decades the railroads have financed rolling stock by this arrangement. The user of equipment, the railroad company, is the lessee and repays the investment in equipment as it wears out in the technical form of rentals. Large sums of money are involved in this type of financing and many banks as well as other investors participate by the acquisition of investments known as equipment trust certificates. Such securities are issued by a trustee who holds legal title to the rolling stock.

To be sure, equipment trust financing in the railroad industry usually contemplated one rather than a series of lessees, but on occasion when the original lessee defaulted equipment was leased to other users. Furthermore, this form of financing has been applied to other types of equipment such as airplanes and heavy machinery. The performance of the lease arrangement in railroad financing has been good. Nevertheless, the legislation as proposed would surely becloud, if it does not actually prohibit, a form of bank investments that his-

torically has financed successfully and at low cost a very large portion of all railroad equipment.

Admittedly, bank financing of equipment by a lease arrangement—irrespective of whether it covers railroad rolling stock, motor vehicles, or other heavy machinery—differs from a bank's loan and discount operations. But this in itself does not taint lease financing. Looking to the substance of the transaction, in any event it is obvious that bank funds would be used to finance the equipment. With respect to equipment financing the difference between the lease arrangement and a bank loan to an equipment leasing company is largely the extent of management needed to service the transaction. Control over the property by the bank in a leasing arrangement would seem to afford better protection for the bank.

Where equipment leasing is lawful for a bank, the practice cannot be condemned out of hand merely because there are nonbanking firms engaged in this business. If a bank has a staff with sufficient managerial skill to engage in equipment financing by means of lease arrangements then this type of business is not objectionable. The same can be said, of course, for many other specialized types of banking that have developed in recent years—for example, consumer financing or the financing of automobile dealers.

In net effect the prohibition of equipment lease financing by banks would increase costs to equipment users. Insofar as the prohibition made it impossible for efficient banks to perform this type of financing, it would support inefficient and high cost operators to the detriment of the public.

Bank supervision in the course of periodic examinations, among other things, reviews the quality of management in each individual bank. Certainly the review that appraises managerial skills would detect those banks that could not properly engage in equipment lease financing and these could be discouraged from engaging in this type of business.

For the reasons set forth herein, this Corporation would not favor the enactment of H.R. 9822 by the Congress. Instead, we would recommend that any question of the authority of national banks to engage in direct leasing be removed by express authorization with the bank's legal limit to any single borrower made applicable to the aggregate of borrowings and leasing by any person. To our knowledge, few banks are now engaging in direct leasing of personal property. If future experience should disclose unsafe or unsound aspects of personal property leasing by banks, this Corporation would support corrective legislation.

We have been advised by the Bureau of the Budget that it has no objection from the standpoint of the administration's program to the submission of this letter.

Sincerely yours,

JOSEPH W. BARR, *Chairman.*

COMPTROLLER OF THE CURRENCY,
TREASURY DEPARTMENT,
Washington, D.C., April 1, 1964.

HON. ABRAHAM J. MULTER,
*Chairman, Subcommittee on Bank Supervision and Insurance, Banking and
Currency Committee, House of Representatives, Washington, D.C.*

DEAR MR. CHAIRMAN: You have requested our views on H.R. 9548 which is designated "A bill to prohibit banks from performing certain nonbanking services, and for other purposes."

We strongly oppose the passage of this legislation. Our opposition is based on both procedural and substantive grounds. Procedurally, the language of the bill would be very difficult to interpret and administer. The operative language of the bill is as follows:

"That no bank of any type described in section 2 of this Act may perform any clerical, administrative, bookkeeping, statistical, accounting, or other similar services for its depositors, borrowers, or other customers, except to the extent that such services are a necessary incident to the proper discharge of lawful functions of such bank as a depository, lender, trustee, or agent."

Difficult problems of interpretation are immediately apparent. For instance: What is the meaning of the word "necessary"?

What are "other similar services"?

Whose determination of necessity is to control? If a banker is of the opinion that a particular service is necessary to the proper discharge of his

duties toward a customer, is this sufficient to make the service permissible under the bill? Or is the supervisory agency to determine what services are "a necessary incident to the proper discharge of lawful functions of such bank as depository, lender, trustee, or agent"?

Even if it were possible to resolve these questions of legal interpretation by redrafting, we would strongly oppose the legislation because we do not agree with its fundamental purpose, which is to constrict by governmental fiat the business operations of commercial banks. Why should not a bank be permitted to perform whatever clerical, administrative, bookkeeping, statistical, etc., services for its customers which its management believes can be performed profitably? We can understand the opposition of groups who imagine they would be hurt competitively by such activities but we see no legal or policy basis for eliminating such competition.

We do not think the argument of some accountants that banks are transgressing on their domain is tenable. The practice of accounting is regulated by State laws throughout the country. Any acts by a corporation within a State's borders which were violative of such licensing statutes, would be subject to prosecution. This has not happened to date because the type of services which we are concerned about here are not in fact professional services, but are repetitive, clerical-type functions which are susceptible to automation. This whole problem is a creature of the automatic data processing machine. The claim of unauthorized accounting is also being raised as a smokescreen by some data processing machine interests who are no more qualified as accountants than are bankers.

The spirit of this bill is directly at odds with the previously expressed intent of Congress as long ago as 1864 and as recently as 1962. In 1864, in the National Bank Act, Congress stated that national banks shall have "all incidental powers as shall be necessary to carry on the business of banking" (12 U.S.C. 24, par. 7). Congress in 1864 wisely did not attempt to define the business of banking as it then existed. They foresaw that the business of banking would change and develop with the passing years. The sweeping nature of the technological changes in the banking business is strikingly illustrated by the necessity for the passage almost a hundred years later of H.R. 8874, the bank service corporation bill (Public Law 87-856, 87th Cong., October 23, 1962) which deals with the virtual necessity of the use today by banks of expensive automatic equipment.

H.R. 9548 does just what Congress in its wisdom in 1864 would not do—attempts to define the business of banking. This definition which is limited to acting as "depository, lender, trustee, or agent" is entirely inadequate as a description of modern commercial banking. In any event, we do not think it is any more desirable to attempt to legislate such a definition in 1964 than it was in 1864.

In 1962, Congress passed H.R. 8874, the bank service corporation bill which empowered banks to invest in corporations created for the purpose of rendering clerical services to banks. The proponents of H.R. 8874 thought that the bill was necessary because of existing prohibitions against national banks' owning the stock of corporations.

There was no question concerning the banks' right to perform these services directly for their customers on their own equipment. We regard it as highly unfortunate that a provision was added to H.R. 8874 at the last minute, prohibiting bank service corporations from performing any services for anyone other than banks.

The Senate Banking and Currency Committee, in its reports on H.R. 8874, had this to say on the subject of the increasing use of automation equipment by banks:

"The demand for bank services is increasing at an extremely rapid rate. Many banks have found it difficult to acquire adequate personnel to handle this mounting workload. Testimony indicated that the volume of checks in circulation has increased tremendously during the past two decades. It was estimated that the check volume in 1939 was 3.5 billion. The volume is increasing at the rate of about one-half billion items per year. By 1970 the number of checks

is expected to be at an annual rate of 22 billion. In addition to check handling there is a need for automation of other bank services. Some banks are now processing their savings accounts, computing payrolls, calculating other credits and charges, and preparing and mailing statements through the use of automatic equipment.

"The high cost of equipment makes it impossible for the majority of banks to buy this equipment. In some cases they are able to lease it, or to have their material processed by firms owning this equipment. But in many cases these solutions are not practicable or desirable.

"Larger banks are generally able to afford this automatic equipment, but smaller institutions find the cost prohibitive. According to a study made by the Federal Reserve System, nearly all large banks in the group they surveyed are now using some form of automated equipment or plan to do so within the next 3 years. However, the ratio of automating banks to the total number of banks falls rapidly as one moves down the scale in bank size. Only about one-fifth of the banks with deposits of \$25 to \$50 million have automation plans and among smaller banks the proportion is negligible. Thus, it is becoming more and more difficult for smaller banks to compete with larger banks in offering complete and efficient banking services to their customers. Testimony was received which indicated that, unless a satisfactory means is devised whereby smaller banks may acquire benefits of automated equipment, many of them may be absorbed by larger banks or compelled to merge with other banks in the area.

"Under this bill two or more banks would be able to pool their resources through the corporate device in order to gain the benefits of this expensive equipment for themselves and for the people in their communities."

We believe it would be quixotic for the Congress to attempt now to stem the performance of automation services for their customers by banks. Banking, like any industry, is entitled to the benefits of technological change and, in our opinion, it would be wrong and perhaps futile for Congress to attempt to shackle this industry as does this bill.

We strongly urge against enactment of H.R. 9548.

Sincerely,

JAMES J. SAXON,
Comptroller of the Currency.

COMPTROLLER OF THE CURRENCY,
TREASURY DEPARTMENT,
Washington, D.C., April 8, 1964.

HON. ABRAHAM J. MULTER,
Chairman, Subcommittee on Bank Supervision and Insurance, Banking and Currency Committee, House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: You have requested the views of this Office on H.R. 9822 which is designated "A bill to prohibit banks from engaging in the business of personal property leasing." This Office strongly opposes the passage of the legislation. The operative language of the bill is as follows:

"That no bank of any type described in section 2 of this Act may be the lessor of any personal property under any circumstances or by any means as a result of which such bank—

"(1) performs or is compensated for any services other than the lending of money or advancement of credit with respect to such property, or

"(2) acquires or may acquire any interest in such property other than as security for the repayment to such bank of money or credit advanced by it together with interest and other charges for exclusively financial services, or may realize from such property in the event of default more than such repayment and charges."

This Office fundamentally disagrees with the purpose of this legislation which is to unduly restrict, for the private benefit of a competing group, the business operations of banks. We see no reason why a bank should not be permitted to engage in all forms of financing and perform all phases of the business of banking for its customers which its management believes can be performed profitably.

The objective of this bill appears contrary to the intent of Congress expressed in the National Bank Act, that national banks shall have "all such incidental powers as shall be necessary to carry on the business of banking" (12 U.S.C. 24, par. 7). Congress in 1864 wisely did not attempt to define the business of banking as it then existed. They foresaw that the business of banking would change and develop with the passing years. The sweeping character of these changes is evidenced by the variety of nonbank financial institutions, including leasing companies, which exist today in response to public financial needs which banks, in part, failed to satisfy. H.R. 9822 would constrict for the benefit of these leasing companies the powers of banks which, as financial-service institutions, are best situated to respond to the public demand for what is essentially a financing transaction.

Banks have, from the beginning of commercial banking, financed the acquisition and the use of personal property. They have lent money on the security of some form of ownership or control of the property financed. They have also lent money to lessors on the security of the lessee's agreement to pay rent. The power of banks to engage in lease financing transactions is entirely a financing power. While the banks may become the owner of commodities, they may not carry out the functions of the merchant. They may not purchase commodities for stock, and hold them for eventual anticipated lease or sale. They may purchase only at the request of a customer who wishes to have the full and immediate use of the commodity on a lease basis. Banks become the owner of commodities in permitted lease financing transactions principally for the purpose of providing a well-defined financial, and not a merchandising, service. They do not offer or solicit the sale of commodities—but only of financing. When banks enter into direct lease financing arrangements, they compete not with leasing companies, but with other sources of financing. The distributive and property management functions, as contrasted with financing, are really performed by the lessee himself where the transaction is handled directly by a bank.

This Office understands the opposition of those engaged in direct leasing who contend that they may be hurt competitively where such activities are conducted by banks, but this Office sees no legal or policy basis for eliminating or preventing such competition. The argument of some leasing companies that banks are violating their exclusive domain of direct leasing of personal property is entirely without merit. Such lessors, in most instances, are thinly capitalized corporations which discount their leases with a bank, act solely as holders of title and are nominal debtors. As such, they are relatively expensive retailers of bank credit. Throughout the private enterprise economy of this Nation, under the influence of competitive forces, there continues a constant search for improved means both of production and distribution. It is not "unfair" for any entrepreneur to devise less costly and more effective methods of serving consumers, which is indeed, the basic aim that we seek to achieve under our free enterprise system. If banks are able to provide a less costly means of financing the distribution of commodities and services, such result inures only to the advantage of the consuming public. It is the consumer, and not any class of producers or distributors who ought to be safeguarded.

It is the position of this Office that it would be an anomaly for Congress to reserve to the benefit of a select group a particular segment of financial business, while it prohibits that some business to the banks, which were clearly created by the Federal and State Governments for the purpose of meeting and satisfying public financial needs. Banking, like any industry, is entitled to the benefits of new business forms and developments in financial transactions and, in the opinion of this Office, it would be myopic and contrary to the public interest to attempt to constrict the banking industry as would this bill.

Sincerely,

JAMES J. SAXON,
Comptroller of the Currency.

NATIONAL ASSOCIATION OF SUPERVISORS OF STATE BANKS,
Washington, D.C., February 24, 1964.

Subject: H.R. 9822 and H.R. 9548.

HON. ABRAHAM J. MULTER,
*Chairman, Subcommittee on Bank Supervision and Insurance,
 Committee on Banking and Currency,
 House of Representatives,
 Washington, D.C.*

DEAR REPRESENTATIVE MULTER: The National Association of Supervisors of State Banks appreciates your invitation to comment upon the captioned bills.

1. H.R. 9822: TO PROHIBIT BANKS FROM ENGAGING IN THE BUSINESS OF PERSONAL PROPERTY LEASING

Background.—As you know, prior to March of 1963, it was generally believed that national banks had no authority to engage in personal property leasing. In September 1962, the Advisory Committee on Banking to the Comptroller of the Currency recommended that national banks be permitted to do so under certain circumstances. On March 18, 1963, the Comptroller addressed a letter to the presidents of all national banks, ruling that certain direct leasing of personal property "is a lawful exercise of the powers of a national bank and necessary to the business of banking." During the hearings before this subcommittee last May, the Comptroller was extensively questioned with regard to the competitive effect of this ruling on automobile dealers.

H.R. 9822, we understand, is an effort to amend the law to counteract the Comptroller's ruling and to restore the status quo prior to March 18, 1963, when, it was generally believed, national banks had no authority to engage in personal property leasing.

NASSB position.—NASSB, of course, takes no position on the question of whether the above-referenced ruling of the Comptroller, applicable only to national banks, should be legislatively reversed. That is the matter for this committee to determine.

Our focus is entirely upon that portion of the bill which goes beyond a reversal of the Comptroller's ruling applicable to national banks, to extend Federal regulation over State banks by promulgating a prohibition against State member and nonmember-insured banks engaging in personal property leasing, and authorizing the FDIC and Federal Reserve Board to establish rules and regulations to implement that directive.

We do not have any information at this time as to the extent to which State banks are permitted under State law to engage in this practice and, if so, the extent to which they have, in fact, done so. Without this information, we cannot even comment on the question of whether the bill is addressing itself to a hypothetical situation as far as State banks are concerned.

Further, we have not had time to poll the 50 State bank supervisors to ascertain their attitude toward this practice.

We have, however, sent out an extensive questionnaire to all of the supervisors and hope to secure the foregoing information as soon as possible. As soon as it is assembled, we will forward it to the subcommittee.

However, we are clear on one point right now. As you know, we have appeared before this committee for many years, indicating our growing concern about the almost geometric rapidity with which the Federal Government has been extending its regulatory blanket over State banks. This Congress has, of course, complete authority to do anything it wants to with regard to national banks. Its authority, however, at least as yet, has only been exercised with regard to State banks which have voluntarily agreed to become members of the Federal Reserve System or have voluntarily agreed to deposit insurance. Federal regulation of State banks, therefore, should be limited to only such regulation where there is a strong, compelling, and vital reason why it is necessary to preserve the Federal

Reserve System or to eliminate any jeopardy to the deposit risk of the FDIC. We do not think this matter of personal property leasing falls into either category.

Accordingly, the NASSB says to this subcommittee, "Please go ahead and pass H.R. 9822 to reverse the Comptroller's recent ruling relating to national banks, if that is your desire, but please do not use that reversal as a vehicle to accelerate the Federal encroachment over the regulation of State banks. All reference to State banks should be removed from H.R. 9822."

2. H.R. 9548: TO PROHIBIT BANKS FROM PERFORMING NONBANKING SERVICES, AND FOR OTHER PURPOSES

Background.—H.R. 9548 is designed to stop banks from providing clerical, administrative, bookkeeping, statistical, accounting, or other similar services for its depositors, borrowers, or other customers, except as incidental to lawful functions of such bank as a depository, lender, trustee, or agent. This practice, we understand, has grown up in some banks anxious to use, in effect, "free time" on its data processing and other automated recordkeeping equipment, to be of assistance to clients.

The bill has received strong support from the National Society of Public Accountants who are seeking to stop what they consider to be encroachment into their area of expertise.

NASSB position.—As in the case of the subject matter of H.R. 9822, we have not had time to circulate our supervisors to ascertain the extent to which State banks can, and do, perform the services covered by the bill, or what the attitude of the supervisors may be with regard thereto. This poll has also been undertaken and the answers will be submitted to the subcommittee as soon as they are ascertained.

However, regardless of the result of the poll, we are again clear on one point which has already been discussed, in part, above.

There appear to be two reasons advanced as to why H.R. 9548 should be enacted.

The first appears to be a desire to protect the public accountants. This may be necessary—we do not comment at this point on the wisdom of that proposition. We do think, however, that this subcommittee will readily agree that it is completely inappropriate to use the fact that State banks have voluntarily joined the Federal Reserve System or the FDIC as a vehicle to impose additional Federal regulation on this in order to protect another group. Insofar as State banks are concerned, therefore, this is a matter which should be left completely up to the State legislatures.

The second reason appears to be a view that the bill is necessary to prohibit nonbanking activities. Again, we cannot agree or disagree with that proposition until after the results of the supervisors' questionnaire are in. However, as in the case of H.R. 9822, the more important question is whether the necessity of prohibiting this type of activity is so strong, so vital, and so compelling, that an additional encroachment of Federal regulation over State banks is required in order to preserve the Federal Reserve System or deposit insurance. We hardly think this is the case.

In concluding, we want to again emphasize the distinction which we are drawing between the end and the means. There are many supervisors who, we are sure, agree with the proposition that the activities covered by these two bills should be prohibited. However, we strongly feel that insofar as State banks are concerned, that prohibition is one which should be imposed by the States, not by the Federal Government. If we cannot draw the line of Federal encroachment over State banks on such relatively minor matters as these, there is, indeed, a dark road ahead for the preservation of the dual banking system.

Respectfully submitted.

RANDOLPH HUGHES,

Chairman, Legislative Committee, NASSB and State Bank Commissioner, Delaware.

NATIONAL ASSOCIATION OF SUPERVISORS OF STATE BANKS,
 Washington, D.C., March 12, 1964.

Re H.R. 9822 and H.R. 9548.

HON. ABRAHAM J. MULTER,
 Chairman, Subcommittee on Bank Supervision and Insurance, Committee on
 Banking and Currency, House of Representatives, Washington, D.C.

DEAR CONGRESSMAN MULTER: You will recall that last month we filed with your committee a letter over the signature of Randolph Hughes, chairman, NASSB Legislative Committee, regarding the above-captioned bills.

In that letter we indicated that a poll of our supervisory members was in process and that the answers would be submitted to your committee as quickly as possible. While all have not answered, we do have more than 40 responses and wanted to acquaint you with the results. Attached is a copy of the survey form on each bill, together with a recapitulation of the answers received to date.

If we can be of any further service to you or your committee, please advise us accordingly.

Cordially,

HOLLIS W. BURT,
 Executive Vice President.

SURVEY RE H.R. 9548—A BILL INTRODUCED IN THE HOUSE OF REPRESENTATIVES TO PROHIBIT BANKS FROM PERFORMING CERTAIN NONBANKING SERVICES, AND FOR OTHER PURPOSES

1. Under your existing law, regulation, or authority, can you prohibit banks under your jurisdiction from engaging in the business of performing certain nonbanking services—clerical, administrative, bookkeeping, statistical, accounting, or other similar services for its depositors, borrowers, or other customers, except to the extent that such services are a necessary incident to the proper discharge of lawful functions of such bank as a depository, lender, trustee, or agent?

Yes, can prohibit, 27; no, can't prohibit, 14; 41 total replies.

2. Assuming that such activity is permissible, do the banks in your State participate?

Yes, 8; no, 33.

3. Do you think that banks should be prohibited from engaging in the business of performing these nonbanking services?

Yes, should be prohibited, 29; no, should not be prohibited, 12.

4. Assuming that your answer to question No. 3 is "yes," should this be a matter for the States to decide—or do you believe there should be Federal legislation to cover this area?

State to decide, 35; Federal, 1.

 Supervisor

 State

NOTE FOR SUPERVISORS.—The House Banking and Currency Subcommittee is holding the record open for your answers. Please return the completed form to this office as quickly as possible.

HOLLIS W. BURT,
 Executive Vice President, NASSB.

SURVEY RE H.R. 9822—A BILL INTRODUCED IN THE HOUSE OF REPRESENTATIVES TO PROHIBIT BANKS FROM ENGAGING IN THE BUSINESS OF PERSONAL PROPERTY LEASING

1. Under your existing law, regulation, or authority, can you prohibit banks under your jurisdiction from engaging in the business of personal property leasing?

Yes, can prohibit, 32; no, can't prohibit, 7; 39 total replies.

2. Assuming that such activity is permissible, do the banks in your State participate?

Yes, 3; no, 36.

3. Do you think that banks should be prohibited from engaging in the business of personal property leasing?

Yes, should prohibit, 36; no, should not prohibit, 3.

4. Assuming that your answer to question No. 3 is "yes," should this be a matter for the States to decide—or do you believe there should be Federal legislation to cover this area?

State, 36; Federal, 1.

Supervisor

State

NOTE FOR SUPERVISORS.—The House Banking and Currency Subcommittee on Bank Supervision and Insurance is holding the record open for your answers. Please return the completed form to this office as quickly as possible.

HOLLIS W. BURT,
Executive Vice President, NASSB.

INDEPENDENT BANKERS ASSOCIATION,
Washington, D.C., March 13, 1964.

HON. ABRAHAM J. MULTER,
Chairman, Subcommittee on Bank Supervision and Insurance, House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: The Independent Bankers Association has your invitation to comment on measures to prohibit banks from performing nonbanking services, presently before your committee, and is privileged to respond, for your committee record.

The Bank Study and the Legislative Committees of our Association, at a meeting held earlier this week, in Chicago, to study a variety of legislative proposals, considered H.R. 9548 and H.R. 9822, currently the subject of hearings before your Subcommittee on Bank Supervision and Insurance.

In principle, we have a philosophy that Government should minimize the detailed regulations and definitions that circumscribe and restrict commercial banks in the exercise of normal and proper banking functions. We are concerned with trends that would replace our American dual banking system with the branches of big city, money market institutions, and are equally concerned lest bigness and concentration of banking power, under any guise or circumstance, eliminate the locally owned, independent banks of our Nation, in the name of progress, technological or otherwise.

Technological advances and improvements, including the automatic data processing equipment, are recognized as developments calculated to enable the locally owned, locally managed, locally oriented independent bank to continue its essential role in the independent American community. Some committee members reported that they are already using such equipment to accelerate accurate, economical, day-to-day recordkeeping.

Others are considering the future employment of such equipment, and all expressed interest in the experience of early users among our committee membership.

Our committee, made up of 17 bankers from 15 States, unanimously voted opposition to H.R. 9548, believing it to be a measure that would unnecessarily circumscribe banks in their efforts to offer the best and most varied services to the business community.

The high initial cost and high upkeep cost of computers forces banks to seek ways to keep these machines operated as closely as possible to maximum capacity. Without this maximum use, banks would be unable to afford computer equipment.

In considering a statement of position on this piece of legislation—H.R. 9548—our committees turned to Public Law 87-856, enacted on October 23, 1962, and concerned with bank service corporations, which are designed to perform bank services for two or more banks. This measure has been referred to earlier, by witnesses testifying before your committee.

In this measure, section 4 provides that no bank service corporation may engage in any activity other than the performance of bank services for banks."

We, therefore, suggest in consideration of the proposed legislation, that the language of section 4, Public Law 87-856, be adapted and amended to provide that bank service corporations enjoy the same privileges which banks enjoy to provide bookkeeping services. In the event an appropriate amendment is not made, a condition will be tolerated which permits a large bank owning its computer, to offer services which cannot be offered by a group of banks which have joined together to establish a bank service corporation.

In the matter of H.R. 9822, our committees took no position at this time, pending further study of the leasing questions posed by the legislative proposal.

Sincerely,

S. E. BABINGTON, *President.*

AMERICAN SOCIETY OF TRAVEL AGENTS, INC.,
New York, N.Y., March 9, 1964.

Re H.R. 9548 and H.R. 9822.

HON. ABRAHAM J. MULTER,
Chairman of the Subcommittee on Bank Supervision and Insurance of the Committee on Banking and Currency, House of Representatives, Washington, D.C.

DEAR CONGRESSMAN MULTER: On February 24, 1964, the American Society of Travel Agents, Inc. (ASTA) requested permission to file comments with your subcommittee concerning its hearings on H.R. 9548 and H.R. 9822, bills to prohibit banks from performing certain nonbanking services. The following are ASTA's comments on this legislation:

On behalf of over 1,700 travel agency firms, members of ASTA, operating some 2,400 travel agency locations, it is a pleasure for us to support your efforts to enact legislation to confine banks to legitimate banking activities. We have analyzed the provisions of H.R. 9548 and H.R. 9822, and neither of these bills appears to prohibit banks from operating travel agencies or travel departments. The explanation for the omission of any reference to the operation of a travel agency by banks may be that this activity is so far removed from legitimate, normal banking business that you did not realize that a very great problem exists in this area. While ASTA does not choose to comment on the merits of those other nonbanking activities listed in each of the two bills, we do request that your legislation be amended to specifically prohibit banks from operating travel agencies or travel departments as part of their banking activities.

The question of banks engaging in the nonbanking activity of operating travel agencies has a most interesting history. The following is a brief summary of the radical changes of direction which have taken place in the office of the Comptroller of the Currency during the last few years regarding this issue:

On November 2, 1956, ASTA filed an extensive brief with the then Comptroller, Ray M. Gidney, and pointed out the lack of enforcement of the then long-established rule 67, which had been promulgated by the Comptroller. Rule 67 stated that national banks had no "legal right" to operate a "regular travel agency" but that a national bank could offer travel services to its customers only if it did * * * not hold itself out to the public as operating a travel agency * * *." The Comptroller responded in a letter of September 15, 1958, after a series of visits and further correspondence with ASTA, taking the position that each national bank should determine for itself whether its activities in the travel agency business were incidental to its specific powers granted by the National Banking Act and were, therefore, permissible. In effect, the Comptroller abdicated any responsibility for enforcing rule 67. Further correspondence was addressed to Comptroller Gidney, and on June 2, 1961, he wrote to ASTA and reaffirmed the September 15, 1958, letter.

On January 31, 1962, ASTA corresponded with Mr. Gidney's successor in the Comptroller's Office, James J. Saxon. ASTA renewed its contention that national banks were acting illegally in engaging in the travel agency business and emphasized the fact that national banks were engaging in the activity on an ever-increasing basis. On February 16, 1962, Mr. Saxon replied and stated that he was of the view that engaging in the travel agency business was " * * * a permissible and proper activity for national banking associations" and that "no restrictions should be placed upon the conduct of the travel agency business by national banks." A copy of ASTA's letter of January 31, 1962, and Mr. Saxon's reply of February 16, 1962, are attached.

The current policy laid down by the Comptroller of the Currency concerning national banks acting as travel agents is contained in ruling No. 7475 of the Comptroller of the Currency.¹ This ruling provides as follows:

"Incident to those powers vested in them under section 12 U.S.C. 24, national banks may provide travel services, including trip insurance, for their customers and receive compensation therefor. In connection therewith, national banks may advertise, develop, and extend such travel services *for the purpose of attracting customers to the bank.*" [Emphasis added.]

We have, therefore, seen in the last 6 years the sorry spectacle of the Office of the Comptroller of the Currency issuing three completely diverse and contradictory opinions on this important issue:

- (1) Banks have "no legal right" to operate a "regular travel agency."²
- (2) Banks should determine for themselves whether its travel agency activities are permissible.³
- (3) Banks may advertise, develop, and extend travel services and "no restrictions should be placed upon the conduct of the travel agency business by national banks."⁴

At the present time, as a result of the encouragement of the Comptroller of the Currency, there are 76 bank travel departments on the approved list of the Air Transport Association's roster of travel agencies in the United States. Approval by the Air Transport Association is a prerequisite to a travel agent selling airline tickets for profit in the United States. Approval by the International Air Transport Association is also required to represent international airlines. Steamship conferences as well as railroad associations have similar provisions for approving travel agents.

Once a bank travel department has been placed upon the approved list of the carrier conferences, it is then obligated under its sales agency agreements to actively promote and sell transportation. In other words, once bank travel departments are approved, they are required to directly compete with independent travel agents operating in the same locality.⁵

Bank travel departments thus bring to bear their full financial power and prestige in the community in direct and, we feel, unfair competition with local independent travel agents. We are concerned over the question of ethics where independent travel agents may be depositors of a bank having its own travel agency if that bank engages in the mailing of promotional material to all depositors, including clients of the independent travel agents. Similarly, we are concerned with the same question when the bank engages in newspaper and other advertising of its travel agency operation. In both of these instances, such a bank would be competing with its own depositors.

As spokesman for the travel agency industry in the United States, ASTA has consistently taken the position that a free enterprise system which encourages competition among those on equal footing is the most effective and desirable way of assuring a healthy industry. Because of this position, ASTA is opposed to banks engaging in the travel agency industry.

Banks have long been recognized as being akin to public utilities as institutions established by the Congress to serve certain specific legitimate purposes on behalf of our national welfare. The whole history of national legislation dating back to the National Currency Act of 1863 right through until the enactment of the Bank Service Corporation Act in October 1962 recognized that banks were granted a privileged status which gave them certain rights, immunities, and limitations in the public interest. As is the case with all rights extended to certain preferred elements of the economy, regulation is necessary to protect the public good. Even the most zealous proponent of banks and banking will admit that there is an outer limitation beyond which banks should not be permitted to go in their efforts to build and broaden their legitimate operations. In ASTA's opinion the conduct of a commercial travel agency is beyond the extremes of the legitimate operation of banks. This specific right to act as travel agents has not been granted to the national banks and while national banks are given miscellaneous incidental powers necessary to implement their express powers, by no stretch of the imagination can the conduct of a travel agency business be considered a matter which comes within the ambit of these incidental powers.

¹ Comptroller's Manual for National Banks.

² Rule 67, Comptroller of Currency.

³ Gidney letter of Sept. 15, 1958.

⁴ Saxon's letter of Feb. 16, 1962.

⁵ ASTA's letter of Jan. 31, 1962, p. 5.

Moreover, aside from the question of its power, a bank, by its very nature, is not a proper organization to engage in the travel agency business. A travel agency can be a creditor or a depositor of a bank or both and with it could find itself in competition. Also, a bank can have other clients to whom it can act as both creditor and travel agent. Such relationships can place the bank in what should be an unwanted position. The fiduciary nature of the banking business should preclude these kinds of situations. The public good is to be served by a sound and healthy transportation system which in turn depends to a large extent upon the sustained efforts of a solid travel agency industry. If banks are to be allowed to compete unfairly with independent travel agents, our industry will suffer extensive and perhaps irreparable harm.

At the present time there are nearly 5,000 independent travel agents throughout the country and they produce 25 percent of all domestic air travel, 75 percent of all international air travel, and more than 90 percent of steamship travel. Certainly if national banks continue their unfettered invasion into the totally unrelated field of operating travel agencies, the power and prestige of these banks is going to continue to erode the independent travel agency industry.

It is apparent from the ruling of the Comptroller of the Currency quoted above that in his zeal to allow national banks to utilize travel agencies as "lead items" to attract new customers that Federal legislation is necessary to protect the interests of the independent travel agent and indeed to assure his continued existence. It is also apparent that in view of the conflicting and contradictory positions taken by the Office of the Comptroller of the Currency that this issue can be resolved only by Federal legislation and cannot be allowed to depend upon the whim of the man who happens to be occupying that Office.

In conclusion, we request that the legislation which you have under consideration be expanded to include a strict prohibition of banks under Federal jurisdiction from operating travel agencies or travel departments. We appreciate the opportunity to submit these views and would welcome an invitation to appear before your subcommittee and present a more detailed and substantive statement in support of our position.

Sincerely yours,

IVAN BULLOT,
Executive Vice President.

WILKINSON, CRAGUN & BARKER LAW OFFICES,
Washington, D.C., January 31, 1962.

Re banks in the travel business.

HON. JAMES J. SAXON,
Comptroller of the Currency,
Washington, D.C.

DEAR MR. SAXON: This letter intends to summarize the more complete file which your office has on the matter of national banks engaging the commercial travel agency business. This matter was first brought to the attention of the Comptroller of the Currency in 1956 by the American Society of Travel Agents, Inc. (ASTA). In 1956, ASTA's concern was with the lack of enforcement of long-established rule 67 of the Comptroller of the Currency governing the activities of banks in relations to travel service. Rule 67 reads as follows:

"It is the position of this Office that a national bank has no legal right to act as an agent or representative of transportation companies in the operation of a regular travel agency, bureau, or service in the same manner as private travel agencies are operated as businesses for profit. However, if a bank does not hold itself out to the public as operating a travel agency, bureau, or service but merely undertakes to assist customers of the bank who wish to travel in obtaining reservations or accommodations, we believe such activity is within the power of a national bank as incidental to the fostering of goodwill by gratuitous public relations services."

It was the position of ASTA that the provisions of this rule were reasonable guidelines which—if observed—resolved a difficult relationship.

However, ASTA's 1956 brief followed by frequent visits, correspondence, and discussions with the Comptroller of the Currency finally resulted in a letter

from the Comptroller of the Currency to ASTA in 1958 which read in part as follows:

"* * * you [ASTA] take the position that they [the banks] may not participate in the carriers' conference system which establishes uniform rates of compensation, and uniform obligations to perform, on all participating travel agents.

"Whether national banks may so participate and whether they can or should enter into agreements in this connection would appear to be a matter to be determined by the banks concerned and their respective counsel, based upon the facts and circumstances of each particular case. As you know, some national banks have been doing so."

The contents of this letter were published by the Comptroller of the Currency in the Federal Register (24 F.R. 1900, Mar. 17, 1959). Since that time, the "rule" has been in effect that each bank shall determine for itself whether its activities in the travel agency business for which commissions are paid, are incidental to the specific powers granted by the National Banking Act.

This is still the policy even though the Comptroller was again asked in February 1961 to review this very confusing situation. Four months later, in June of 1961, the Comptroller wrote to ASTA, referred to the September 1958 letter, and added that "by tradition and custom this [financial and related services] has included services related to travel." The letter further pointed out that "providing travel services is not one which to this date has been the subject of any Federal legislation, nor is it so impressed with the public interest as to require the exclusion from it of anyone who wishes to engage in it."

These statements were both difficult to understand as well as, in some aspects, factually incorrect. Tradition and custom would have certainly dated back to the time of rule 67 when the Comptroller had a different policy concept in effect. Factually, the letter revealed a total ignorance of the very detailed and comprehensive body of regulation affecting directly the appointment, conduct, and detailed method of operation of travel agents, all of which must, in the case of air travel for example, be submitted and specifically approved by the Civil Aeronautics Board.

There exists a considerable body of rulemaking governing the public interest role and responsibilities of travel agents promulgated by Federal agencies, including the Interstate Commerce Commission and the Federal Maritime Commission, as well as the Civil Aeronautics Board. Not "anyone who wishes to engage in it" can do so; appointment of travel agents must meet financial and sales criteria and be approved by the carrier conferences which operate under statutory antitrust immunity for this purpose. To the contrary, only in the area of banks in the travel business is there no real direction and guidance from the Federal official concerned. As a result, ASTA is once again bringing this matter to the Comptroller since the role of banks is becoming increasingly intolerable.

ASTA is a national trade organization representing more than 1,500 travel agents operating more than 2,000 agency locations in the United States and Canada. It is estimated that more than 90 percent of all steamship travel, 75 percent of international air travel, and 25 percent of domestic air travel is handled through travel agency businesses in the United States. As indicated, travel agents must be professional men well versed in the complexities of both domestic and international commercial and pleasure travel.

It has become clear that the nature of a travel agent's activity is not understood. It is not mere "ticket taking." It involves affirmative action by the appointed agent (in this case, the bank) in order to receive commission payments; advertising, printing of tour folders, securing IT numbers (independent tour—these require specific carrier approval and listing), sales promotional efforts, escorted tours, fare construction—these are just a few of the obligations imposed on the successful travel agent.

Travel by domestic air carriers alone amounts to a \$2 billion a year industry and can be of even greater economic importance to our country in the future. Last year, President Kennedy, recognizing the vital role tourism can play, made a special recommendation to the Congress which resulted in the enactment of the U.S. Travel Service. This is a new Government agency of growing importance whose purposes include the encouragement of "two-way" travel to help redeem the dollar imbalance as well as promote international understanding. Certainly the public interest cannot be more adequately "demonstrated."

ASTA vigorously supported passage of this legislation. And it is in an effort to protect the interest of the traveling public, the transportation industry and the independent travel agent that ASTA once again addresses itself to the very serious problem of the increasing activity of a number of national banks in the professional travel agency business.

It is submitted that the present activity of those national banks aggressively engaged in the travel business is unwarranted and improper. As pointed out in our February 1961 letter, it is evident that national banks have those incidental powers necessary to implement their express powers. It is equally evident that those powers not specifically granted by Congress are denied. The specific right to act as a travel agent has not been so granted.

It has perhaps not been made clear (particularly in view of the June 1961 letter stating "anyone" can do it) that the conduct of a professional travel agency business is not a simple "incidental service" which a bank can easily provide. There is a well understood, albeit not always defined, test of a national bank's public interest and financial role in a community. The cited case decisions in our February 1961 letter inevitably turn on this role. We maintain that using this criteria, there is obvious incompatibility between a bank and the proper conduct of a professional travel agency. An institution cannot effectively operate as a national bank and act as a travel agency at the same time. A national bank, by its very nature, is in a fiduciary relationship, a bank must confine its activities to dealing in a fair objective and efficient manner with the funds entrusted to it by its depositors and at all times function with the welfare of its depositors in mind. Just as a bank cannot operate an insurance or brokerage business, neither can it engage in the aggressive, competitive and even speculative tourist agency business.

We would like to further illustrate the nature of a travel agent's business. A travel agent undertakes a contractual obligation by virtue of its agency appointment by the Air Traffic Conference and is certified to affirmatively do the following:

(a) * * * Represent the carrier for the purpose of promoting and selling air passenger transportation.

(b) * * * Furnish information to its clients and to the public concerning the carrier's air passenger transportation services in conformance with current authorized forms, folders, advertising, schedules, tariffs, rules, regulations, and instructions issued by the carrier.

(c) The agent shall make known the services of the carrier in every reasonable way practical. * * *

(d) The agent shall endeavor to create and stimulate the sale of air passenger transportation offered by the carrier to perform and to provide adequate service to the agent's clients and to transact a sufficient amount of business to justify the costs and responsibilities incurred by the carrier in retaining the agency.¹

Similar obligations are imposed by carrier conferences in other areas of transportation.

From the foregoing, it becomes apparent that the obligations and scope of activity of a national bank conflict with the obligations and scope of activity of a professional travel agency to such an extent as to be incompatible in a single institution.

It has also become obvious that in operating a travel agency through a bank location a bank can use its depositors' funds and the prestige incident to a banking institution to the detriment of independent travel agents.

It is further obvious that a travel agency can be a creditor or a depositor of a bank or both, and with whom it can find itself in competition. Also, a bank can have other clients where it can act as both creditor and travel agent. Such relationships can place the bank in what should be an unwanted position. We have had examples of this unfair competitive position given us. The fiduciary nature of the banking business should preclude these kinds of situations.

¹ Extracts from ATC sales agency agreement.

In conclusion, it is respectfully requested that the present interpretation of this question be again reviewed and a new study, if necessary, be made to more clearly define and limit the activities of banks in the travel agency business.

At your convenience, we would appreciate the opportunity of meeting with you to discuss this matter. The Board of Directors of ASTA will be meeting here in Washington from February 13 through the 15th and if at all possible, several of the officers would like to meet with you during this time.

Sincerely yours,

WILKINSON, CRAGUN & BARKER,
Attorneys for the American Society of Travel Agents, Inc.
ROCCO C. SICILIANO.

TREASURY DEPARTMENT,
COMPTROLLER OF THE CURRENCY,
Washington, February 16, 1962.

ROCCO C. SICILIANO, Esq.,
WILKINSON, CRAGUN & BARKER,
Washington, D.C.

DEAR MR. SICILIANO: Reference is made to your letter of January 31, 1962, and your visit to this office on February 13, 1962, concerning activities of national banks in the commercial travel agency business.

As you have been advised, it is our view that this is a permissible and proper activity for national banking associations. Moreover, we are satisfied that no restrictions of the type sought by you should be placed upon the conduct of the travel agency business by national banks.

Sincerely yours,

JAMES J. SAXON,
Comptroller of the Currency.

STATEMENT SUBMITTED BY THE NATIONAL AUTOMOBILE DEALERS ASSOCIATION IN
SUPPORT OF H.R. 9822

The National Automobile Dealers Association is comprised of approximately 21,000 enfranchised retail merchants, engaged in selling and servicing new and used automobiles and trucks of all makes, domestic and imported. Its membership extends into every State of the United States.

Over the past two decades there has been a growing recognition on the part of NADA members that the automobile and truck merchant today must be more than just an automobile and truck dealer. He must be a transportation merchant. He must be concerned with every facet of transportation involving the use of his primary products, the automobile and truck. As a result, a large number of the Nation's dealers are now engaged in the business of leasing and renting of automobiles and trucks.

Therefore, the NADA and its members view with grave concern the March 18, 1963, ruling of the Comptroller of the Currency that the leasing by a national bank " * * * of personal property acquired upon the specific request of and for the use of its customer, and the incurring of such additional obligations as may be incident to becoming an owner of personal property and the lessor thereof, is a lawful exercise of the powers of a national bank and necessary to the business of banking."

The NADA and its members submit that the March 18 ruling of the Comptroller is without the purview of the National Bank Act and constitutes a radical departure from long-established public policy that banks may not engage in business other than the business of banking.

As depositories of public funds, banks are charged, above all, with the duty of safeguarding the funds entrusted to them. Accordingly, the public interest with which banking is vested was recognized by the Congress when it enacted the National Bank Act and defined the powers of national banks, as follows:

"To exercise by its board of directors or duly authorized officers or agents, subject to law, all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits, by buying and selling exchange, coin, and bullion; by loaning money on personal security; and by obtaining, issuing, and circulating notes according to the provisions of this title." [12 U.S.C. 24, clause 7.]

Over the years since its enactment, this clause has been universally and uniformly interpreted by the courts to mean that national banks have no power to engage in business or commercial activities beyond that necessary to save them from loss. In addition, all prior Comptrollers of the Currency have ruled consistently that national banks are prohibited under the National Bank Act from acquiring and owning assets for the sole purpose of leasing them to others.

Direct leasing of automobiles and trucks is a highly specialized, competitive business activity of a type prohibited by the National Bank Act, as interpreted by the courts. It involves the sale of the use of motor vehicles, the acquisition of such motor vehicles to be leased, and the sale of such vehicles at the conclusion of the lease period. It requires highly specialized and knowledgeable leasing personnel, involves legal and tax complexities and aggressive advertising and merchandising. The legal complexities are magnified because of the mobility of motor vehicles and the lessor must at all times be certain that he is meeting all of the obligations of a motor vehicle owner in all of the States in which the vehicle he leases may operate. It also involves the question of whether or not the lessor must qualify to do business in all of the States in which the vehicles he leases may operate.

To automobile and truck dealers, leasing is a means of rendering a real transportation service to a dealership's customers, leading to repeat customers and increased market penetration for the dealership and its make of car. From the dealers' standpoint, the only difference between the retail automobile and truck sales business and leasing is time. On the retail sales side, when the automobile or truck is sold, or a repair job is performed, the dealer knows the results of the transaction almost immediately. In leasing, the real results are not evident until the end of the lease term and the sale of the used vehicle. This is so because much of the profit from lease operations is in the marketing of the used unit which must be sold at the right time even if it means giving the lessee another vehicle for the balance of the term of the lease.

Thus, direct leasing of automobiles and trucks is a commercial activity beyond the scope of banking as such is defined by the National Bank Act.

Aside from the legality of the Comptroller's ruling, the NADA and its members feel that the entrance of national banks into the area of direct leasing of automobiles and trucks, pursuant to the Comptroller's ruling, would constitute unfair competition. The commodity or stock in trade of a bank is money. The automobile or truck dealer "buys" money at the going market price. The bank generally is a "seller" of money. The cost of money differential between the bank and the dealer would unquestionably be to the detriment of the dealer.

Therefore, the Comptroller's ruling that banks may engage in direct leasing raises questions of equity and justice and the right to compete on equal terms under the law. The concept of equality of opportunity is a cornerstone of our society and the profit motive is the very foundation of the economy on which our society is sustained. Certainly there can be no equality of competitive opportunity when a bank can use the vast public funds at its resource in direct competition with local merchants in everyday commercial activities. In addition, all national banks are automatically covered by FDIC insurance which was never conceived as a measure to shelter unlawful and inappropriate banking practices and protect bank depositors from losses resulting from the banks engaging in speculative and commercial activities.

Furthermore, smaller banks which lack the experience and trained personnel necessary to qualify them to engage in direct leasing might well be tempted to enter this speculative field to their detriment and to the detriment of their depositors. In addition, the engaging in the business of direct leasing requires huge amounts of money which most small banks would not have available and this could only tend toward undue concentration of economic power on a few large banks.

In view of the foregoing, it is submitted that the Comptroller's ruling is not requisite to the public need nor is it in the public interest. If the Comptroller can by administrative fiat distort the intent of the National Bank Act and ignore completely the courts' interpretations of that act by permitting national banks to engage in direct leasing, it can only open the door to abuses of the type Congress has wisely legislated against.

For the reasons stated above, the National Automobile Dealers Association and its members heartily endorse and strongly urge the prompt enactment of H.R. 9822, which would nullify the Comptroller's illegal ruling and prohibit national banks from engaging in the business of direct leasing of personal property.

Mr. MULTER. Our first witness is Congressman Halpern, who has asked to be heard. He was to be the first witness, but since he is not present at this time, we will go on to the next witness. Do any of you gentlemen desire to make a statement?

Mr. MOORHEAD. No.

Mr. LLOYD. No.

Mr. MULTER. Our first witness will be Mr. Browning.

Will you come forward, please?

Mr. LLOYD. I do not see Mr. Browning in the room. However, he is in the city. I assume that he is having a little problem of finding this room. He does have a statement. I am sure that he will be in in a minute. If we could pass him over for the moment, I would appreciate it.

Mr. MULTER. We will pass him for the moment. The next witness is Mr. Guy S. Balser. Will you come forward, please, sir? You may proceed. Introduce yourself for the record and tell us who you are and whom you represent, also introduce the gentlemen who are with you. You can proceed to either read your statement in full or to make your full statement a part of the record and to summarize it.

STATEMENT OF GUY S. BALSER, CHAIRMAN, COMMITTEE ON BANK RELATIONS; ACCOMPANIED BY MARTIN J. KAUFMAN, VICE CHAIRMAN, COMMITTEE ON BANK RELATIONS, AND STANLEY H. STEARMAN, STAFF COUNSEL, NATIONAL SOCIETY OF PUBLIC ACCOUNTANTS

Mr. BALSER. Thank you, Mr. Chairman and gentlemen of the subcommittee. My name is Guy S. Balser. I am a licensed public accountant in California and senior partner in the public accounting firm of Balser, Abrams & Horowitz, with offices in Long Beach. I have been engaged in the practice of public accountancy in California since 1937. I am a graduate of the Baltimore City College and completed several special accounting courses at Johns Hopkins University. I am admitted to practice before the U.S. Treasury Department.

I am appearing before you today as a representative of the National Society of Public Accountants in the capacity of chairman of our committee on bank relations. I have been associated with the national society since 1947 and have served in various capacities. I have been a State director from California, a member of the board of governors, second vice president, first vice president, and this past August I completed a term as president. In addition I have been a member of the committee on bank relations since its inception several years ago.

Accompanying me here today are Martin J. Kaufman of Pawtucket, R.I., vice chairman of our committee on bank relations, and Stanley H. Stearman, staff counsel for the national society.

The members of our organization are quite concerned over the increasing numbers of banks throughout the country which are advertising and providing accounting, bookkeeping, income tax, and related business services to individuals and firms of all types and sizes. We believe that these recent developments in the banking field will have adverse consequences for the public, the business community, and the public accounting profession.

It is for this reason that we strongly support H.R. 9548 which would prohibit banks from providing accounting, bookkeeping, or related business services to their clients beyond that necessarily incident to normal banking services.

We concur completely with the views expressed by the subcommittee chairman that not only are these activities outside of the realm of normal banking functions, but they also constitute a serious encroachment into the area of those individuals who are professionally trained and equipped to perform these services for the business community.

We believe that legislation should be enacted to return banks to their proper functions and out of the accounting field. Passage of H.R. 9548 will accomplish this objective.

We are submitting a detailed statement of our position for the record. Rather than read the entire 13-page statement I will, with your permission, summarize the contents and will be pleased to answer any questions.

We certainly can understand the need for banks today to invest in data processing equipment in order to keep abreast of changing conditions in the business world, and to render much more efficient service to customers. As advisers to our clients, we also recommend the use of modern equipment and procedures in their business. A great many of the accounting firms use data processing equipment for their own use as well as for their clients' use. We do, however, object to a bank utilizing this equipment to offer accounting and related services to the business community.

In order to understand this problem, let me explain what a public accountant is and does. He is skilled in the knowledge, science, and practice of accounting. His training, education, and experience enable him to offer financial analysis and management services to his client. He no longer is the old-fashioned fraud detector, as we have always known the public accountant or used to know him. Today he offers and operates as a business consultant; he analyzes the operation of a business; he determines areas of deficiency or improper functioning; and he counsels with his client in long-range planning.

The so-called accounting business services offered by the banks are, we understand, performed by technicians who operate automated equipment, so that the only real service offered by banks in this field is a pure recording function. Certainly, the technician is not qualified to render service and counsel. It is very questionable whether responsible bank officers can afford the time to analyze each of these statements that come in. So, therefore, there is a danger that the businessman can be lulled into the belief that he is getting a complete accounting service from the bank, where he is not. We can cite cases of incorrect and incomplete information furnished to the computer, either as an error on the part of the client or on the part of the computer operator, with ridiculous answers coming out. And these ridiculous answers are being undetected because of the unfamiliarity of the operator with the accounting functions.

There is a possibility, also, which is quite a problem, that banks could exert certain pressures on prospective borrowers to use the bank's accounting service as a condition of a loan; in fact, we have already had reports from some of our members that this has happened. Competition among the banks seems to be increasing. We know and have

evidence that banks in some cases are offering free accounting service to their clients.

What would be the effect on the accounting profession? The accountant is subject to codes of ethics and rules of professional conduct, either imposed by State law or by a professional society. These restrictions are necessary to protect the public interest.

The accountant is an independent practitioner; and, therefore, can give unbiased judgment. Advertising is prohibited to the accountant nor can he solicit clients. This, also, is a protection to the public.

There is no restriction on the bank, however. It can advertise freely and intensely for business services. And as we can show you, in some instances blatantly. Our files are complete with evidence. We have many advertisements and brochures that are put out by the banks, and we have several here which we would like to enter into the record.

We have an advertisement here from the Citizens Bank & Trust Co. of Park Ridge, Ill., which is a suburb of Chicago. This is a large bank. Just to quote briefly it states:

No doubt you've enjoyed a long and friendly relationship with your bank. But what has your bank done for you lately? For instance in the face of rising overhead, will your bank pick up your payroll, process it on high-speed computers and deliver the completed work back to you—at no charge?

Will your bank, at no charge, tackle your inventory control problems, advise you when to purchase new materials?

Will your bank, at no charge, make an electronic analysis of your market, measure its potential, dictate selling strategy?

Will your bank do more than just perform the everyday loan and checking services dictated and limited by banking tradition?

Ask your banker. After he explains why he can't phone Edward Reilly, president of Citizens Bank & Trust Co. He'll offer your company free rein of \$7 million worth of the newest and most advanced computer equipment and will agree to meet with you personally, in your plant if you desire. He will discuss the numerous ways this equipment and Citizen's experience can most profitably be utilized in your particular operation—at no charge.

In other words, here is the president of a large bank with \$7 million worth of equipment who offers to give free advice by himself and free service. How can they do it?

We, also, have a quotation here from Banking magazine, the official magazine of the American Bankers Association which starts out in the opening paragraph:

These services provided by commercial bankers have embraced nearly everything from supplying investment counsel to disposing of circus elephants pledged as collateral. However, there is one field of possible profitmaking, and a broad one at that, from which bankers have traditionally abstained. That is the business of rendering income tax record services on a broad scale.

We have next an article from the Providence Journal on the Industrial National Bank of Rhode Island which is offering as a major promotion, with a high-ranking bank officer, to sell services to fill up time of its processing equipment not used by the bank.

We know that in the normal course of events this computer service is for the bank itself, that is, the service is done at night. That is outside the bank's regular hours. So, therefore, the bank, after using equipment for 8 or 10 hours a day for its own purpose, is now trying to put computers on a 24-hour service basis. We can understand when overtime is necessary to keep up with the regular functions of a bank's business, but we cannot understand why the bank has to go out

and make work to keep the computers busy 24 hours a day on a three-shift basis.

The independent accountant cannot hope to meet such competition, unless he renders inferior service, and this we refuse to do. The businessman should not be forced to accept inferior service because of unfair competition.

The accountant accepts the responsibility for his work, but who will accept the responsibility for the accuracy of the bank's work?

In this same article from Banking magazine, there is a statement that says since the customer assumes responsibility for encoding each transaction, if there is a mistake there is no legal liability on the bank.

The accountant, in rendering this same service, reviews all of these items after they come off of the computer, and will find obvious errors. If he fails to find them, he is legally liable.

We believe that the provisions of the Bank Service Corporation Act, which was enacted in 1962, should be applied here. Section 4 of that act declares that no bank service corporation may engage in any activity other than the performance of bank services for banks. We believe that this same provision should apply in the case of banks, as well as bank service corporations.

We do not believe that accounting, bookkeeping, income tax or other business service falls within the province of banks. We feel that the custodians of the funds of depositors, the banks, should devote the full time of their officers to the bank's clients. We believe that business firms will suffer from the so-called revolution in banking service which we are facing today where banks are all things to business and are entering into the field of insurance, travel agencies, messenger service, equipment leasing, real estate brokers, collection agencies and, of course, public accounting. We believe that the time is now appropriate for Congress to investigate this situation vigorously and thoroughly and to take steps necessary to protect the public and, yes, even the banks themselves. We believe that this problem can be solved by the passage of H.R. 9548.

On behalf of the National Society of Public Accountants, Mr. Chairman, we extend our appreciation for the opportunity to appear before this subcommittee and hope that our comments may prove of some value in your deliberations.

Mr. MULTER. Thank you, Mr. Balser. Your complete statement will be made a part of the record, together with the exhibits.

(The prepared statement of Guy S. Balser, the two advertisements from the Citizens Bank & Trust Co., the article from Banking magazine entitled "A New Service—With 100 Million Customers," the article entitled "Special Services at Proctor," the article entitled "Income Tax Service," and the newspaper ad from the Wall Street Journal of Tuesday, October 1, 1963, follow:)

TESTIMONY OF NATIONAL SOCIETY OF PUBLIC ACCOUNTANTS,
WASHINGTON, D.C.

My name is Guy S. Balser. I am a licensed public accountant in California and senior partner in the public accounting firm of Balser, Abrams & Horowitz, with offices in Long Beach. I have been engaged in the practice of public accountancy in California since 1937. I am a graduate of the Baltimore City College and completed several

special accounting courses at Johns Hopkins University. I am admitted to practice before the U.S. Treasury Department.

I am appearing before you today as a representative of the National Society of Public Accountants in the capacity of chairman of our committee on bank relations. I have been associated with the national society since 1947 and have served in various capacities. I have been a State director from California, a member of the board of governors, second vice president, first vice president, and this past August, I completed a term as president. In addition I have been a member of the committee on bank relations since its inception several years ago.

Accompanying me here today are Martin J. Kaufman of Pawtucket, R.I., vice chairman of our committee on bank relations, and Stanley H. Stearman, staff counsel for the national society.

The National Society of Public Accountants is a nonprofit individual membership organization which was formed in 1945. Our more than 11,000 members are engaged in the public practice of accountancy in all States, the District of Columbia, and several territories. According to our constitution and bylaws, the national society is dedicated to elevating and maintaining among its members high standards of professional competence and integrity. We are constantly at work promoting good will and understanding between the general public and the public accounting profession throughout the United States.

The members of our organization are quite concerned over the increasing numbers of banks throughout the country which are advertising and providing accounting, bookkeeping, income tax and related business services to individuals and firms of all types and sizes. We believe that these recent developments in the banking field will have adverse consequences for the public, the business community, and the public accounting profession.

It is for this reason that we strongly support H.R. 9548 which would prohibit banks from providing accounting, bookkeeping, or related business services to their clients beyond that necessarily incident to normal banking services.

We concur completely with the views expressed by the subcommittee chairman that not only are these activities outside of the realm of normal banking functions, but they also constitute a serious encroachment into the area of those individuals who are professionally trained and equipped to perform these services for the business community.

We believe that legislation should be enacted to return banks to their proper functions and out of the accounting field. Passage of H.R. 9548 will accomplish this objective.

Banks have begun to offer accounting, bookkeeping, and related services because of rather extensive investments in data processing and other automated recordkeeping equipment. This equipment is being acquired to enable individual banks to render more modern and efficient banking services to their customers. However, from all indications it would appear that the banks have found a sleeping giant in this automated equipment, because it is being utilized by more and more banks to provide a type of service to the business community which is rather far removed from the traditional concept of banking.

Today we see numerous brochures, pamphlets, advertisements, booklets, and custom-made proposals describing the fact that banks are now

in a position to offer a wide range of accounting and bookkeeping services. These activities include, but by no means are limited to: payroll services, account reconciliation, cost accounting, billing, sales reports, inventory control, and the preparation and filing of various tax returns. These services, which the banks have generally described as "business services" to distinguish them from the traditional banking functions, are the same type of services which have been and are being competently performed for the public by independent practicing accountants.

Our files are replete with documentary material which clearly indicates the extent to which banks have moved into the "business service" field. This material takes various forms, and it is published by banks large and small, urban and rural.

One brochure in particular makes the following bid for new "business service" clients:

No doubt you've enjoyed a long and friendly relationship with your bank. But what has your bank done for you lately? For instance, in the face of rising overhead, will your bank pick up your payroll, process it on high-speed computers and deliver the completed work back to you—at no charge? Will your bank, at no charge, make an electronic analysis of your market, measure its potential, dictate selling strategy? Will your bank do more than just perform the everyday loan and checking services dictated and limited by banking tradition.

An article in a recent issue of Banking magazine offers this profitable possibility:

The services provided by commercial bankers have embraced nearly everything from supplying investment counsel to disposing of circus elephants pledged as collateral. However, there is one field of possible profitmaking, and a broad one at that, from which bankers have traditionally abstained. That is the business of rendering income tax record services on a broad scale.

Just the other day an article in Rhode Island's Providence Journal reported that the Industrial National Bank has launched a major promotional effort to sell automated accounting services to fill up time at its big electronic data processing center not used by the bank. The article added that the bank will make available to its customers accounting functions that can be performed on a mutually advantageous basis.

To our way of thinking, the so-called new business services are nothing more than services which are and should be within the realm of the independent professional accountant. If the present trend is permitted to continue without abatement or control, and if banks are given a free rein to offer more and more variations of "business services," we foresee serious repercussions for the business public.

In order to properly understand why bank services in the accounting field will not be in the best interests of the business community, it is important to describe the public accountant and the services he renders.

A public accountant is one who is skilled in the knowledge, science, and practice of accounting. His education, training and experience are all directed to enable him to offer financial analysis and advice to his client. The public accountant performs services for individuals, businesses, and governmental agencies and is thus available to a variety of clients and under varying circumstances.

Moreover, the public accountant is independent. His independence denotes the absence of self-interest or bias in forming judgments.

He, therefore, can bring complete objectivity and integrity to the performance of his professional services.

Finally, the modern public accountant, unlike his "fraud detector" image of the past, is often described as a "business doctor" in the sense that he can investigate and analyze a business operation, determine areas which are deficient or improperly functioning, and make constructive suggestions and recommendations for improvement.

It is clear then that the independent public accountant can bring to each assignment professional skills which include objectivity, an analytical mind, and professional judgment.

Unfortunately, there is every indication that "business services" being offered by banks are handled by the technicians who operate automated processing equipment rather than professionally qualified accountants. This means that in actual practice the only real services that banks are offering are pure recording functions, generally without any attempt to advise or counsel the client as to the meaning or significance of the figures presented to him by the machines.

This could lead the individual businessman to believe that he is obtaining adequate professional-level accounting services, whereas he would really be missing the analysis, judgment, and advice which the independent professional accountant can offer. In other words, there is a danger that the typical businessman may be lulled into feeling that his accounting is being well taken care of by the bank, when in reality such might not be the case at all.

Within the past several years more and more of our members have turned to the use of automatic data processing equipment in their own accounting practices. They are doing this in order to be able to provide a better service to clients who are being faced with an increasing demand for more detailed and extensive accounting records. Through the use of machine accounting, our members are able to provide their clients with detailed information which would not otherwise be so readily available.

But the important point to bear in mind is that independent accountants are able to follow up automated machine accounting with professional evaluation and analysis of the client's financial condition.

The National Society of Public Accountants and its members have constantly tried to impress upon the business public that while a good recordkeeping system is vital to business health, records in and of themselves are valueless unless they can be properly analyzed to determine where the company has been, where it is now, and where it is likely to be heading. Unless the average businessman can obtain a proper evaluation of the message contained in his records, his needs will hardly be served. All of the records in the world will do him no good unless he can rely with confidence on a professionally trained accountant to tell him what the records mean.

The importance of financial statement analysis and evaluation is pointed up by the fact that most firms of reasonable size have their own accounting departments and professional controllers. These key staff personnel are able to provide their employer organization with professional counseling and advice. The smaller firms, on the other hand, which cannot afford or justify professional accounting staff personnel, turn to the independent public accountant for this indispensable service.

There is another possible condition which is likely to exist and which definitely is not in the best interests of the business community. That is, that the temptation will be quite strong for some banks to take the position, subtle as it might be, that the availability of loan funds will be predicated on, or at least influenced by, the bank's being able to provide accounting and bookkeeping services to the prospective borrower.

For example, if a bank is anxious to obtain new customers for its "business services," and many of them seem to be, it is not inconceivable that undue pressure could be exerted upon a prospective borrower in order to persuade the borrower to become a client for the bank's accounting, bookkeeping, or tax services. In essence, a bank could say to a prospective borrower: "Since we know what financial information we want and how we want it presented, let us keep your accounting and bookkeeping records. Otherwise, there may be a serious question as to our granting you a loan under any other arrangement."

Or, depending on the competitive situation among banks, a bank could, as some already have, advise borrowers that if the borrower utilizes the bank's "business services" he will be able to get his accounting and recordkeeping work done without charge. In the final analysis, is anything really free today?

As members of an honored profession, public accountants are subject to various rules and codes of professional conduct. Such an arrangement obviously operates to protect the public interest.

For example, independent accountants who are licensed under State law are subjected to discipline and control by proper State authorities in the course of their performing professional accounting services. Moreover, their professional society insists that they adhere to rigid rules of professional conduct during the course of their practice. One of these rules is the prohibition against soliciting clients or advertising. Such a rule is designed not to unduly restrict the profession, but to protect the public. Banks, on the other hand, are subject to no similar requirements and, accordingly, are advertising and promoting "business services" in a very intense and dedicated fashion.

Since banks are anxious to maintain their new data processing equipment at maximum operating capacity, the typical situation finds them providing accounting and bookkeeping services to customers during periods when the machines are not being used for normal bank needs. Consequently, since automated "business services" take up "slack time," banks are in a position to offer these services at extremely nominal rates and in some instances on a free basis.

Obviously, the independent public accountant cannot possibly hope to meet competition of this type. The members of the national society, as an example, have a considerable investment in education, practical experience, and office equipment and supplies and it is necessary for them to earn a fair return on this investment in order to remain in practice. Any development which unfairly competes with public accountants and prevents them from earning fees commensurate with their services, will result over the long run in a reduction in the number of independent practitioners engaged in performing accounting services for the public. If we are to meet the needs of our country's expanding and dynamic economy, we will require all of the public

accountants we can get. The interests of the public will not be served if there are insufficient numbers of qualified independent practicing public accountants.

Two actual situations reported to us by our members will serve to emphasize this important consideration. One of our members in California had a client of long standing who was on a monthly retainer. The client's stock was purchased by another corporation which agreed to retain the services of our member on the same basis as previously and for the same fee. A short time later, however, the new owners put the client under a bank's automated payroll plan. As a result, there was a serious reduction in the services required from our member and he was subsequently dropped as their independent accountant.

A member in Georgia reported that a former client returned and requested him to prepare a tax return. He asked why the former client did not use his present accountants for this service. The client replied that his bank had approached him about a month or two previously and solicited his accounting business. After first finding out what the accounting firm had charged, the bank agreed to make monthly statements for the same amount. However, the deciding factor was the bank's suggestion that the proposed arrangement would facilitate the bank's consideration of the client's needs for funds from time to time on the theory that the bank would have a continuous picture of his business and would know enough of his affairs to warrant an extension of credit. On this basis the former client switched to the bank, apparently under the impression that such an arrangement would strengthen his credit position. Naturally, he assumed that he would get the same quality of services previously received from his regular accountants.

It seems, however, that the bank would not make out a tax return and that was the reason why the former client approached our member. Needless to say, our member sent him back to the bank.

We seriously question whether banks should be permitted to engage so extensively in services and activities which long have been within the province of the individual practicing accountant and which, for many reasons, should remain so.

We certainly can understand the need for banks today to invest in data processing equipment in order to keep abreast of changing conditions in the business world. However, we see no justification for banks using this same equipment to offer accounting and related business services to the business community.

We believe that Congress should impose the same restrictions on all banks as have been imposed on bank service corporations under Public Law 87-856.

The statute provides in section 4 that "no bank service corporation may engage in any activity other than performance of bank services for banks." If Congress in its wisdom has recognized the need for bank service corporations to be confined in their activities to servicing banks and banks only, should not similar restrictions be applicable to the banks themselves?

During debate in the Senate on the legislation which has since become Public Law 87-856, Senator William Proxmire of Wisconsin proposed amending language to confine bank service corporations ex-

clusively to servicing themselves and other banks. Senator Proxmire observed that with the adoption of his amendment "we are in a position to have a bill that provides what the banks really want, and what the members of the committee feel is justified, and at the same time safeguard legitimate business enterprises which otherwise might be put out of business." We believe the Senator's reasoning to be absolutely correct and applicable as well to banks themselves.

We do not believe that accounting, bookkeeping, income tax services, and other business services fall within the province of banks under the traditional concept of banking as it has developed over the years in this country.

We do not believe that banks should be allowed to continue to offer accounting, bookkeeping, and similar services.

We believe that business firms will suffer if what has been described as the "revolution" in banking services leads the banks of the future, as Sylvia Porter says, "to become all purpose cradle-to-grave bookkeepers—receiving our income, paying our bills, allocating funds to various members of the family, earmarking money for special occasions, and managing the savings nest egg."

We do not believe that the best interests of individual customers, business firms, the public accounting profession and probably even the banks themselves will be protected if this trend continues.

We believe the time is now appropriate for Congress to completely, thoroughly, and vigorously investigate this entire matter, and take whatever action may be necessary to place reasonable restrictions on expanding bank services which are not in the best interests of the public and the business community and which definitely encroach into the field of the independent practicing accountants of our country.

We believe the problem can be solved through enactment of H.R. 9548. We urge your favorable consideration.

On behalf of the National Society of Public Accountants, may I extend our appreciation for the opportunity of appearing before this subcommittee. We hope that our comments and suggestions will assist you in your important studies and deliberations.

[Article from Providence Journal, Feb. 13, 1964]

INDUSTRIAL BANK TO RETAIL ELECTRONIC DATA SERVICES

Industrial National Bank of Rhode Island yesterday launched a major promotional effort to sell automated accounting services to fill up time not used by the bank at its big electronic data processing center in Glocester.

John Simmen, the bank's president, said the move to retail electronic data processing services is in line with policies adopted by many other banks faced with the need to keep expensive data processing equipment on nearly full time operation in an effort to overcome the profit squeeze created by rising costs.

He disclosed that Donald E. Bossi, former finance and banking representative with International Business Machines Corp., has been elected an assistant vice president of the bank and will handle the sales promotional activities.

Mr. Bossi will be charged with the task of making available to bank customers accounting functions that can be performed on a mutually advantageous basis, Mr. Simmen said. After a period of orientation, the bank president disclosed, Mr. Bossi will also sell other bank services, many of which will become available for the first time locally.

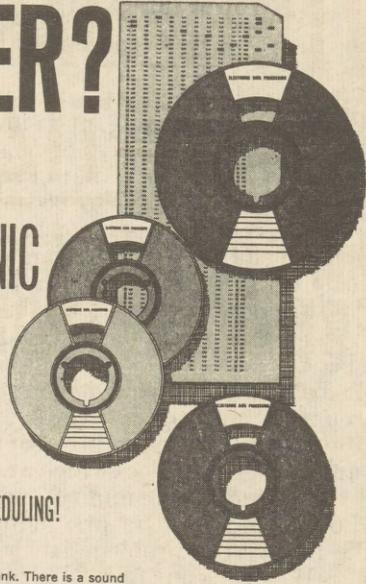
A Barrington resident, Mr. Bossi completed his formal training with IBM in 1957 and was made a senior applied scientist and assigned to the company's Providence office in that year as a computer technical specialist. In 1960 he became IBM's finance and banking representative for Rhode Island and southern Massachusetts. He is a 1952 graduate of Boston University.

[From the Wall Street Journal, Oct. 1, 1962]

WHY BUY OR LEASE A COMPUTER?

OUR \$90,000,000 BANK
WILL DO YOUR ELECTRONIC
DATA PROCESSING

FREE! *PAYROLL!
INVENTORY CONTROL!
SALES ANALYSIS!
BILLING! STUDENT SCHEDULING!



An exceptional offer? Sure it is—especially when made by a major bank. There is a sound business reason behind it, however. Even our experts couldn't keep our computer center's RCA 501, two RCA 301's, NCR 310, IBM 1401 and associated unit record equipment busy enough, so we decided to offer complete electronic data process services to industry.

Look what our pioneering means to industry: Four years ago we developed for a \$220,000,000.00 insurance company, Bankers Life and Casualty, electronic payroll handling—the first in Chicago. Ever since then we've been paying their 2800 employees with our computers . . . Savings? \$19,000.00 per year.

Another example—Just recently a small manufacturer, O'Brien Manufacturing Company, makers of sewer and pipeline cleaning equipment, contacted us with an inventory control problem. Our experts developed a program that solved their problem. Estimated Savings—\$10,000.00 per year.

Even large corporations, like Transo Envelope Co., whose computers were busy, have come to us for computer services rather than pay a service bureau. Reason—BECAUSE WE PERFORM THIS SERVICE FREE.

We now have 27 Chicago area corporations who use our computer services. We would like to offer these exceptional services to 73 more Chicago area companies. First come—first served. To find out how these services would apply to your business—phone, write or wire our President, Edward Reilly, TA 3-1155.

**All Services herein are available to our regular commercial depositors at no charge.*



**CITIZENS BANK
& TRUST COMPANY**

NORTHWEST HIGHWAY AT TOUHY • PARK RIDGE, ILLINOIS
Telephones: TA1cott 3-1155 • NEwcastle 1-4270

*an exceptional
offer from an
exceptional bank!*

MEMBER FEDERAL DEPOSIT INSURANCE CORP.

[From the Wall Street Journal, Oct. 8, 1962]

MOST BANKS CAN'T! OTHER BANKS WON'T! NOW CITIZENS WILL!

**Only Citizens Bank & Trust Company offers
FREE* ELECTRONIC PROCESSING**
*of Payrolls, Inventory Control, Billing, Sales and
Marketing Analysis, Statistical Computing of All Types!*

No doubt you've enjoyed a long and friendly relationship with your bank. But what has your bank done for you lately? For instance, in the face of rising overhead, will your bank pick up your payroll, process it on high-speed computers and deliver the completed work back to you—at no charge?

Will your bank, *at no charge*, tackle your inventory control problems, advise you when to purchase new materials?

Will your bank, *at no charge*, make an electronic analysis of your market, measure its potential, dictate selling strategy?

*All services herein are available to our regular commercial depositors at no charge.

Will your bank do more than just perform the everyday loan and checking services dictated and limited by banking tradition?

Ask your banker. After he explains why he can't, phone Edward Reilly, president of Citizens Bank & Trust Company. He'll offer your company free rein of \$7 million worth of the newest and most advanced computer equipment and will agree to meet with you personally, in your plant if you desire. He will discuss the numerous ways this equipment and Citizen's experience can most profitably be utilized in your particular operation—at no charge!

*an exceptional offer
from an exceptional bank!*



[From Banking magazine]

A NEW SERVICE—WITH 100 MILLION CUSTOMERS

(Paul E. Hanchett¹)

The services provided by commercial bankers have embraced nearly everything from supplying investment counsel to disposing of circus elephants pledged as collateral. However, there is one field of possible profitmaking, and a broad one at that, from which bankers have traditionally abstained. That is the business of rendering income tax record services on a broad scale.

Although the largest single money payments operation in the world—the U.S. personal income tax—involves a captive and growing market of nearly 100 million customers, the servicing of this never-ending stream has been largely assigned to lawyers, accountants, and bookkeepers. Banks have neglected it partly because of a mistaken identification of “accounting” with “bookkeeping,” and partly because of a desire to retain the good will of the accounting profession.

It has also stemmed, in part, from the low-profit yield of trust departments that have been forced into performing tax and accounting services of a high-cost, nonstandardized nature. And certainly a big factor in keeping bankers out of the income tax field has been the genuine apprehension that it could expose them to formidable lawsuits.

Whatever the reasons may be, the fact is that there are commercial banks today that are rendering income tax record services to even their very small depositors. And they have been doing it long enough, in different regions of the country, to suggest that it is not merely an unprofitable pastime.

THREE SIMILAR SYSTEMS

At least three essentially similar systems have been developed in the last 5 or 6 years for providing bookkeeping and tax record services to individual bank depositors. In the East there is “Check-a-Tron,” developed in affiliation with the Princeton Bank and Trust Co. (N.J.), and merchandised in banks from Maine to Florida. In the Midwest there is “First-Tronic Check Service” developed by First Wisconsin of Milwaukee and offered through the First National Bank of Fond du Lac.

But the credit for being first with the plans seems to rest with the “Bank-a-Count” system pioneered by the Farmers & Merchants Bank in Rudolph, Wis. Like many country banks, this small (capital, \$52,500) bank in Rudolph had been rendering personal tax service to farmers since the early 1940’s. More than 10 years later the bank took its first step to introduce it as a regular service.

On December 5, 1955, offering the inducement of doughnuts and hot coffee, President C. M. Amann of the Farmer & Merchants Bank called a meeting of farmers at the village school in Rudolph. The plan which he proposed called for depositors to pay \$5 per month for unlimited checking facilities, agreeing to write in a comment or two (in longhand) on each check to indicate for what it was drawn. Subscribers also agreed to indicate on deposit slips the source of each deposit. The bank promised to do the rest. Of 26 farm families invited to the meeting, 23 signed up for the plan.

HOW IT WORKS

From this rude beginning the plan has evolved and expanded until today it also embraces independent nonfarm businessmen and individuals working for wages and salary. Continuous service has been provided from the data processing

¹Dr. Hanchett, of the Wilson College faculty, based this article on material gathered while doing research into applications of electronics to commercial banking.

affiliate of the Farmers & Merchants Bank since January 1, 1956—and today this service is “syndicated” through six other Wisconsin banks and the First National Bank of Geneva, Ill.

Although there are some variations, the simple secret of all these bookkeeping plans is a dual-purpose check which simultaneously “pays your bills as it keeps your books.” All three use master codes, special check forms with space for inserting code numbers, and duplicate data cards for supplementary account processing.

At the start of the tax year the customer selects a simple numerical code to identify each type of transaction for bookkeeping records. Then, as deposits are made and checks drawn, he affixes the appropriate code number to each. The bank duplicates the amounts and the code numbers on key-punched data cards. From these cards it is a simple electronic data processing operation to prepare a printed, comprehensive, and permanent set of books with which the customer can fill out the necessary tax forms with accuracy and dispatch.

For the sake of simplicity, a code booklet provides each customer with a listing of the various kinds of income and expenditure commonly encountered and an appropriate code number to go with each. There is, of course, enough flexibility so the customer can include additional items or get a finer breakdown of some that are already included in the code booklet.

Since the customer assumes the responsibility for the initial encoding of each transaction and also for filling out his own tax form, the bank is not exposed to undue legal risks. And there are decided advantages for the customer, too.

First, it is low cost. The banks provide full checking facilities, bookkeeping services, and one copy of a permanent cumulative annual report to individual and family subscribers for about \$3.50 per month. To encourage a wide coverage of expenditures and a more significant tax report, there is no stated limit to the number of checks that may be drawn. For business subscribers, the charges range from \$5 to \$13 per month, depending on the volume.

Second, it is confidential. All of the complex processing is carried out by electronic brains whose memories have been erased. The final summary is mailed to the subscriber in a sealed envelope within 30 days after the end of his tax year, no copy being retained by the bank.

Third, it is flexible. The taxpayer is free to define special sorting categories to meet his own particular needs, and he alone controls what items are to be placed within each of the classes. Furthermore, it is not necessary to write two separate checks to embrace a compound payment such as mortgage interest and principal. If two codes are placed upon the check, the bank provides the necessary breakdown to create posting of both accounts.

Fourth, it is economically and psychologically satisfying. Scores of subscribers have radically revised their expenditure patterns after learning for the first time how much was leaking through their fingers in payment for trivial items.

THE CRUCIAL TEST

Recently an Illinois workingman was called in for tax audit—fortunately after he had adopted the do-it-yourself plan. The Internal Revenue agent nearly swooned when handed a printed summary report made out in IBM data script that looked as if it belonged to a division of General Motors. When he had recovered sufficiently to speak, the agent begged permission to keep the dossier for several days so that he might display it to his colleagues. Needless to say, the taxpayer had no trouble because the system had taught him how to keep objective track of his income and his expenses: He actually had the bookkeeping records to back up his claims.

Special Services at Proctor

- 4% paid on your money invested in saving certificates.
- Up to 6% on your money invested in Mortgages.
- Free bank-by-mail kits: we furnish envelopes and pay postage both ways.
- Free use of community room for your organizations.
- Free depository - - use it any time day or night for any bank or insurance business.
- Free parking: big parking lot at Bank door.
- Free printing, your name and address on checks.
- Free use of the Bank's telephones.
- Free napkins and placemats for church suppers.
- Free record forms for keeping family expense accounts.
- Free consultation service: you're invited to discuss any financial problems with our officers.
- Open Saturdays, 9 AM til noon.
- Driveup windows open 5:30 PM weekdays.
- Rental Service to find homes for families and tenants for property owners.
- Free subscription to the Bank's newsletter, "It's Your Money", written by our employees to help local people with the current financial problems of our area.
- Free postage on deposits and loans.
- Public accounting: bookkeeping service for business firms or individuals.
- Income Tax Service to fill out your State and Federal returns.

Christmas Clubs and Vacation Clubs to pay for these annual expenses in monthly instalments.

Package insurance with Bank financing: immediate protection of fire, auto, life of other insurance - - as much of each as you want - - to be paid for in monthly budget installments. 3% interest.

Real Estate Service to buy or sell homes and farms.

Photocopy service to reproduce any document.

Auto loans: 5% interest on new cars.

Checking accounts at 10¢ per check: no other charge no matter how small the balance.

Joint accounts in the names of two people; if one dies, survivor has full possession

Loans to buy or build homes, including homes in the country.

Loans to buy or build basement homes or to erect superstructures over basements.

Loans to buy or build lakeshore cottages.

Loans to enlarge, remodel or add new rooms to homes, or for wiring, plumbing, landscaping, roofing, basements, screens, windows, repairs or to build a garage or farm building.

Loans on appliances, furniture, equipment and livestock.

Safe deposit boxes for your papers and valuables.

Money orders at lower cost than post office.

First National
BANK of PROCTOR

Income Tax Service

Including preparation and mailing of state and federal returns, and duplicate copies for your own records.

**\$4
UP**

Every year a lot of people in this area pay more income taxes than they should. And every year a lot of other people get into trouble with the Internal Revenue Service and the Minnesota Department of Taxation because, often through error or misunderstanding, they haven't paid enough.

In doing your tax work we have two objectives:

1. To prepare accurate, honest returns that will keep you in good standing with state and federal tax authorities.
2. To make sure that you pay the lowest tax possible by seeing to it that you get every credit that is coming to you: every tax saving to which you are legally entitled.

Our tax consultants are available for daytime, evening, and Saturday appointments at the red insurance and real estate building. Please phone 628-2285 to arrange for an interview before you come.

On the average, the tax savings that we find save our clients more money than our service costs them.

First National Bank of Proctor
Minnesota

LOANS TO BUY, BUILD, OR REMODEL HOMES ANYWHERE WITHIN 40 MILES OF PROCTOR

Including the following hard-to-get kinds

Small Homes
Inexpensive Homes
Homes in Remote Areas
Farms
Basement Homes
Home-made
Homes built by the owner
Lakeshore Cottages
Temporary Homes - to serve as a garage or
workshop when permanent house is built
Shell Homes - to be finished later



YEAR-'ROUND ACCOUNTING

FOR STORES, SERVICE STATIONS, CONTRACTORS,
REPAIR MEN, AND OTHER BUSINESS FIRMS

An inexpensive service that does your book-keeping on bank accounting machines and provides the records you need for income tax returns, loan applications, and your own business decisions.

"Disentanglement from the increasing mass of paper-work is one of the small business man's basic keys to profit."

OPTIONAL SERVICES ALSO AVAILABLE INCLUDE:

1. Keeping your accounts receivable records
2. Mailing out monthly statements to your customers
3. Other mailing and letter services
4. Photostating any papers
5. Financing and collecting your larger sales and your installment accounts
6. Payments on all your accounts can be received for your credit here at the Bank

[The Wall Street Journal, Tuesday, Oct. 1, 1963]



**RELAX! GIVE YOUR
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Mr. MULTER. Mr. Lloyd, do you have any questions

Mr. LLOYD. Just for my own benefit, Mr. Balsler, I would like to ask you one or two questions. It seems to me that there are many people in the income tax business besides accountants. I see signs all over the streets which state, "Have your income tax returns made out by us."

This bill is not going to effect that any. And it seems to me that banks would be much more qualified in most instances than many of the people whose signs you see along the streets to do that.

Mr. BALSER. That is true, Mr. Lloyd. We do understand that. And that is a matter that we are, also, attempting to combat. We are attempting by legislation to bring all practitioners under control and under regulation. We feel that this is necessary. If we are able to provide this legislation it would, also, be necessary, if the bank would do income tax service, to come under it.

Mr. LLOYD. If I go into a bookstore, I can see, "Buy your bookkeeping service here—much more effective and much less expensive than hiring an accountant." This kind of legislation would not stop that; would it?

Mr. BALSER. No, sir; that is true. There are uncontrolled situations now. We do now have pending some matters which we have been discussing for about 3 years with the American Institute of Certified Public Accountants. We are attempting to provide for the regulation of all bookkeeping and accounting services through the licensing of practitioners. This is in the planning stage yet, but we are aiming toward that. We feel that the businessman deserves protection from any practitioner—that anyone who offers this service should demonstrate that he is qualified and should be able to answer for any malpractice and should be held liable by licensing laws.

Mr. LLOYD. Do you have any incidents where banks have required as a condition of a loan that the client accept bookkeeping or other nonbanking services as a condition of receiving the loan?

Mr. BALSER. We have had, I believe, one report that has come to us where this condition exists. We have had several reports where the inferences have been there, but they could not pin it down.

Mr. LLOYD. I am in favor of the public being protected against non-professional services when they think that there is difficulty, but it appears to me that you are batting at swarms of gnats by trying to take out one gnat. Is not the profession of accounting regulated at the State level?

Mr. BALSER. In some States, they do regulate it. I think we now have regulation in 35 States.

Mr. LLOYD. It would seem to me—and I am attempting to become more informed on this—that better progress could be made if you were to go to the individual State statutes and tighten them up to determine what professional can offer service and what it is and under what circumstances the service can be rendered.

Mr. BALSER. In 1945, I think there were some 14 or 15 States that had regulatory regulations. Today, there are 35 States, and we take credit for it.

Mr. LLOYD. So you are making real progress?

Mr. BALSER. Very definite progress. As I said, this negotiation with the American Institute of Certified Public Accountants has a tremendous value if it reaches the stage of cooperative effort in the

various States. We have had conflicts in various States. We are trying to bring in a uniform type of regulation or pattern for uniform type of regulation which the various States can adopt.

If we, as the National Society of Public Accountants and the American Institute of Certified Public Accountants, can jointly sponsor this legislation and suggest to our affiliated State societies that they jointly sponsor it, tremendous steps will be taken. And I think it will be a very short time before the type of legislation we are talking about will be in progress, though it will take time to implement.

Mr. LLOYD. I have no further questions. Thank you.

Mr. MULTER. Mr. Moorhead?

Mr. MOORHEAD. Mr. Chairman and Mr. Balsler, I would like to ask you, sir, when did banks start into these practices. Was there any incident or fact such as the use of computers, that brought about these practices?

Mr. BALSER. Actually, this was brought about primarily by the development of the computers. In other words, I think that the primary factor that started this has been, as I said, that here is a bank with \$7 million invested in expensive equipment. The utilization of that equipment for the bank service justifies its cost, but the bank's records are picked up after closing hours, taken to the computing center and the records are in the hands of the tellers the next morning when they open up for business. Therefore, during the daytime hours that expensive equipment is idle. That was a \$7 million investment. Naturally, the bank would like to keep that equipment busy 24 hours a day, but we feel that it should be kept within proper circles.

The first instance that we had was back in 1955 when Sylvia Porter, the columnist, wrote a story, I think, in advance of any intent to have it broken, that the Bank of America, was contemplating this type of service. I was then working with the Society of California Accountants. We traced it down through the bank, and they at that time advised us that they had been studying such a thing, but that they had not gone ahead with it and were doubtful that they would. This was from one of their vice presidents who was presently in charge of operations. It lay dormant for 7 or 8 years, but the utilization of computers by so many different banks has brought this to the fore now and the competition between banks, I think, has created this situation. They started out offering the computer service for a nominal fee. And as I pointed out, now they are competing with each other until they are offering, as you gentlemen know better than I, free interest, free tax returns, free computer service, free adding machine use in the lobbies, et cetera. The competition has brought this about. And, of course, this bookkeeping service is a tremendous lure to the unsuspecting small businessman.

Mr. MOORHEAD. Do accounting firms have the same computing service to offer as the banks have?

Mr. BALSER. There are very few accounting firms that have that type of computer in their own offices. They have smaller computers which will serve the needs of their offices. They are not as large. Naturally, they do not accomplish as much. They do, however, when they get into this type of thing, have available many computer centers which are developed, primarily, to serve the public, and the accountants for the gathering of statistical data, which is the biggest thing that a computer can do. It will not keep a set of books.

Mr. MOORHEAD. I realize that.

Mr. BALSER. But that is the misleading information that we feel is being given to the businessman. The businessman has a great deal of respect for the bank. This has been built up over a period of time. We think that is fine. We do not like to see the banks mislead the businessmen into believing that they have a full and complete accounting service from computers.

Mr. MOORHEAD. You cite the example of a banker handling a payroll for a businessman. If we pass this bill, and if this businessman wants to have his payroll made out on a computer, where would he go?

Mr. BALSER. The accountant can offer that service at a fair and reasonable price, because the accountant can get that computer service from a service bureau or, as I say, in a great many accounting offices, they have their own computers on a smaller scale which are adequate to perform these services for the average business. We are not talking about a payroll for Lockheed with 50,000 or 60,000 people. We are talking about the average man with a small business with anywhere from 5 to 150 employees. We have an example in our own firm. One of our clients wanted this type of service and we were looking at various services. We felt that it was comparable, and that if they wanted to buy it, all right. We expected them to do it. The bank recommended at the time that they could save a great deal of work for this man, if they took the payroll and instead of preparing the payroll checks, returning them for signature and then to be passed out to the employees, that the bank would open accounts for each employee and deposit the payroll amount directly into each employee's account. That was very nice business for the bank, of course.

We felt that we did not trust the computers to that extent; that we did not want to checkup; so we said, "No", we would rather have those payrolls come back, and have the payroll checks completed, so that we could review them for our client, or the client's payroll clerk could review them, to make sure there were no errors. Computers can make errors if improper information is fed in. We found over a period of 4 or 5 weeks a half dozen errors which we caught. The most glaring was a dishwasher who was making \$45 a week and received a check for \$600. If that dishwasher had cashed that check, he would have long been gone, and somebody would have been out the \$600.

That is the sort of thing that I think we have to watch for in any mechanical service. The machine can only deliver what information has been put into it. If improper information is either furnished by the client or the customer or is improperly selected by the computer operator, that will result. In this particular case we think that what happened was that the payroll clerk had some poor information which was inadequate. The computer technician had no knowledge of accounting; and therefore, did not detect that it was an error. He fed that through, the computer balanced everything all right, and that check came back. It took someone with some knowledge of that client's affairs to recognize that that was, obviously, an error.

Mr. MOORHEAD. Which demonstrates that a human being is still important in our society today.

Mr. BALSER. That is right. We have had many lectures at various society functions by people from the computer centers or computer builders, and the first thing they tell us is, "do not depend on the com-

puter to do any thinking. The computer is a pure mechanical operation. It does mechanical operations a thousand times faster than any human being can think, but the information must be fed in by humans and after it comes out it must be reviewed by humans."

The Internal Revenue Service should know—they started the use of computer services. They have three districts in operation now that are using them. It will be wonderful when they get them all in operation. You will find glaring errors, occasionally. You read in newspapers every once in a while that somebody gets a refund of \$6 million or something like that who is entitled only to about \$6.36, but those are things that are computer errors or the result of improper information fed into the computer. So the computer will not take the place of professional people. That is our entire major point.

Mr. MOORHEAD. Thank you, Mr. Chairman.

Mr. MULTER. In the 35 States that you say have laws regulating accounting, do they provide criminal penalties for those who perform such services without being licensed?

Mr. BALSER. In most cases they do. Those that do have any licensing controls have severe penalties. They have the loss of the license. And in the violation of any criminal law they provide for criminal penalties.

Mr. MULTER. Will you supply for the record a list of these 35 States indicating the penalties they impose and showing how they vary from State to State?

Mr. BALSER. We will furnish that for you.

(The information requested is as follows:)

States having regulatory accountancy laws arranged chronologically by date of enactment

Louisiana.....	1924	Alaska.....	1949
Maryland.....	1924	Washington.....	1949
Michigan.....	1925	Oregon.....	1951
North Carolina.....	1925	Vermont.....	1953
Florida.....	1927	Arizona.....	1955
Illinois.....	1927	Connecticut.....	1955
Virginia.....	1928	Hawaii.....	1955
Iowa.....	1929	Tennessee.....	1955
Mississippi.....	1930	Nebraska.....	1957
Wisconsin.....	1935	West Virginia.....	1959
Colorado.....	1937	Utah.....	1959
Georgia.....	1943	Ohio.....	1959
Missouri.....	1943	New York.....	1959
Puerto Rico.....	1945	Nevada.....	1960
Texas.....	1945	South Dakota.....	1961
California.....	1945	Rhode Island.....	1962
Kentucky.....	1946	Massachusetts.....	1963
New Mexico.....	1947		

The above laws provide in general that any person who violates the provisions relating to practice without a license shall be guilty of a misdemeanor and subject to the levy of a fine, imprisonment, or both. For the most part, the fines are set at a maximum of \$500 and imprisonment for not more than 1 year. In a few cases a \$1,000 maximum fine may be provided. Also, a 6 months' maximum prison term is provided for in a few statutes.

The most recently enacted law in Massachusetts provides that persons who may violate its provisions shall be subject to a fine of no more than \$1,000 or 1 year in jail or both. In New York State, the law provides for a maximum \$500 fine or 1 year in prison.

Mr. MULTER. I think that in every one of the 50 States we have laws prohibiting persons who are not admitted to practice law from practicing law.

Mr. BALSER. That is correct.

Mr. MULTER. I think that in every one of those 50 States there are criminal penalties and in addition to that the violator or the person practicing law without having been admitted to the bar may be cited and punished for contempt of court. You do not have any similar contempt proceedings for violation of the accounting laws?

Mr. BALSER. No, sir. I do not think there are any.

Mr. KAUFMAN. It is mostly fines or imprisonment.

Mr. MULTER. In each of the 35 States which regulate the accounting profession, the person must pass a test before he can practice?

Mr. KAUFMAN. It definitely prohibits the use of advertising and the like.

Mr. MULTER. Do each of these 35 States that regulate accounting and license accountants or certify accountants, prohibit them from advertising?

Mr. KAUFMAN. That is right.

Mr. BALSER. That is right.

Mr. MULTER. Is there any difference in the States between the so-called certified public accountant and the licensed accountant?

Mr. BALSER. In some States there is quite a bit of difference. For instance, in California they are under the same type of regulation, the same code of ethics, the same rules of professional conduct, the same penalties. And now after some 20 years, there is a State joint resolution which passed sometime ago recognizing that wherever a certified public accountant is called for by any State agency it should, also, include public accountants, so that they are recognizing the fact that they are exactly alike. In other States, which are newer, there is still a distinction—there is still some discriminatory practices which will take merely a matter of time to work out.

Mr. MULTER. Is it true that in those States that certify public accountants, they do not license public accountants, that the certification is the licensing process?

Mr. BALSER. Actually, for instance, in California the licensed public accountant is either a public accountant or a certified public accountant. In other words, there are two classes of licenses the way they treat them. Utah has the same thing.

Mr. KAUFMAN. And that is true in Rhode Island.

Mr. BALSER. It is different in different States. In some States they come in only by a grandfather clause. And then there is a closed-door type of legislation. In other States—Tennessee, New Mexico—there are continuing licensing of accountants, and by examination.

Mr. MULTER. In New York you have both certified and licensed accountants?

Mr. BALSER. Yes. They passed a law in 1959 licensing public accountants. And so they have both the licensed public accountant and the certified public accountant.

Mr. MULTER. Would it be safe to say that in every State where there is a regulatory law that the person must either be certified as a public accountant or licensed as a public accountant to practice the profession of accounting?

Mr. BALSER. That is correct. In some of those States, the laws are flexible enough so that they do not control the minimum bookkeeping type of service. This we would also like to control because we feel that even the bookkeeper who offers a service to the public should be under restrictions and should be required to provide adequate service.

Mr. MULTER. Many States indicate what a lawyer may do in connection with the tax law and what an accountant may do in connection with the tax law.

Mr. BALSER. That is, also, true in joint statements between the various professional groups in an attempt to define the limitations. There is a broad, gray area of overlapping and there always will be. In other words, in the preparation of a State tax return at one time the bar association felt that should be exclusively in the realm of the attorney. They have found that there is so much accounting to it that a great many attorneys are calling upon the accounts now to prepare those returns for them, because they can do it so much more easily and because they have the knowledge and familiarity with the figures which the attorneys do not have. So there is greater cooperation coming between the professions in that respect.

Mr. MULTER. Is it safe to say that, generally speaking, the accountant may not give advice regarding the effect of the tax laws. He may set up his client's books and records and may prepare the forms and investigate all of the necessary factors to sustain the tax return but when it comes to a contest whether an item is deductible, or what particular section of the Revenue Act applies to the taxpayer, that falls within the category of legal advice and is assigned to the lawyer?

Mr. BALSER. That is true. There are lawyers, for instance, who deal in that field. But in the appellant part of the Internal Revenue Service we are dealing mostly with accounts. The accountants find that they can work better up to that level. When it gets to the Tax Court level, then usually we, as accountants, step in the background as advisers to the attorneys, and they take over. Up to that level, if we get to a borderline point, we usually advise our members to call in an attorney to advise them. We are working much better in cooperative arrangements with the bar associations than we have ever had.

Mr. MULTER. I have before me several items that you submitted for the record.

Mr. BALSER. Those I did not quote from, but I just wanted to give you examples.

Mr. MULTER. There are seven or so in all?

Mr. BALSER. Yes.

Mr. MULTER. I have not had an opportunity to read them thoroughly, but only to scan them. Do any of these refer to the service some banks are now offering where they bill the client or the customer or the bank's customer and collect the bills by charging them to the bank account of one customer and crediting the account of the other customer?

Mr. BALSER. I do not believe there are any of those. We have one from the Wall Street Journal that the Bank of America offered that service not too long ago.

Mr. MULTER. What is that service?

Mr. BALSER. The Bank of America has set up a service for doctors and dentists in which they will handle all of the accounts receivable,

and all of the payments on computers and send out the bills and make the collections and everything else. This is the United California Bank. It is another chain of banks. It is a billing and collection service being programed for hospitals and a variety of other businesses. It is a service that will provide a billing and collection service for accounts receivable and to prepare the necessary reports for management. They state that also beneficial to businesses are extensive services in remittance banking which utilizes a lockbox arrangement for expediting the collection of payments. They have a savings account complete reconciliation service. This is the type of thing we are running into.

Mr. MULTER. Is it fair to say that no institution is going to undertake to bill customers and collect the money and render the full service without doing an accounting job and reporting exactly who paid and who did not pay and how much they paid and how much is outstanding?

Mr. BALSER. Not only that, but the doctor's office will have no accounting records in the office. The patient may come in and want to know what the balance is. They call up the bank and the bank gives them the information from the computer. So the doctors do not even have the records in their own office. The bank is actually the central billing accounts receivable department for them and handles the collections, and so forth.

Mr. MULTER. How does the doctor handle cash items?

Mr. BALSER. I do not know how they will do it.

Mr. MULTER. Reference has been made to the matter of a set of books, which permits the person purchasing the books to learn to be his own accountant or bookkeeper. Your organization is not urging that people should not try to do their own work or not buy these books and not educate themselves as to how to do that?

Mr. BALSER. No. Actually, one of the things that we run into with the Internal Revenue Service is this, that they have stated many times that they do not want any restriction placed upon anyone performing his own service in preparing his own tax return or selecting anyone whom he pleases to select. We have had discussions with some of the leading people in the Internal Revenue Service on this. We feel that they would like to have a way out of that so that if you select someone that person is recognized and trained. But so far as the preparation is concerned, it is the same thing with the doctors, with the homeopathic remedies that you can buy books on—you can buy books on law simplified and everything else. Those things will always be done. And we believe that it is good for the average businessman to know something about bookkeeping and accounting.

Mr. MULTER. If you do choose to be your own lawyer you would have a fool for a client.

Mr. BALSER. That is it exactly.

Mr. MULTER. Any questions, Mr. Bolton?

Mr. BOLTON. I will yield to the other two. I will come back in later, if I may.

Mr. TALCOTT. I have a few questions. It seems to me at first blush that you people in the public accounting field are getting too worried about something that should be of benefit to you rather than a detriment. I think I would prefer to have somebody else do the legwork,

the basic bookkeeping and provide the raw data for me, so that I could better perform the professional work, the analysis, and the advice. I would welcome someone who would bring in all of the raw material, so to speak, if I were an accountant. I do not yet see why you people would object.

Mr. BALSER. We do. We do welcome that. In fact, we use it, because there are many service centers that are in business just to handle that. And a great many accountants refer those to the centers. The centers prepare the statistical information and send the information back to the accountant for analysis and for interpretation and discussion with his client. The bank is not offering that service. The bank is offering to give advice and creating the image, like the Citizens Bank and Trust Co., that the president of the bank will confer personally with the businessman, and all of that service is offered free.

Mr. TALCOTT. Is it your contention that the bank is actually giving accounting advice, rather than just supplying the data?

Mr. BALSER. They are actually creating the impression, in a great many cases, that they are. We feel that they are actually not doing that. In other words, I cannot believe that the president of the bank can afford to do so. With a \$7 million installation of computer equipment, he can't be serious when he says, "we will offer all of these services free, and you can call on me personally to confer with you either at the bank or at your own place of business about your business problems."

Mr. TALCOTT. Actually, of course, the image that is created might be a little different from the fact. We need to get the facts. It would seem to me, along this line, that you may have created the image that the public accountant and the certified public accountant in California was pretty much the same. It is my understanding that they are quite different.

Mr. BALSER. I said that they can do the same things. They can perform all of the same services. There is no differentiation between the services they may perform.

Mr. TALCOTT. But the requirements are different. Also the background, training, experience, examination, and licensing may be different.

Mr. BALSER. I think I stated, that the certified public accountant passes the examination in California and in many other States. Public accountants have been grandfathered in; that was some 20 years ago, or 19 years ago.

Mr. TALCOTT. Is there some way that this bill could be limited to make certain that the bank would supply only the raw data, the bookkeeping data for the client, rather than accounting devices, analysis, and professional services? If so, would you then have no objection?

Mr. BALSER. We would have no objection—I mean, it would certainly reduce our objections. However, we do feel that if we were to do that, the bank should make it very clear to the customer that it is not attempting to enter the accounting field or to offer accounting advice. In other words, the image of the bank is such that when a bank does something, the average small businessman thinks that the bank is competent—they have built an image like that and justifiably so. I think they should limit that and should recognize the fact that when they state, "we will do bookkeeping and accounting services for

you," the businessman is going to say, or think, that the bank is doing his accounting service, the same as the accountant is doing it.

Mr. TALCOTT. Is it not important for a doctor and a dentist to have a service like this, so that the doctor and the dentist does not have to perform all of these bookkeeping procedures leaving him more free to pay attention to his professional work. Many doctors and dentists have such facilities, in one way or another, where they do not have records in the office, whether it is your service or some other large accounting firm's service or a bank's service, which gives him the data, but not advice.

Mr. BALSER. Actually, the various branches of the medical association, for instance, in one county in California, are trying to create this same service. We have no objection to people doing the bookkeeping service. As accountants we are not particularly interested in sitting down and writing up the entries. We have gone beyond that, the same as the banks have.

Mr. TALCOTT. So far as the banks are concerned, is it not impossible for them to practice accounting? The law prohibits corporations from practicing accounting, does it not?

Mr. BALSER. They cannot be recognized as public accountants or certified public accountants, but the California law would permit them to do any form of bookkeeping. There is no limitation in the law. The law is rather strange in California in that respect. It covers everything but the service.

Mr. TALCOTT. This is the point I am trying to bring out. Should not the accountants and the bankers and the bookkeepers be joining in this effort, to determine if there is any way that we can speed up or facilitate the gathering of this raw material, to permit the accountant to better perform the professional service, rather than a menial service, and that they should get together to do that. I think that my time has expired, but I wanted to point out some common ground on this subject.

Mr. BALSER. We have no objection—in fact, as I say, we use the computer services that were developed in business for that purpose. They give us much faster service than the banks can give us, because you can get overnight service. So the bank is not offering a service that is not being offered already. It is being amply offered by other services. In that case they are in conflict with the computer services which we do not represent here today.

Mr. MULTER. Mr. Grabowski, any questions?

Mr. GRABOWSKI. No questions.

Mr. MULTER. Mr. Halpern?

Mr. HALPERN. Mr. Chairman, I am not a member of this subcommittee. I do appreciate the privilege, as a member of the full Committee on Banking and Currency to sit in on this hearing. I am very much interested in the subject matter of these hearings.

Mr. MULTER. Mr. Bolton?

Mr. BOLTON. I am sorry to have been late. We have three hearings going on this morning. I have taken the opportunity while the others were asking questions to read your statement. At the bottom of page 6 you make a point that there is danger that the typical businessman may be lulled into feeling that his accounting is being well taken care of by the bank when, in reality such might

not be the case at all. Are you suggesting that this decision should be taken from the businessman?

Mr. BALSER. Oh, no.

Mr. BOLTON. I raise this question because in conversation with a member of the present administration the other day that member specifically stated, in answer to a question from me, that yes, it was the policy of this administration in the field of normal consumer affairs to advocate the ruling of common law, caveat emptor, and to go further, to let the buyer beware, that this was the policy of the administration. As you know, one of the great problems with which business is faced or has been over the last few years, has been an effort to cut costs of operation. And this has been directed at the general costs of business. There is no question that public accountants offer a very great service to business in analysis, et cetera, but would you not agree that any steps which could be taken, which would reduce costs to business, both large and small, from the accounting standpoint, from any recordkeeping standpoint, would be good for the country?

Mr. BALSER. Very definitely. In fact, actually, in our discussion here we have said that we have no objection to this. In fact, the service that the banks are offering is not exclusively a service that the bank normally renders. They have entered into a field which for many years, ever since the development of computers, has been offered by service centers, and by accountants, who use the information. There are a great many business firms who use small computing services. We have no objection to the use of the computer services, but we feel that this is a service that is available to any businessman through any other facility. The big problem that we have here is in reading the publications, the brochures, and the advertisements that are being put out by the banks, which create the impression, as we say here, that the bank is offering a complete accounting service. And in 90 percent of the cases they are not. They are doing the legwork. The most important point is that the interpretation and the analysis of what those statements are when they come out is not being done. And the businessman feels upon reading the advertisement that is all the service he needs.

Mr. BOLTON. Let us take a regular commercial bank operation before the computer. A businessman comes in and asks for a mortgage loan which is made. And that mortgage loan the bank supervises. It is a sizable loan. It may be that the bank will ask to have a member of the bank put on the board of directors. It may be that this will be in a pro forma fashion, merely so that the mortgage department can follow the operation of that company. And then to protect its loan it may have to go further and it may have to give advice to the management, so that the bank can keep that a good loan. That is a service which banks have offered over a long period of time. And here we have been forced, because of a very expensive machine—a machine in due time can additionally offer services to its customers, to do so.

You mentioned the relationship earlier between lawyers and accountants. And that there was a gray field in between. Is this not also a gray field that of necessity must grow out of the regular services which heretofore the bank has not been able to provide for its customers?

Mr. BALSER. I think that you have overlooked one point, where you have the member on the board. There is one tremendous factor which has always been available, and that has been that the bank has looked to the independent accountant to prepare financial statements and to present them from an independent source. The bank can discuss them with the accountant and get a great deal of information from the accountant on which to base judgments.

In other words, even when the banks put a man on the board, you will find in 90 percent of those cases—maybe in more than that—that there is a condition that an independent financial statement must be rendered. On the other hand, these are not the ones we are worried about so much. Many firms are large enough to do that. It is the small businessman who has 1 bookkeeper, maybe 3, 4 or 5 or 20 employees, and who does not have a comptroller available, as in the large organization, and who does not have a board of directors to share the responsibility in reviewing these things. The small businessman by himself is not familiar with this.

Large businesses can afford to spend thousands of dollars a year for comptrollers and financial advisers. They can have them on their payroll, and keep them there for that purpose. The small businessman cannot afford that. He has to look to someone else, because he needs financial advice as much if not more than, the big businessman.

Mr. KAUFMAN. If I may add one particular point. In the example that you cite, the bank is interested in protecting the depositors' funds which are used to make the loan. If they are offering a service now, where there does not have to be any consideration of the fact that they are loaning any depositors' funds, that is another thing, the banks are offering a service to business, and this is not a matter of their protecting the loan funds they made available to a company.

Mr. BOLTON. I did not make that point. It is as to the use of the equipment to its maximum extent. It is very, very expensive equipment.

I was in a small business and I had a bookkeeping staff of three. I could not afford a topnotch certified public accountant. I had two very good bookkeepers and an accountant. Sure, we had a public accountant firm that came in and made a quarterly audit. But if I had been able to have service, the checking of the figures, checking on my bookkeeping, this would have been a very real service to me.

Mr. BALSER. You see, the bank does not offer that. The bank merely offers this. "We have this computer." The computer is not a verification. It merely does the detailed work faster and more accurately than the handwritten system. That same service today is available. If you were in business today, your accountant, undoubtedly, would have already said to you, let us stop this handwriting, let us bring in a punch tape adding machine and we will tape those figures off. And that tape will go to the computer tonight and tomorrow or the next day we will have that back, that is, the information.

This is not a service exclusively done by the bank. It has been done for many years now, 5 or 10 or 15 years by the accountants, and by the service centers. IBM has tremendous service centers all over the country.

Mr. BOLTON. Then my line of questioning has brought out the point that I was getting at, because if that is the case, why does the offering

of the computer service by the bank, why does not that fact exclude in any way your fear that this is a job that the accountant is performing for the company.

Mr. BALSER. The primary problem has been in reading these advertisements. They do not say, "We will do your detail work, we will not do your analysis"—the advertising says, "financial analysis." We have right up there that "the president will meet with you in your own place of business."

Mr. BOLTON. I am confused, Mr. Balsler, because again I go back to my original question, a commercial bank in precomputer days did do analysis service work for customers in the commercial loan department of the investment department. It would sit down and analyze your problem in the personal loan department.

Mr. BALSER. Right.

Mr. BOLTON. It would sit down and analyze your problem. It would help you work out your financial problem. This was one of the great services that the bank offered.

Mr. KAUFMAN. There would be no attempt to stop the bank from doing this, especially when you are discussing the borrowing of the bank's funds.

Mr. BALSER. That is right.

Mr. KAUFMAN. No accountant is adverse to that.

Mr. BALSER. We have worked with the banks closely in that field.

Mr. BOLTON. Your position is that if the bank has a vested interest in the person, namely, if they have an account of \$100 or more, this is all right, but if they do not have an account with the bank, then they should not be able to do it—is that the point?

Mr. BALSER. No, no. We say this, as you say, the bank has done this traditionally for one purpose, to protect their loan. The bank does not go to you who do not ask for any money and say, "We will do your bookkeeping free," does it? It never did.

Mr. BOLTON. It does it for two purposes. It does it to protect its loan, and it does it to give service to the customer, to attract more customers.

Mr. KAUFMAN. I think you will find that the tradition has been that you walked into a bank to discuss the consideration of a loan, the borrowing of money or financing, and the bank has always asked, "Do you have an accountant?" and "Has the accountant prepared a financial statement which you can submit to us for analysis which we will then analyze and we will discuss, or we will call the accountant in and discuss the situation with him, and then we will make a decision as to whether we can loan you funds or not loan you funds." But the implication now is that on the basis of the computer system operation they are indicating that, "We will prepare the groundwork, and then we will finish the statement, and then we will decide without discussing it with anybody else whether we are going to loan you funds or not."

Mr. BOLTON. In other words, your fear is that this development will cut out the financial reliability part of the independent judgment of an accountant or an outside financial expert?

Mr. BALSER. That seems to be the trend. If you will look at those clippings we have submitted you will see that they imply that. "Who does your accounting now?" they say.

Mr. BOLTON. Well, gentlemen, if we are dealing with a corporation and you are asked by management on a particular matter, dealing with an accounting firm, and the house accountant has rendered an opinion, that is, the house counsel, do you rely on that house counsel's opinion or do you insist on going to outside counsel?

Mr. BALSER. It depends on the situation.

Mr. BOLTON. Does it not depend on the situation in this very instance?

Mr. BALSER. I agree you would do that.

Mr. MULTER. Are you suggesting that the bank should have house counsel who advises the customer?

Mr. BOLTON. I am not suggesting that, although you and I know, as a matter of practice, that most large banks have a lawyer who is not practicing law, but who is a member of the bank.

Mr. MULTER. Yes, but not giving legal advice to the customer.

Mr. BOLTON. I understand that.

Mr. MULTER. Why should the bank now give accounting service and advice to the customer?

Mr. BOLTON. I did not suggest this. I was pointing out that this was similar to an instance where an accounting firm, in going over the history of the corporation, comes upon a legal question in its preparation of its accounting records, that it does not in every instance insist upon going to outside counsel, but in its judgment may take the opinion of the house counsel of the corporation that they are auditing.

Mr. KAUFMAN. The house counsel is practicing law and is retained by the firm to practice law.

Mr. BOLTON. That is what I implied by the term of house counsel.

Mr. MULTER. This is quite different.

Mr. BALSER. A big difference.

Mr. MULTER. The lawyer who is house counsel for the bank cannot give advice on behalf of the bank to the customer. If he gives his advice to the bank, he is being paid by the bank—he is not being paid by the customer of the bank.

Mr. BOLTON. If I may interrupt the chairman, I think that you are twisting the point I was trying to make. I was using it as an example of the contrast of judgment on the financial report which might be given by the bank as to whether or not another lending member of a State bank, whether or not they would require that, that the potential borrower went to a certified public accountant or outside financial analyst.

Mr. MULTER. I was not twisting what you said, but I was deliberately trying to make the point that the accounting profession and the legal profession are the same and that the same provisions that apply to a bank as to lawyer services should apply to accounting services—that the same restrictions should apply to the bank in the practice of law as it does in practicing any other profession. If they are going to be permitted to give accounting services free, why not give legal services free?

Mr. BOLTON. I agree. I do not understand that there is a law that requires otherwise. In the law profession, as you go to court, there is the requirement that you have legal counsel.

Mr. MULTER. I think that most regulatory authorities insist that banks make loans on the basis of certified public accountants or

licensed accountant's statements, while in some instances they may be permitted to make loans on the basis of accountant statements, when he is neither licensed or certified.

Mr. BOLTON. If that is the case, then we are not talking about anything, because if the certified public accountant, that is required by law, there would be no change in the position.

If I may return to the statement, at the top of page 7 you point out that more and more use is being made by accounting firms of specific data computing equipment, et cetera. If this is true—if the analysis of the accountant is what you use, his report, as you have every right to believe is correct—what puts the bank in a different competitive position?

Mr. BALSER. I would say this, that the service that is offered by the accountant includes the service that is offered by the banks. That service, in some instances, is done right in the accountant's office with his own computers. These are much less expensive, of course, and much less rapid, but they do not need to be as rapid or as expensive.

Mr. BOLTON. I know nothing about this.

Mr. BALSER. It is a smaller computer. An accountant can handle a thousand or 2,000 accounts on this small computer. The bank that handles 200 or 150,000, or a large chain bank which will handle millions of accounts, will need a much larger type of computer, but the small computer will do the same job for the small man that the Bank of America's tremendous installation will do for all of their clients, so that the computer service is available to the businessman through the accountant. If the accountant does not have his own computer, there are commercial computer services which have large installations where they will do work for the accountant and return the work. They have no direct connection with the businessman. We have other computer services which work directly with large manufacturers, and large companies, where they need statistical data, cost information, and similar information which is done directly, either within the company's own computers or through a service bureau. So there are many fields available. The bank is not offering anything new, except that the bank says, we want to get into this gravy train, because every one of these bookkeeping accounts that they handle means another depositor for them. And the payroll service, too. They are selling that on the idea that they will make out the payrolls. They will not make out a payroll check, but will open an account for every person on the payroll and transfer that money directly into the employee's account. That means that if there are a hundred people on the payroll that there will be 100 new accounts. We do not feel that is a good service, because the businessman does not have a chance to look at the information. And as we have pointed out in our testimony, we have found instances where there have been many mistakes, either on the basis of the information that was given to the computer or the improper handling of it by the technician who fed it into the computer, and ridiculous answers have come out.

The technician has no accounting knowledge; and, therefore, does not detect the errors. It would go into somebody's account before it was detected. We had one case with one of our clients who used one of those services, where if the bank had been able to do the service they recommended originally, rather than have checks come back to

the plant for review, a \$600 check would have gone into the account of a dishwasher in a restaurant who, probably, received \$50 or \$60.

Mr. BOLTON. I realize I have overstepped my time. I apologize to the members of the subcommittee, but I find it exceedingly difficult to understand why if a service is being provided that is valuable, which it is, by the accounting profession, that this will not prove itself, and that the service as such, if it will reduce the overall cost to a businessman, why it should not be a good thing to have.

Mr. BALSER. May I pose one question on this?

Mr. BOLTON. Yes.

Mr. BALSER. I think it might point this up. Suppose that the bank takes over the bookkeeping accounts and the bookkeeping work, we will say, for one of my clients, and that client goes to the bank and says, "I want to borrow some money," who is the bank going to look to for a statement? They have kept the books themselves. Are they going to ask for an audit or are they going to say, "We have the records here, we can handle it alone"?

Mr. BOLTON. He can take those records himself wherever he wants to go with them.

Mr. BALSER. Not a computer. It does not produce the type of ledger sheet that we are used to. It produces complete information.

Mr. MULTER. Theoretically you are correct. You can take the information where you please, but the danger is, as I see it, that this makes the customer of the bank a captive of the bank.

Mr. BALSER. That is right.

Mr. MULTER. That is the real danger, plus the fact that there is a difference in philosophy. They cannot control the accountant. I think this is unfair competition and it is very bad to put a bank officer on a board of a company as a condition for making the loan.

Usually that type of loan contract has a provision in it that if any further borrowing is necessary, that the bank has first call. This is the worst type of unfair competition and restriction. This ties the customers into the bank so that they are not able to go anywhere else.

There is another very serious problem. My friend stated that this is a service that the bank should be permitted to render. He would be the first one to say that the banks should not give gifts in order to induce a customer to come in—whether it be a \$5 gift or \$10 gift. What is this except a gift? It is an evasion of the restriction against paying interest on demand accounts. Anytime that a bank renders a service to its customers, other than banking service without charge, it is evading the restriction against paying interest on demand accounts. Whether it is giving a service or a gift or anything else, it is evading the statute which prohibits paying interest on demand accounts. That is another vice that I see that is inherent in this kind of service being rendered free.

If banks are going to charge for this service, then in 35 States they will be violating the law in selling the service. So either way such service is a violation of law. Are there any other questions?

Mr. TALCOTT. May I take about 30 seconds more?

Mr. MULTER. Surely.

Mr. TALCOTT. In California, if the banker practices accounting is there not some recourse that you have against him?

Mr. BALSER. There is a problem of a definition of the practice of accounting.

Mr. TALCOTT. Would it not be more appropriate then to direct your attention to the inadequate or the improperly defined law in California, rather than to promote a Federal law?

Mr. BALSER. Actually, I think that it is an entirely different problem. I think that as the chairman pointed out there is a question of ethical problems.

Mr. TALCOTT. I disagree with him about the gifts and services. There is a great deal of difference between a service that a bank renders and a gift.

Mr. BALSER. Certainly, there is a question of the bank entering into the field of accounting, which may be different from the type of service they render. As to bookkeeping service, there is nothing in the California law to prevent banks from doing that, because there are unlicensed practitioners who do straight bookkeeping.

Mr. MULTER. May I suggest, Mr. Talcott, that national banks are not subject to the restriction of local laws in the various States.

Mr. TALCOTT. It is my understanding, that no bank—National, Federal, State, or local—can practice accounting in California.

Mr. MULTER. I am sure that the State law may prohibit the State banks from practicing law and accounting, too, but we are dealing here with national banks, as well as banks that are insured by the FDIC, as well as members of the Federal Reserve System, so that we can reach through this legislation institutions that might not otherwise be reached.

Mr. TALCOTT. I think the important thing is that if the people in California or in New York do not want banks to practice accounting, that the California and New York laws should reflect their desires.

Mr. MULTER. I think it is pretty definite as to State banks. I think that it is very appropriate that we should enact legislation such as this, if the committee sees fit. This is not a question of trying to regulate matters that should be left to the States. If a bank wants to be subject to State regulation it should have a State charter and should stay out of the Federal Reserve System and the FDIC. If it can exist that way, it will then be subject only to the State law.

Mr. BOLTON. As I understand it—and I would appreciate a comment on the New York law—the question here that is important now is not that the witness objects to the bookkeeping function of a bank, but rather that he objects to the credibility that will be put upon the records which come from such bookkeeping functions, is that correct?

Mr. BALSER. That is one phase.

The second phase is as the chairman mentioned, the implied captivity of the customer, once he has his records in the bank.

Mr. BOLTON. Again cut me off, Mr. Chairman, if I am exceeding my time—I am not familiar with the systems that are available today in the data processing systems. Is not the record the final sheet that is the result of the data processing machine equipment—is that not available as readable evidence of the financial transactions in the same way that a ledger sheet is?

Mr. BALSER. The summary is there. In other words, the thing that comes out of the data processing equipment is not a ledger sheet that

you can look back to. If you want to see what has happened in the past 12 months, you take the 12 monthly statements and put them together.

If you want to see the progress of your bank account, you cannot look at one page and see it.

Mr. BOLTON. If the books show 30 cents out, can you trace that?

Mr. BALSER. You would not have that on the computer. It will not feed the information out until it balances.

Mr. BOLTON. If the 30 cents is in a food account, rather than in the rent account—

Mr. BALSER. The point that I am getting at is that would not be a fault of the computer, because the computer, when it puts that 30 cents in, posts a debit and a credit, so that you will not be out of balance. If improper information, such as the wrong account number, is put on there, the computer has nothing to do with that. That is again the human coding that could be wrong, and that could be analyzed again.

Mr. BOLTON. But it could be analyzed from the records? Did I understand you to say that in your capacity you can take the record from the computer and you can audit that record just the same as if you were handling the books of accounts?

Mr. BALSER. That is right.

Mr. KAUFMAN. In answer to the particular point as to the human element that is involved, if a computer operator capitalizes an item, instead of expensing it, or he expenses it instead of capitalizing it, until an audit takes place, it will go on before it is found.

Let us assume the example that the client thinks the bank is infallible and accepts the statement. This could be a possibility. There could be the possibility that I could feed a capital item in that is expense. The return is prepared. And this is expensed out. And as a conditional result the tax liability is reduced, instead of being capitalized, and 3 years later the audit takes place, and the client has an interest charge and might possibly have a penalty situation. Who is going to accept the responsibility? Who is going to say, "Well, this is an improper result of an audit or something?"

Mr. BOLTON. Just one more question. Actually, then, with the new method of bookkeeping what your fear is that because of the machine job is under the aegis of a responsible organization, that the customer will be lulled into security as contrasted to the feeling that he must come for an audit. Are you, perhaps, not a little ahead of yourself which will be proven out after 2 or 3 years that the same situation will exist?

Mr. BALSER. We have evidence of that already; of reports from our members as to what is happening.

Mr. MULTER. That is one of the reasons that you feel that way?

Mr. BALSER. Oh, yes.

Mr. MULTER. You emphasize that part of the problem. Where a statement has a \$100 charge, it may be fed into the computer either as a contribution or an advertising expense. There is no way of checking that item when it comes to making up the income tax return. Instead of being in the advertising column as an expense, it can well be in the contribution column, where it may be only partially deductible?

Mr. BOLTON. The gentleman testified that there was a way of checking it out, in just exactly the same way as if it was posted by hand.

Mr. MULTER. Provided it was audited.

Mr. BOLTON. If it had not been audited with personal posting it would not show up, either.

Mr. BALSER. That is true.

Mr. BOLTON. So it is six of one and half a dozen of the other?

Mr. BALSER. The only difference, though, is I think when the accountant takes that information from his client he feeds it into the computer or sends it to a processing center and it comes back to the accountant and before he presents that to his client he reviews it and checks it. If it is sent to a customer of the bank directly by the bank, who makes up the statement, and they return it to the customer, who is not qualified to review those statements properly, it may go undetected.

Mr. BOLTON. If so, this would revert to the reputation of the bank.

Mr. BALSER. Not necessarily.

Mr. BOLTON. So that, obviously, the bank would take steps to see that they have qualified people to review the data processing equipment.

Mr. BALSER. Banking magazine, in an article that I quoted, had a paragraph which pointed out that the customer codifies the checks before they go to the banks, so that the bank has no responsibility for errors on that point.

Mr. BOLTON. I am sure that they have no legal responsibility.

Mr. BALSER. Right.

Mr. BOLTON. And I just ask you as an adviser of many businesses how long would you keep on going utilizing the service of a bank if that kind of thing kept cropping out?

Mr. BALSER. We run into that.

Mr. MULTER. It could be 4 or 5 years until the auditors complete the Internal Revenue Service check, and the customer would be faced with an assessment.

Mr. BALSER. We run into them all of the time.

Mr. TALCOTT. Mr. Chairman, there is a banker here who apparently will testify favorably to your bill.

Mr. MULTER. We are going to hear from him. If there is nothing further from these gentlemen, we thank you very much.

Mr. BALSER. Thank you.

(The following information was subsequently submitted for the record:)

NATIONAL SOCIETY OF PUBLIC ACCOUNTANTS,
Washington, D.C., March 16, 1964.

HON. ABRAHAM J. MULTER,
U.S. House of Representatives,
Washington, D.C.

DEAR REPRESENTATIVE MULTER: I believe you will be extremely interested in the enclosed booklet from the Chase Manhattan Bank describing a new "payroll accounting service."

This particular booklet has been called to our attention by quite a few of our members throughout New York State. Apparently the Chase Manhattan Bank has made a mailing directly to thousands of business and commercial firms.

This is an extremely timely development and clearly demonstrates that banks with increasing frequency are offering accounting and related services to the business community.

This development emphasizes the importance of early passage of your bill, H.R. 9548. Please be assured that you can count on the complete support of the National Society of Public Accountants.

Cordially,

STANLEY H. STEARMAN,
Counsel and Director of State Member Services.

THE CHASE MANHATTAN BANK

PAYROLL ACCOUNTING SERVICE

Preparing payrolls is an irksome, time-consuming and unprofitable chore for most businesses. Chase Manhattan's payroll accounting service will relieve you of this burden. This booklet discusses the reasons why you should consider using this service in your business. It also outlines the way the service operates and the many options available to you.

BENEFITS OF USING THE SERVICE

Paying its employees promptly and accurately is an important obligation of any business; but preparing its own payroll does not directly help a business produce and profitably market its products or services. Payroll preparation consumes time, energy, knowledge, and facilities that the business can often invest more profitably in directly serving its customers.

Here are some of the reasons why Chase Manhattan's payroll accounting service may be helpful to your business:

Lower costs

Use of specialized equipment and specially trained personnel usually permits the bank to prepare a payroll at a lower cost than the business can do it for itself. The fee charged for the payroll accounting service depends on the number of employees to be paid, and the range of payroll service needed by the business.

Privacy of payroll

Salaries of their associates are a subject of discussion among employees within any business. It's difficult to keep this information confidential. Fortunately, salary information is only of great "local" interest within the firm. The Chase Manhattan employees who will process your payroll are pledged to keep your salary information confidential, just as they do all the financial information that they process as part of their daily activities.

Use of Chase Manhattan's payroll accounting service means that fewer people within your firm need to know salaries.

Accuracy

The use of electronic computers and experienced personnel means that the bank can often prepare a payroll for an employer that is more accurate than one he can prepare for himself. This means that there are fewer misunderstandings and a reduction in the time wasted in correcting errors.

Promptness

When Chase Manhattan provides a payroll accounting service to one of its customers, the bank agrees to prepare the payroll on schedule. Again, the use of computers and specially trained personnel enables the bank to confidently assume its part of this obligation on behalf of the employer.

Elimination of peakloads and crises

Many businesses have to assign extra employees to payroll work during the time when the business' own work is at a peak. For example, preparing withholding statements sometimes comes during a crucial season for the business. Chase Manhattan's payroll accounting service solves this problem. The customer can assign his employees to the work that is most important to his business at any given time and remain confident that the bank will prepare his payroll and reports on schedule. This also applies to firms owning or renting computers where workflow scheduling may be interrupted by preparing a payroll.

Options for employees

Under Chase Manhattan's payroll accounting system your employees can choose either of two ways to receive their pay: (1) They can be paid by means of

an official Chase Manhattan check; or (2) they may elect to have their pay automatically deposited to their personal Chase Manhattan checking account.

Either of these options will have a strong appeal to your employees. They will appreciate the easy negotiability of an official Chase Manhattan check or they will be pleased with the convenience and prestige of having their own checking account at Chase Manhattan.

Chase Manhattan inplant banking service racks are also available to payroll accounting customers, without cost. With inplant banking your employees can transact practically all of their banking needs without leaving your premises. This is an extra convenience for them and you save the expense of long lunch hours or unofficial absence from work while their banking business is being conducted.

Flexibility

Nearly every business has certain payroll needs that make it unique. In designing and pricing its payroll service, Chase Manhattan has built into its program a high degree of flexibility that can be adapted to a wide range of payroll requirements. And by pricing separately each step in the payroll operation, the customer can select only those elements that he needs and thus keep his total payroll cost at a minimum.

PAYROLL COST CHECKLIST

Before offering this service, the bank conducted a survey to find out what it cost a cross section of businesses to prepare their payrolls and what type of payroll service was needed. One finding of the study was that many businesses are unrealistic about what it really costs to pay their employees. As a result of this finding, the bank developed the following checklist to help you determine the true cost of paying your employees.

In computing the present cost of performing your own payroll operation be sure to include the cost of all the necessary steps. Most businesses need to perform the following steps—yours may also require others:

1. Prepare wage and salary rate records.
 2. Prepare changes in wage and salary rate records.
 3. Prepare exemption and deduction records.
 4. Prepare changes in exemption and deduction records.
 5. Compute hours worked for hourly payroll.
 6. Compute special pay or special deductions.
- (NOTE.—You need to complete only the above steps under Chase Manhattan's payroll accounting service. The remaining steps can all be performed by the bank depending on the options you select.)
7. Compute gross wages for hourly payroll.
 8. Compute overtime.
 9. Compute statutory deductions.
 10. Compute or list voluntary deductions.
 11. Compute net pay.
 12. Prepare earnings statements.
 13. Prepare checks or obtain cash and stuff envelopes.
 14. Record salary data on employee ledgers.
 15. Prepare overtime or special earnings checks.
 16. Record cumulative salary data for year-to-date or quarter-to-date.
 17. Prepare salary expense distribution reports.
 18. Prepare FICA form 941A reports (quarterly).
 19. Prepare W-2 tax withholding reports (annually).
 20. Prepare IT-2102 tax withholding reports (annually).
 21. Reconcile payroll account and file checks.

Your accounting records may not show the costs of performing these steps. It's more likely that you have broad expense classifications that relate in part to the cost of payroll preparation. Expense classifications that you will want to include in your cost analysis will involve many of the following—and perhaps others:

1. Salaries and overtime of payroll department personnel (including management).
2. Social security taxes.
3. Unemployment taxes.
4. Disability insurance.
5. Hospitalization, surgical, and major medical insurance costs.

6. Group life insurance expense.
7. Pension costs.
8. Profit-sharing or thrift plan costs.
9. Temporary help.
10. Space costs (rent or depreciation, taxes, etc.)
11. Heat, light, power.
12. Telephone.
13. Maintenance.
14. Equipment and office furniture.
15. Machine repair and maintenance.
16. Supplies (ledgers, worksheets, report forms, checks, machine supplies, tax forms, etc.).
17. Bank service charges on payroll account.

Be sure you are realistic in assigning a portion of your management's time allocated to payroll supervision.

When you have computed your total annual cost of the payroll function in your business, divide it by the number of payments you make to your employees to derive the cost per check. We believe that you will be favorably impressed with the savings gained by using the service from Chase Manhattan when you compare our fees to your costs; and when you add on the other benefits of using the service—privacy, accuracy, promptness, elimination of peakload crises, and orderly, quick and convenient reports, we feel sure you will be convinced that Chase Manhattan's payroll accounting service can help your business.

HOW CHASE MANHATTAN'S CUSTOMER PAYROLL SERVICE OPERATES

Initial information needed

The customer provides the following data on each employee covered: 1, name; 2, address; 3, social security number; 4, employee number; 5, department or expense code; 6, basic salary rate; 7, tax dependents; 8, voluntary deductions; and 9, year-to-date salary data.

Data changes

When any of this data except the last changes, a data change form is prepared. Or, as employees are added, the data change form is prepared listing the above information. You need supply the basic data only once; Chase Manhattan performs the repetitive tabulations with the accuracy inherent in a computer installation.

Each pay period you compute the regular and overtime hours for your employees and total these to provide a proof for the pay period. This may be done on the timecards you are now using or on your present timesheets provided that they meet the requirements of the service. However, most businesses will prefer to use the preprinted Chase Manhattan timesheet record for this purpose. The bank's payroll specialists will help you develop the most efficient method of preparing this input data.

From this point, Chase Manhattan takes over your payroll function—computing gross pay, involuntary deductions, voluntary deductions, and net pay due each employee. At the employee's option, either a Chase Manhattan official check or a deposit receipt is prepared along with his complete earnings statement. A payroll register listing all the data on each employee is also prepared. Chase will deliver your completed payroll 48 hours after receipt from you of the necessary payroll information. We will charge your account for the total net salary expense for the pay period plus the fee for performing the service.

At each quarter end Chase Manhattan will prepare for you, if you wish, the required FICA (social security) report on form 941-A. At yearend the bank will also prepare, at your option, your W-2 and IT-2102 withholding tax reports.

If you wish, a labor distribution by department or other classification can be provided.

You will be relieved of all of the tedious, time-consuming part of the payroll function. You will receive prompt and accurate reports in convenient form. You will not need a separate payroll account and will be relieved of reconciling it. Should you need a copy of any check, Chase Manhattan will supply it.

Customer options

In order to make available to each payroll accounting customer the payroll service tailored to his specific needs, the bank offers a complete range of options. Payroll service is available for hourly employees, salaried employees, or a combi-

nation of both. We will prepare weekly, biweekly, semimonthly, or monthly payrolls.

If you prefer to compute your own payroll to the point of net salary we will complete the payroll from this point.

Tax reports are separately priced so that you may perform this portion yourself if you choose.

Pickup and delivery of the payroll data and/or completed payroll is also available.

In short, the service gives you maximum flexibility in selecting just the elements that meet your requirements. Our payroll specialists will be happy to discuss your requirements and any options with you.

Fees

The cost to you depends on the number of employees covered and the degree of activity and scope of service you require. Again, our payroll specialists will be happy to review our fees with you and help you analyze your present payroll costs.

CUSTOMER SERVICE CENTER

Visit our customer service center at 1 Chase Manhattan Plaza. You can inspect our modern equipment and observe the efficiency of Chase Manhattan's payroll accounting service. Payroll specialists will be there to discuss our payroll accounting service.

SUMMARY

Chase Manhattan's payroll accounting service is designed to meet the individual needs of its customers. Call your friend at Chase Manhattan to learn more about how we can help you pay your employees promptly and accurately, keep your salary information confidential, and reduce your payroll costs.

Mr. MULTER. Has Mr. Browning come in? Will you come forward, sir?

Mr. LLOYD. I wonder if I may have the privilege of introducing my friend to this committee?

Mr. MULTER. Certainly.

Mr. LLOYD. The name Browning is a great name in the West, particularly in our State. It is somewhat rare, when a man of great affluence and influence will subject himself to a political campaign. This is a case where a man of great stature in the State has not only been willing to sit on the sidelines and to advise, but to submit himself to the political processes. I had the pleasure of serving in the Utah State Senate with him. Although we were on opposing political sides, I consider him a personal friend, and I would like to welcome him to this committee.

Mr. MULTER. We are very glad to have you here.

STATEMENT OF FRANK M. BROWNING, CHAIRMAN OF THE BOARD, BANK OF UTAH AND BANK OF BEN LOMOND, OGDEN, UTAH

Mr. BROWNING. Mr. Chairman and members of the committee, you can see why Congressman Lloyd is respected in our community. I looked up to Sherman as the president of our senate. I sat on the minority side. He carried the deep love and affection of everybody on both sides of the aisle due to his great sense of integrity and fairness. It was nice of you to say what you have. I do want to say that it is, indeed, an honor to bask in your glory here.

Mr. MULTER. We respect him here, too, even though here he is on the minority side.

Mr. BOLTON. Temporarily. [Laughter.]

Mr. BROWNING. My name is Frank M. Browning. I am organizer and chairman of the board of the Bank of Utah and the Bank of Ben

Lomond, both in the Weber County area in the northern part of the State of Utah. These two institutions would be classified as independent banks.

My background, other than banking, includes being presently a Utah State Senator, having served approximately 12 years; and former director of the Federal Reserve Bank of San Francisco, Salt Lake City Branch. These activities, along with oversea service in two World Wars and at present on retired Army status; and as organizer of various corporate activities in the development of our area, cover my background.

I appreciate the opportunity of appearing before your honorable committee to express my views as to the need for legislation to control unwarranted activities that we, as independent banks, have had to face since the introduction of automation.

I would want to clarify first, that neither I nor my associates are fighting the trend of expediting bank accounting processes. Our own institutions have laid groundwork to the approach for complete automation and our final installation of computers will be made this summer. We hope to confine its use to banking.

We are deeply concerned about the abuses which have entered into the use of this revolutionary change, which I shall attempt to cite clearly.

Many larger banks rushed into the installation of these high-priced units and in some cases have reached far beyond ethical practices in obtaining nonbank business either to cover the cost of excessively large computers or to compete unfairly with smaller banks. An example of such practice is that certain banks have taken over the payroll functions of large school districts.

I want to clarify what I consider are ethical approaches to bank participation in payroll account processing and what I consider to be an unethical approach.

I would hasten to make clear that not all banks have unethically abused this practice. I am citing our experiences as an indication wherein banks and bank control regulatory agencies are headed for trouble and unlimited calls for more and more laws pyramiding onto the present legal crazy quilt pattern.

In the case of our institution, we have been successful through supporting progressive education in maintaining friendly customer relationship and were favored with our share of teachers' depository checking accounts. My own record in the State senate, where I have successfully spearheaded educational legislation, has placed us close to our teachers' groups.

Our larger competitive banks, in order to spread the cost of computers into other areas (I think that is putting it nicely) have padlocked all school board payroll accounting by creating a captive account in the name of each individual employee and then crediting this account with the employee's monthly earnings. This is a joint arrangement between the banks and the allied school boards. This is where the great danger comes in, the allied school boards. The penalty to the taxpayer is that these banks demand the public institution maintain a large frozen bank account to compensate for their cost. The tax burdened citizen should soon be aware of his hidden frozen tax dollar.

If this had been handled as the Federal Government handles its employees, wherein the Government agency asks the individual where his check is to go, other banks could not have been hurt—even though we question the propriety of this revolutionary activity on the part of privately owned financial institutions.

In the cases that I have cited, our school boards and the banks capture the teachers' salaries by a very sinister approach. They state to the schoolteacher that his earnings have been credited to an account at their bank and in all fairness, they will allow the recipient to transfer it to the bank of his choice by making out another check. There is at least a 3-day delay before the wage earner actually knows how much has been credited to his account because of miscellaneous deductions. This confusion, along with having to transfer his funds each month makes personal accounting more complicated than ever, and gradually we have found that in spite of all our efforts to convince the teachers that they should follow this extra procedure, in the end we have lost the accounts except in cases of a few dedicated individuals who appreciate what we have done for their cause. That is what they commonly describe as captive accounts.

I presented our case against this unethical procedure to the Federal Reserve authorities in San Francisco and all they would offer was the thought that the staff offered their sympathy, but the procedures did not violate any existing law. We understand now that it does violate a Federal antitrust and restraint of trade law. They offered no help at all to bring it up to the Board of Governors to see if there could not be some law set up to protect the little bank in that respect.

I am positive to this date that no one on the Federal Reserve staff attempted to differentiate (here in the important point) between allowing the employee freedom of choice as to his bank, as the Federal agencies do in their payroll procedure, or being regimented in a captive group.

Other banks, with a more ethical approach, have also reached into payroll activity, but they have followed the ethical and dignified procedure established by the Federal Government in allowing the employee to select his own bank. In other words, the paying bank would credit so many accounts over in John Doe's bank, and that would take care of that group, and that is all there is to it. Conforming to the more ethical approach, the aspiring bookkeeping bank would still carry a monopolistic advantage in having first chance to tie up all payroll personnel. In other words, the recipient, the janitor, the teacher, has got to go there to initiate his banking. And they have great leverage in a lot of cases, because a youngster, for example, is just growing up and starting his first account. There is a terrific advantage to the paying bank.

To sum up all of this to your honorable committee, I am sure that what I have offered will indicate the terrific responsibility that our controlling agencies will have to assume to keep ambitious banks from injuring smaller banks and professional people in carrying out their responsibilities.

I might add, Mr. Chairman, not only does it involve the bank's capital and much risk in case of errors, and the loan officers and loan committees could be put under pressure by the favored bank to authorize substandard risk loans.

The historic function of a bank is to properly and ethically handle depositors' funds. Assuming accounting responsibilities, direct and contingent, that do not properly belong to a bank, subjects a bank to great and unreasonable risks. Even the best national accounting firms are now frightened to directly verify their reports as a result of recent scandals; namely, the vegetable oil exposure. They can put all of the computers to work in the world, but in the final outcome you will find a decision has to be made by the members of the loan committee, the directors, in the bank—the final factor there is the integrity of the man on top of the tank who was supposed to let the weight go down to the bottom of the tank. I mention that, because you cannot shake off that responsibility. Can the terrific burden of responsibility on banks justify this certain peril?

I foresee that bankers could be subjected to severe pressure in granting questionable loans. This threat could occur by officers of corporations, whose accounting work is done by the bank and as a result of this, the bank obtains several hundred employee accounts. The threat of transferring these captive employee accounts to a competitive bank may result in heavy pressure on bank loan officers to compromise their credit judgment in making unwise loans.

This is merely one segment of terrific problems which will arise if this process is not harnessed right from the start.

I call your attention, Mr. Chairman, to the great complexity of the banking laws that now exist that are set up to protect mostly the things in the background, the shadow of the contingency. And if we go off in this unexplored sea with all of its shoals you can imagine the time that will be spent in studying legislation to control it. This is unlimited in its scope. And there are other risks that will develop faster than laws can be made.

The complicated, highly competitive financial world today, as exemplified in banking, can ill afford to be neglecting their terrific responsibility in guarding the widows funds by reaching into the activities and assuming risks that properly belong to other businesses and professions.

From the sublime to the ridiculous, I love to use the expression, "We should kick the bookkeeper's stool from under the banker and put him back in monetary responsibility. Therein lies an unlimited field, deep with many problems."

Thank you.

Mr. MULTER. Thank you very much. Are there any questions?

Mr. LLOYD. I would like to say, Mr. Chairman, that Senator Browning speaks from the greatest personal experience. And I know that what he has said here is verified by the facts.

As to how this particular legislation might get to the problem of captive accounts of school boards. Do you feel that this bill would somehow or other attack that problem? I cannot see where it would.

Mr. BROWNING. You called me Frank and I will call you Sherman. Sherman, it would, in my estimation, because it is starting to take the banks out of the bookkeeping business directly and indirectly. Your committee should know and the public should know that these bookkeeping banks insist frozen balances of the taxpayers' money be kept in the bank for its profit to compensate for the bookkeeping help. And I would say that this legislation would stop it.

Mr. LLOYD. In other words, you would feel that if it did not stop it directly it would have a healthy effect?

Mr. BROWNING. That is right.

Mr. LLOYD. One of the problems which we have and which I personally have is the language that permits the bank to perform these functions to the extent that such services are a necessary incident to the proper discharge of the lawful functions of the bank.

It occurred to me that we are getting into a maze when we attempt to interpret what is necessarily incident to the proper function of the bank.

I will conclude with the statement that Senator Browning's testimony should be taken with the utmost seriousness. I, for one, certainly will.

Mr. BROWNING. Thank you, sir.

Mr. MOORHEAD. I want to state that Senator Browning has been very helpful and very persuasive with his statement.

Mr. BOLTON. Mr. Chairman, I, too, appreciate the Senator's testimony. Although I had to go outside, I have had a chance to review his statement.

Do I understand, sir, that you would not object to those banks who handle such an accounting as you referred to, a more ethical approach to it, where the person could designate whatever account he wanted his funds deposited in?

Mr. BROWNING. When I appeared here today, first of all, it was to try to speak a word against the terrific evil. Time will have to take care of it. Frankly, I believe that in my last closing statement that the faster we can get banks right back to banking, the better off we will be and we will least embarrass our loan boards.

I heard discussion this morning about statements supporting a loan. The final answer had to be that of men. In fact, Mr. Chairman, I would not have been in business if we had taken the computer's financial statement at the time I started with nothing.

And I think that these things are all going to deprive the responsible loan boards and board of directors of that great responsibility they have, not only in the figures that are submitted, but in the knowledge and experience of these individuals applying for the loan.

Mr. BOLTON. Thank you, sir.

Mr. HALPERN. I have no questions.

Mr. MULTER. Senator Browning, would it help if we amended this bill that is before us by putting in a specific prohibition against these

captive accounts and a specific prohibition against this unfair competitive practice by these agencies, whether they are government or otherwise. We could prohibit banks from taking these accounts and paying the payees for their employers. Would that help the situation?

Mr. BROWNING. That is right. We are about 65 percent automated in our small banks. We are going the full way. We have no desire to set up accounting systems or anything that would put us out on a limb, an exposure, as a matter of ethics, with these people who are well trained in their profession.

Mr. MULTER. We cannot regulate State or local governmental agencies. Is it likely to lead to political corruption to permit a local governmental agency to pick one bank and say, "This bank will receive all of our funds and hold all of our funds and pay all of our employees."

Mr. BROWNING. It is a greater exposure.

Mr. MULTER. There is a temptation there, surely.

Mr. BROWNING. I am sure that it would happen.

Mr. MULTER. Thank you very much.

Mr. BROWNING. Thank you.

Mr. MULTER. Our next witness is Mr. Robinson. We are pleased to have you with us. You may read your entire statement, or you may summarize it. You may proceed as you desire.

STATEMENT OF HERBERT W. ROBINSON, PRESIDENT, ADAPSO, AND ALSO PRESIDENT, C-E-I-R, INC.

Mr. ROBINSON. Mr. Chairman and members of the subcommittee, my name is Herbert W. Robinson, president of ADAPSO (the national Association of Data Processing Service Organizations) and also president of C-E-I-R, Inc., a publicly held company with data processing centers in Boston, New York, Washington, Los Angeles, and San Francisco, as well as overseas. I want to take this opportunity to express my appreciation to the subcommittee for the privilege of appearing in support of H.R. 9548.

The extent to which the larger banks are moving into the data processing business is of concern not only to the members of our association, but, in my opinion, to the whole country. Having been in the business of providing data processing services, including computer time, systems design, and programming, from the inception 10 years ago of large scale commercial computers, I would like to take a few minutes to describe the nature of our business—one of the few new frontiers for small and independent businesses.

ADAPSO has upward of 60 member firms in numerous locations across the country, all of whom are engaged in providing computer services mainly to businesses which are not large enough to establish in-house capacity. Most of these firms have been organized by pro-

gramers, business data processing experts, statisticians, and economists with computer experience. In some cases, they have grown to national dimensions. In others, they have continued on a local basis for the purpose of providing professional services to businesses in a single community. Well-established organizations like C-E-I-R own or lease even the largest computers as an adjunct to the professional programming services which they provide and also as a source of machine time for processing business and scientific data. Smaller data processing business have had tabulating installations and have utilized time on other larger computers in the vicinity; recently they, too, have been installing smaller electronic computers in their own facilities.

On behalf of the members of ADAPSO, I am here to testify in favor of H.R. 9548 and, in view of recent developments, to recommend that its scope be broadened to prohibit banks expressly from engaging in the general data processing and computer business except for their own internal operations. As you know, banks have traditionally enjoyed protection and Government assistance. As a corollary, the Government has imposed restrictions designed to protect the funds of bank depositors. For example, to preserve the liquidity of bank deposits, strict requirements have been established governing the use of such funds, such as minimum collateral, interest requirements on loans, the nature of acceptable collateral, etc. To this end, banks have always been precluded from engaging in nonbanking business except by express statutory consent and then only when such business is inseparable from the banking business—the right to own real estate, for example, was only granted as a necessary corollary to the right to lend money on real estate. Clearly, general data processing services constitute a separate and distinct business from banking operations and there is every reason why this area of business enterprise should be no exception to the general rule.

Thus, 2 years ago, H.R. 8874 was introduced to permit banks to establish subsidiaries which would own or lease computers and provide data processing services to banks. As originally written, the bill would also have permitted such bank service subsidiaries to provide up to 50 percent of their services to persons other than banks, that is, to engage in the commercial data processing business for the general public. Because of the hazards involved and the unfair competitive practices which I will discuss later, the Senate amended H.R. 8874 to restrict bank subsidiaries to furnishing data processing and computer services exclusively to banks. As so amended, the bill was enacted as Public Law 87-856. The rationale of the amendment, as expressed in the Senate committee report and the floor debate, was that banks should not, through subsidiaries, engage in commercial business which would have been improper as a direct bank activity. Notwithstanding this statute, a number of banks during the past year have purchased

or leased some of the largest computers available and have immediately advertised aggressively for commercial data processing business. (Some examples of these advertisements are appended to this statement.) These banks apparently assume that Public Law 87-856 applies not to banks but only to bank subsidiaries, an assumption clearly contrary to the expressed intent of Congress.

It is true that computers are necessary for internal bank accounting operations. However, any contention that banks need to sell excess computer time and data processing services to the public in order to operate economically is untenable. This completely ignores the fact that computers can be bought or leased in all sizes and shapes; that leased equipment from most hardware manufacturers, including IBM, can be terminated on 30 to 90 days' advance notice without penalty; and that at any one time the capacity installed therefor need be no greater than the bank's requirements for its own internal accounting operations.

Excess capacity is extremely expensive. Let me give you at this point a few figures on the cost of computers. At least a dozen of the largest banks in the country, most of whom are advertising for commercial data processing, have installed large machines which cost about \$3 million, and rent for approximately \$70,000 per month for first shift usage. The more popular smaller machines cost about \$300,000 and can be rented for about \$7,500 per month for the first shift. Beyond the aforesaid first shift rentals, a lessee of computers pays for additional usage on an hourly basis at 40 percent of the first shift cost. (The first shift is essentially 40 hours per week, or 176 hours per month.) Moreover, the cost of establishing a large computer operation is not limited to the rental or purchase price of the computer itself. The larger computers require expensive computer rooms with special air conditioning, false flooring, etc. Such a computer area will often cost from \$50,000 to \$100,000. Expensive operating personnel and program library support are also required. A competent programming staff is especially costly, particularly if it is sufficiently skilled to handle broad gage computer problems in addition to the banks' internal operations.

To the extent banks depart from the banking business, where safeguards and legal limitations of liability have been developed to protect the funds of depositors, installation of excess capacity to venture into the field of providing commercial computer services is subjecting depositors' funds to substantial risks. Moreover, this field is one where legal liability for damages can be extremely high. You may recall, in the summer of 1962, a multimillion dollar missile shot from Hawaii misfired and the malfunction was traced directly to an error in the computer program. Equally serious consequences can occur in the financial and business world. Inasmuch as computers are used in all areas of business activity, the potential damages arising from faulty

performance of data processing operations can be disastrous. These are substantial threats to the inviolability of depositors' funds.

The committee should also take into account the fact that the larger banks can use electronic data processing services as an economic weapon to capture the business of the small banks who cannot afford such equipment and of those banks who believe they should remain solely in the banking business. Moreover, banks have many built-in advantages plus the ability to sell at cut-rate prices and to exert intangible pressures upon borrowers and depositors to capture the business being done by the commercial data processing firms and the accountants. There is thus a real danger that the smaller banks as well as data processing service organizations and accountants will ultimately be driven out of business.

There is another subtle but, in the long run, perhaps more dangerous problem in permitting banks to engage in this business. Should the large banks succeed in obtaining control of most of the commercial data processing activity in this country, they will have records and statistics at their command covering, in minute detail, every aspect of industrial and commercial life. Combined with the power to give or withhold credit to individual enterprises, and to channel large investment funds, this concentration of power could well be dangerous in the wrong hands.

To sum up the position of ADAPSO:

Banks need install only enough equipment to meet their own requirements. There is no reason why they need undertake commercial data processing as an adjunct to their legitimate internal banking operations and many reasons why they should not. Commercial data processing service organizations and accountants are already meeting the needs of the community for these services. Unfair competition from the large banks will drive small banks, commercial data processing organizations, and accountants out of business. Moreover, as I have pointed out, to allow banks to engage in this business is against public policy in that it jeopardizes depositors' funds, puts the bank into an unrelated and hazardous enterprise, and enables banks to use their economic power to tie in the sale of data processing with the provision of normal banking services. Congress recognized these facts when it enacted Public Law 87-856, limiting bank subsidiaries to the performance of computer services for banks exclusively. Additional legislation restricting the banks themselves from engaging directly in the commercial data processing business is now urgently needed.

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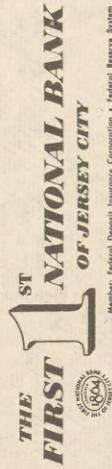
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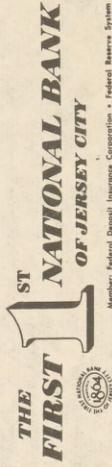
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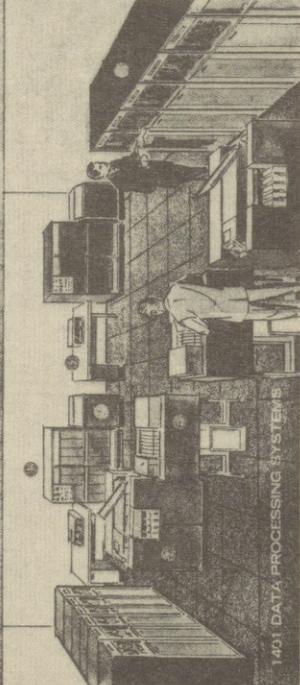


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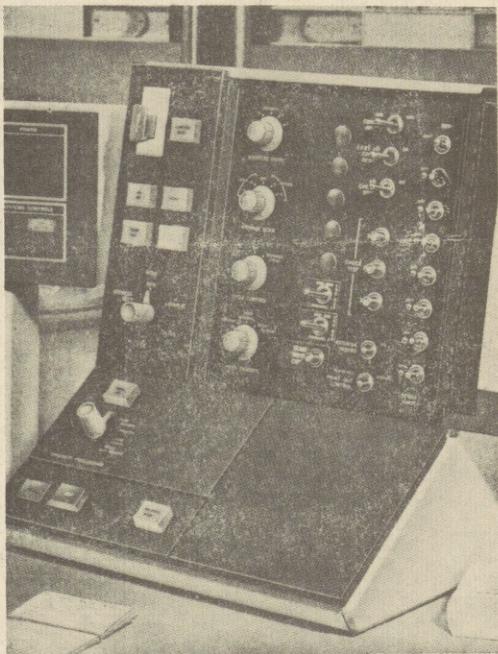
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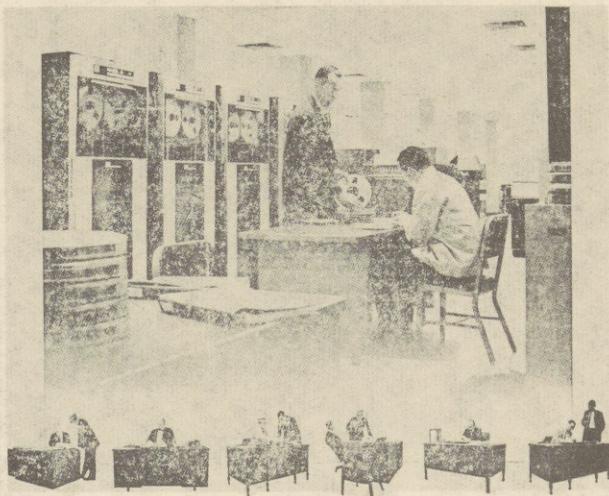
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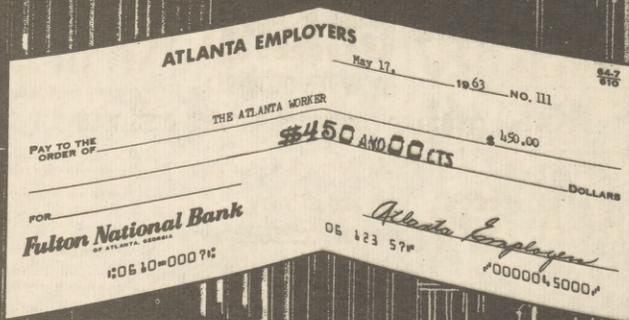
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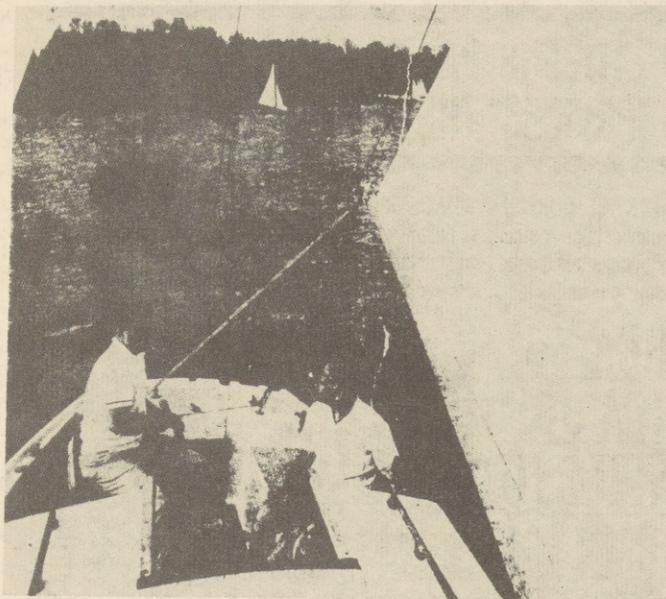
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Mr. MULTER. Thank you very much, Mr. Robinson. Our time has just about run out this morning. As to the next to the last exhibit attached to your statement, will you submit to us for the record a clear copy that can be reproduced?

Mr. ROBINSON. I certainly will.

Mr. MULTER. Are there any questions?

Mr. BOLTON. I have just one question, Mr. Chairman. You mentioned the fact, Mr. Robinson, that a bank would have through its data processing a great deal of confidential material regarding the commercial and industrial world. Is there any limitation upon ADAPSO on the spreading of the information that the members of the association have?

Mr. ROBINSON. Yes, sir, by our code of ethics we undertake to preserve the confidentiality from anyone of any data which is entrusted to us for processing.

Mr. BOLTON. And is that in the contract of anybody who uses the services of one of the members of ADAPSO?

Mr. ROBINSON. Normally, the customers do not insist in putting that in the contract. They usually have confidence in our service.

Mr. BOLTON. Thank you.

Mr. MULTER. You hold it in confidence?

Mr. ROBINSON. Certainly we would. Of course, many of us are working on secret and top secret contracts for the Government. There again is an added warranty that we would do so.

Mr. MULTER. That is a provision of the contract with the Government in every instance?

Mr. ROBINSON. It is a part of our security regulations, that is right.

Mr. MULTER. All of your employees in those cases are checked for security?

Mr. ROBINSON. Exactly.

Mr. MULTER. Thank you very much, sir.

The committee will meet again tomorrow morning at 10 o'clock to continue these hearings. I would like, if possible, to have each of the other witnesses scheduled for today return tomorrow and present his testimony orally. However, if any witness cannot come back, we will convenience him by making his statement a part of the record at this point, reserving the right for any members of the subcommittee to submit questions in writing which, when answered, will be made part of the record. Is there any witness who has been scheduled for today who cannot be present tomorrow?

Mr. ARMSTRONG. My travel orders from my president did not include tomorrow. If it would be in accordance with your procedure I would like very much to submit my statement, and then if I cannot be here tomorrow it will be in the record, but if I am wanted by the subcommittee for questions I will return tomorrow or at any other time.

Mr. MULTER. We will make your statement a part of the record at this point.

Mr. ARMSTRONG. Thank you, sir.

Mr. MULTER. If you can stay over and return tomorrow, we would appreciate it.

Mr. ARMSTRONG. I shall, certainly, try to do so.

Mr. MULTER. If not, we will address questions to you by letter.

Mr. ARMSTRONG. Thank you very much, sir.

Mr. MULTER. We are very sorry that we could not get to you this morning.

(The prepared statement of J. Sinclair Armstrong, executive vice president, U.S. Trust Co. of New York, follows:)

STATEMENT OF J. SINCLAIR ARMSTRONG, EXECUTIVE VICE PRESIDENT,
U.S. TRUST CO. OF NEW YORK

My name is J. Sinclair Armstrong, my home is at 211 East 18th Street, New York City, and I am executive vice president of the U.S. Trust Co., of New York, 45 Wall Street, New York City.

My colleagues at the trust company and I very much appreciate the opportunity afforded me to express our views on H.R. 9822, entitled "A bill to prohibit banks from engaging in the business of personal property leasing," and H.R. 9584, entitled "A bill to prohibit banks from performing certain nonbanking services." As one who has in earlier official capacity frequently testified before other committees of the House of Representatives, it gives me great pleasure to appear before the Subcommittee on Bank Supervision and Insurance of the Committee on Banking and Currency.

The U.S. Trust Co. of New York, a banking institution chartered by the New York Legislature in 1853, has specialized for 111 years in trusts and investment management for individuals, members of families, and religious, educational and charitable institutions of all kinds, and for pension, and retirement funds of corporations, employee associations and labor unions, and a number of public authorities, including the State of New York. The trust company is a member of the Federal Reserve System and the Federal Deposit Insurance Corporation, and is under the regulatory jurisdiction, as well, of the superintendent of banks of the State of New York.

Gentlemen, I speak on behalf of the trust company in opposition to these bills.

The first, H.R. 9822, would prohibit a bank from leasing any personal property under any circumstances or by any means as a result of which it performs or is compensated for any services other than the lending of money or advancement of credit with respect to such property, or acquires any interest in such property other than as security for the repayment of money or credit advanced together with interest and other charges for exclusively financial services, or may realize from such property in the event of default more than such repayment and charges.

The second, H.R. 9548, would prohibit a bank from performing any clerical, administrative, bookkeeping, statistical, accounting, or other similar services for its depositors, borrowers, or other customers, except to the extent that such services are a necessary incident to the proper discharge of lawful functions of such bank as a depository, lender, trustee, or agent.

Your committee's release of February 12, 1964, adds: "The subcommittee will also consider the advisability of enlarging these bills to exclude the performance of all nonbanking services by banks for depositors and others with or without compensation."

The interest of the U.S. Trust Co. of New York in presenting these comments, which will be brief to conserve the committee's valuable

time, comes from our wish to be helpful and constructive. We make these comments from the point of view of the national public interest.

This committee will want to base any legislative action on a clear record of need for legislation in the public interest. The banking industry provides one of the most vital elements in our Nation's economic well-being and growth. It is one of the most tightly restricted, highly regulated, and competitive industries in our Nation. This committee, which has as its concern the proper functioning of our banking system, will not wish to impose unnecessary shackles on it in the absence of a convincing showing of abuse that requires correction to protect the public.

The language of these bills is very broad, and their meaning is not very clear. At present, there is no disclosure of what abuse, what practice, the bills seek to prevent or to correct. One can testify on them only by making certain assumptions. One can fear that the bills, if enacted, could deprive the public of services which they look to banks to provide and which they may never be able to get unless banks provide it.

With respect to H.R. 9822, the assumption is that its purpose is to prohibit banks from leasing out unused time on their computers, and I shall deal with the bill on that assumption. The bill must proceed from a belief that it is contrary to the public interest for a bank to lease unused time on a computer it owns or rents, but that it is not contrary to the public interest for any other owner or renter of a computer to rent its time out to the public. In other words, it discriminates against banks having unused computer time, and in favor of corporations or others having unused computer time. In so doing it will prevent banks from owning or renting computers unless they can afford to absorb the expense of unneeded time. The convenience and service to others who might not otherwise be able to gain access to any computer will be denied to the public. Even more basically, so to restrain the use of privately owned personal property, without any showing of danger to the public interest or welfare, is a very drastic interference with traditional American freedoms.

We believe that banks should be permitted to make their data-processing equipment available to third parties for a consideration. We think that this activity is entirely proper. Ordinarily a bank will acquire data-processing equipment primarily for its own use. The acquisition of such equipment is demonstrably needed by banks today in performing their functions as banks, and the equipment is expensive. Against that background, if open machine time on computers is available, we see no reason why a bank should be forced to leave its expensive equipment idle, and we see many benefits to the public from banks making unused computer time available. The enactment of H.R. 9822 would make it more expensive and, for many smaller banks, perhaps impossible to buy or lease expensive equipment needed in order to serve better the banking needs of the public.

Speaking for the trust company, we have over \$1 million of our stockholders' capital invested in computers and we spend over half a million dollars of annual expense in connection with them and other rented electronic equipment. Our operations are not yet fully converted to computer use, but we are working toward that objective as hard and as fast as we can. We have leased out time to others, and

we would like to do so more if, when our operations are fully converted to computers, there is free time left on them. This will help reduce our net cost for the equipment and confer a benefit on others whose need for time is small and who otherwise might have no chance at all to get on a computer. So we urge you not to pass H.R. 9822.

Now let me turn, briefly to H.R. 9548. Here I must assume that tax report and payroll preparation by banks are under scrutiny.

The preparation of income tax returns is performed mostly by trust companies and the trust departments of banks. It is not a service offered to the public as such. Rather, it is an adjunct to the overall care of a customer's financial affairs which has been entrusted to the bank when the bank acts as fiduciary of family trusts, as investment adviser or manager for an individual portfolio, or as custodian for securities. From the investment point of view, the tax status of a beneficiary of a trust or the holder of an investment management account is of prime importance. It has a bearing on what kinds of investments should be held and what transactions made. Many customers of trust departments have their remittances budgeted after provision for real estate and income taxes, and so, in any intelligent and effective approach to a fiduciary customer's finances, it is necessary for the bank to be brought into the picture on the tax computation as well.

In the case of trusts, the Federal tax law requires the trustee to prepare fiduciary tax returns, and it is only a logical extension of this legal requirement for the bank to prepare the beneficiary's individual return if he wishes. Being in possession of information leading to the determination of an individual's gross income, the banking institution is best qualified, with least expense to the customer, to prepare the personal returns. This is especially true in the usual case when the only missing element is that of personal deductions. This is a vital service to customers of our trust company and one to which we feel that they are entitled.

It should be noted that it is very much in the interest of the Government that banks compute customers' taxes and prepare their returns. It makes for accuracy of tax reporting and prompt payment, and reduces the enforcement burden on the Internal Revenue Service. At the trust company we remit many millions of dollars on behalf of fiduciary customers whose returns we have prepared, and we are very proud of our record of accurate tax reporting.

Now I will turn to the payroll services. Corporate payroll and bookkeeping chores, according to our experience as a trust company, are primarily performed for charitable organizations as distinguished from business corporations. Charities very often engage the custodial and investment advisory capacities of a trust company largely because such an institution is in a position to perform emunerated services at a fee which is much less than would be the cost if the corporation were to maintain a staff of its own for those fiduciary and ministerial functions. Under Federal law and otherwise, charitable organizations are being called upon more and more to make a disclosure of their activities and to render reports of their financial affairs. It is therefore not unusual, in fact almost to be expected, that charitable organizations will call upon their banks to render bookkeeping and payroll paying services.

Performances by banks of payroll service to corporations may become very important in the years ahead. We think that the complexities of modern payrolling will make it a necessary bank service, especially to small and moderate-size businesses, for which their own payrolling is expensive and burdensome. Technically, payrolling is bound to come to computers, and only by using computers of others will small businesses be able to keep their payroll work from becoming very expensive.

Think for a moment of the computations and deductions that have to be made in today's complex payroll preparation and reporting. The Federal laws require employer withholding for employees' income taxes and social security payments (FICA), and employer reporting on them. The Treasury Department urges employers to withhold on a voluntary basis for savings bonds. In New York employers are required to withhold for employees' New York State income taxes. Further, by collective bargaining agreement or other arrangement, many employers withhold for labor union dues. Beyond that, voluntarily, many employers withhold for contributory pension, group life insurance, and medical and hospitalization plans, and for savings deposits. Finally, in an era when social responsibility permeates our entire society, many employers voluntarily withhold for community service agencies—in our city the Greater New York Fund.

The complexities of a payroll for the small business are a great burden. More and more they are turning to their banks for assistance. We, at present, are providing this service for one moderate-size brokerage firm and one mutual savings bank, and we hope to be called on by other customers who find it expensive, burdensome, and technically beyond their capability without great expense to them. We believe that this is clearly a proper role for banks to perform in the interest of the public.

It might be argued that the exception clause in the bill would make it harmless. We think not. The bill makes it seem as though a bank is skirting illegality every time it engages in an activity described even though for a depositor, borrower, beneficiary, or principal. It would have to stop, look, and listen each time to determine whether an act was "a necessary incident to the proper discharge of its lawful functions as a depository, lender, trustee, or agent." We see no public interest requiring the Congress to place this added burden on banks, or to place the added burden of policing the prohibition on the supervisory agencies. The Congress should not pass a prohibition to stop practices which are clearly consistent with the banking industry's objective to serve the public well. So we urge the committee not to approve H.R. 9548.

Mr. MULTER. Is there any other witness who cannot return tomorrow?

Mr. ARMSTRONG. I will try to be here if I possibly can.

Mr. ZISES. I am sorry that I will be unable to return. My statement is available for the record.

Mr. MULTER. Your statement will be made a part of the record at this point. Your statement is in support of H.R. 9822?

Mr. ZISES. Yes, sir.

Mr. MULTER. I am sure that the members were looking forward to hearing your testimony orally, but if you cannot be here we will make

your statement a part of the record as requested. The members may if they desire, submit questions to you in writing.

Mr. ZISES. I will be delighted to answer any questions. Thank you.

Mr. MULTER. Thank you very much for coming in.

STATEMENT OF ALVIN ZISES, ON BEHALF OF THE ASSOCIATION OF EQUIPMENT LESSORS, INC.

Mr. ZISES. My name is Alvin Zises. I am a member of the board of directors of the Association of Equipment Lessors, Inc., which is a nonprofit membership trade association composed of companies engaged in the leasing of all variety of equipment to industrial and commercial lessee users. I am, also, president of Bankers Leasing Corp. of Boston, Mass. I appear here as the representative of the association to place before this subcommittee our views concerning H.R. 9822, a bill to prohibit banks from engaging in the business of personal property leasing. On behalf of the association, we appreciate very much the opportunity to appear here today.

We heartily endorse H.R. 9822 as being not only in the public interest but also in the best interest of banks themselves. We urge its enactment for the basic reason that personal property leasing has never been, is not now and should not properly be part of the banking business. Moreover, banks should not be permitted to engage in commercial enterprises by mere administrative fiat, but only by act of Congress, particularly when such an authorization overturns almost a century of settled practice and established legal principles.

The question of banks engaging in the business of personal property leasing is a very complicated subject, bristling with legal and practical problems for banks. If I undertook to discuss its many ramifications here today, I would impose unduly upon the time of this subcommittee. I have just had published in the most recent issue of the Bankers magazine a rather lengthy article entitled "Equipment Leasing by Banks—Problems and Solutions." This article deals with many of the problems which are raised when banks undertake to engage in a commercial venture such as equipment leasing. It also analyzes the authority of national banks under the National Bank Act and concludes that the Comptroller of the Currency's ruling authorizing national banks to purchase personal property for simultaneous leasing is an unwarranted and unauthorized and illegal extension of the power of a national bank.

I would like the chairman's permission to submit a reprint of this article for the record. The entire article is germane to the subject matter of this hearing. By submitting the article for the record, instead of reading a similar statement to the subcommittee, a great deal of the subcommittee's time will be saved.

In addition, I would like to summarize here the substance of our reasons for favoring the enactment of H.R. 9822. Finally, if I can answer any questions that the subcommittee may have concerning this subject, I shall be glad to do so.

We favor the enactment of H.R. 9822 because the direct leasing of equipment by commercial banks is contrary to sound economic principles, Federal and State law, and the public interest.

1. According to Professor Shaw, of De Paul University, the very purpose of the National Bank Act was to keep banks "in the commer-

cial banking business—that is, making loans and discounts, receiving deposits, and handling other related transactions—and to prevent it from becoming a nonbanking business of any sort.” As trustee of the public’s funds, commercial banks have been restricted to lending and not to commercial ventures which may risk the public’s funds. Banks are endowed with the depository function only because they are restricted from risking the public’s funds in businesses unrelated to traditional banking.

2. The Comptroller claims that granting banks authority to open and lease property has the purpose of devising “less costly or more effective means of serving consumers.” If this is so, it is mainly because banks obtain much of their funds through noninterest bearing deposits. The privilege of accepting the public’s deposits endows banks with a singular economic advantage which, if banks engage in competition with ordinary business corporations, favors the banks. Commercial banks pay no interest on demand deposits, but ordinary businesses do pay interest on the money that they borrow from banks. Using the Comptroller’s logic, banks should engage in any business activity in which interest expense is a major cost and thus cut cost to the consumer. An extension of such logic is that, if banks may engage in ordinary business ventures, regular business should be allowed to accept the public’s deposits. Either premise is, of course, fallacious.

The Comptroller’s claim that banks by leasing may not engage in merchandising is also based on erroneous concepts. He stated that a bank may engage in leasing only upon the request of the lessee for immediate possession and use of the equipment. Once a bank owns equipment or tries to sell it after the lease term, it in fact is in the merchandising business. Sears, Roebuck & Co., and Montgomery Ward have hundreds of catalog stores which stock no appliances but merely take orders on credit terms for refrigerators, washing machines, and other equipment. Food brokers, commodity dealers on the exchanges, drop shipment jobbers, sales agents, motion picture distributors are additional commercial and marketing enterprises which do not stock merchandise and which perform minimal physical functions, many of a financial or credit nature. May banks engage in these activities?

Once a bank owns a property leased to lessees, the bank incurs the same obligations and risks as any owner of inventory; the bank in fact has a stock in trade. It must assume all the obligations and liabilities of ownership including qualifying to do business in foreign states, speculating on used equipment inventories, incurring liabilities for injury to third parties by equipment, and merchandising of equipment when the lease expires. Every leased item must ultimately be sold and the bank becomes a merchandising operator in the sale of used equipment.

3. Thousands of smaller banks may incur losses if they engage in leasing because they do not have the specialized knowledge or trained staffs to engage in the leasing business nor are they financially equipped to cope with the many problems foreign to conventional bank practice. Specifically:

(a) Operating in foreign states produces a Pandora’s box of problems for commercial banks. The lending of money and acts incidental thereto is considered interstate business, but the ownership and leas-

ing of property is generally considered local or intrastate business subject to the local authority of the foreign state as to taxes, qualification to do business, regulations, and so forth. The laws of most States require an owner and lessor of property to qualify locally to do business. Many States by law restrict an out-of-State bank from qualifying locally to do business. Thus, a bank trying to lease in a foreign state is on the horns of a dilemma: in accordance with the foreign state's law it must qualify to do business, but that state's law prevents a foreign bank from so qualifying. If the bank does not qualify to do business, the enforceability of the contract may be impaired to the detriment of the bank, its depositors, and the public.

(b) Federal tax risks face banks in the ownership of property. Most commercial banks seek to amortize term loans, for example, within 3 to 5 years. Most equipment, however, have depreciable lives longer than are prudent for a commercial bank to use as an amortization period. If a machine tool has a tax life of 15 years and a cost of \$150,000, the owner of the property can accrue yearly depreciation on a straight-line basis of only \$10,000 or only \$20,000 for the first year on accelerated depreciation. However, a bank amortizing the cost of the equipment over 5 years would receive gross income from such amortization of \$30,000 a year. The difference between the gross income received and the depreciation incurred would be taxable income to the bank.

(c) A lease does not offer a bank the same protection and security as an evidence of debt. A lease differs from debt in the myriad ways it may be written; it is as flexible as the human mind may devise. Rents may be calculated on the cost of the property, its productivity, mileage, use, and so forth. Courts have ruled that an interruption of the quiet enjoyment of the leased property may excuse the lessee from his obligation to pay future rates. The bankruptcy laws facilitate the avoidance of a lease and the court applies rules to limit damages. On the other hand, an evidence of debt is a fixed, absolute, and unconditional obligation to pay a sum certain.

(d) Many banks will find costs rising in view of expenses of staffing, handling tax returns in various States, and reviewing the highly complicated legal aspects of qualification and taxation.

4. The power to authorize banks to engage in the leasing business is one which may be granted only by Congress. It has been traditional for almost a century for banks, their counsel and their regulatory authorities to acknowledge that banks do not have the power to engage in nonbanking activities such as leasing. In New York State and Massachusetts the laws regulating State banks are similar to those of the Federal Government. In both of these States the banks and the legislature considered that a change in the law allowing banks to lease required a change in the statute and not an administrative ruling. Thereupon, house bill 686 was introduced this year in the Massachusetts Legislature to allow banks to own and lease property. It is interesting to note that this bill was withdrawn during this month of February 1964, at the specific request of the Massachusetts Bankers Association.

Although the Office of the Comptroller has power to interpret banking law, his authority is clearly circumscribed by the terms of law and the National Bank Act. The courts have held that he does not

have the power to make substantive changes in the law. This principle is set forth in a number of decisions including *First National Bank of Capital Hill v. Murray*; *Baltimore & Ohio Railroad Company v. Smith*; and *Inland Waterways Corporation et al v. Young*. The courts held in these cases that the Comptroller may determine the policy which national banks should pursue so long as that policy is not unlawful and that the Comptroller of the Currency himself must move within the orbit of the National Bank Act. Illegality, claimed the Supreme Court, cannot attain legitimacy through practice.

5. A long series of cases claims that statutes conferring power on national banks are to be construed narrowly. The U.S. Supreme Court in *Texas & Pacific Railway v. Pottorff* (291 U.S. 245 (1934)), through Mr. Justice Brandeis, stated of national banks:

The measure of their powers is the statutory grant; and powers not conferred by Congress are denied * * * moreover, even a practice commonly pursued may not be a necessary one.

The Comptroller's action allowing banks to lease is in contravention of this longstanding axiom and of the National Bank Act, paragraph 7 of 12 U.S.C. 24.

6. The Comptroller has incorrectly held that the ownership and leasing of equipment is incidental and necessary to the business of banking. Again, a long series of cases refutes this claim and reveals that incidental powers are those related to conventional lending, taking liens or property incidental to lending, and foreclosing on and promptly disposing of such collateral. The courts have held that acts not incidental and, consequently illegal for national banks, have been the ownership of property with the intent of obtaining earnings therefrom similar to leasing.

7. The Comptroller's position that no legal limit applies to ownership of property leased by national banks is also in contravention of longstanding congressional policy. As far back as 1878, in *National Bank v. Matthews* (98 U.S. 621 (1887)), the court noted that "The object of the (legal limit) restriction was obviously threefold. It was to keep the capital of the bank flowing in the daily channels of commerce; to deter them from embarking in hazardous real estate speculation; and to prevent the accumulation of large masses of such property in their banks * * *." In *Anderson v. Ackers* (7 F. Supp. 924 (D.C.W.D. Ky., 1934)), the court stated that the legal limit "was for the obvious purpose of preventing the bank from putting too many of its eggs into one basket."

8. The courts may well determine from statute, case law, and historic precedent that the ownership and leasing of equipment is an ultra vires act which opens the bank to suit by its stockholders. One consequence would be exposure of bank directors to personal liability to the extent that a loss is sustained. Another possibility is that a lessee or its trustee in bankruptcy may raise the defense of ultra vires in endeavoring to break the lease and to be relieved of the obligation to pay future rent. Many counsel believe that, so long as the bank was compensated for past use of the equipment and received back in kind from the lessee that which was granted in the first instance, not money as would be the case under a debt but the property as is the case under a lease, the bank would be unable to recover future rentals.

On November 13, 1963, the American Banker published the results of its survey of more than two dozen leading national banks in seven

large cities and reported that only a few banks at this time are ready to enter the leasing field because the "problems are many." Some bankers, the survey stated, "doubt the legal soundness of Mr. Saxon's March ruling that puts banks in the leasing business * * *. Bankers in Chicago, for instance, will not say so officially but many look for trouble ahead. A court test of the ruling is certain, they say privately * * *."

The numerous hazards faced by banks and the public through court determination emphasize the need for Congress to settle the issue promptly. For the protection of the public, depositors, and the banking community, it is essential that the matter be resolved quickly by the rule of law and the enactment of H.R. 9822.

Many National banks have written to us and concurred with our feelings. For example one large bank said :

We have given much thought and consideration to the advisability to entering the leasing business directly as authorized by the Comptroller of the Currency last March. Our decision was to continue providing funds to acceptable lessors, evidenced by collateral notes and secured by the assignment of lease payments due from financially responsible lessees.

In arriving at our decision, emphasis was given to many of the reasons advanced by you in your article. Perhaps, more significant to us was the factor of additional costs required to market a program of direct leasing, and to provide the trained staff to supervise the activities.

And then this bank stated :

I appreciate very much the two copies of the article which you had in the January 1964 issue of the Bankers Magazine. This bank has never considered going into the leasing business, for we consider it foreign to our activity as an important part of the consumer credit operation in this area. We have felt that our interest was in financing leases rather than in owning equipment.

And the next stated :

It is apparent that the points are well taken and, certainly, should give banks planning to enter such a leasing program thought before committing themselves too heavily in that field.

And then another :

I have been interested to note your comment regarding the number of banks engaged in the leasing business which confirms my own impression.

The banks are concerned about the legalities of entering the leasing business.

And another :

According to the Comptroller's December issue of the National Banking Review, banks have written only \$5 million on a direct lease basis through September 30, 1963, which is a further indication that you are correct in pointing out the considerable problems involved in this type of financing.

(The letters and document entitled "Equipment Leasing by Banks, Problems and Solutions" follow:)

STATE OF OREGON,
BANKING DEPARTMENT,
Salem, February 25, 1964.

Mr. ALVIN ZISES,
President, Bankers Leasing Corp.,
Boston, Mass.

DEAR MR. ZISES: I have for acknowledgment your letter dated February 20, 1964, which, together with the enclosures, makes reference to equipment leasing by banks.

This data has been read with much interest, an interest heightened by my considered opinion that equipment leasing is definitely an unrelated business activity where banks are concerned and one that could bring significant problems in its wake.

Your courtesy in furnishing me with this material is appreciated.

Very truly yours,

J. F. M. SLADE,
Superintendent of Banks.

STATE OF LOUISIANA,
STATE BANKING DEPARTMENT,
Baton Rouge, La., February 24, 1964.

Mr. ALVIN ZISES,
*President, Bankers Leasing Corp.,
Boston, Mass.*

DEAR MR. ZISES: Many thanks for your letter of February 19, 1964, enclosing two reprints of an article appearing in the January 1964 issue of the Bankers Magazine regarding the considerable problems incurred by banks in leasing equipment.

It is also the feeling of this department that equipment leasing is not a banking function.

With best wishes, we are,

Very truly yours,

J. W. JEANSONNE,
State Bank Commissioner.

STATE OF DELAWARE,
OFFICE OF STATE BANK COMMISSIONER,
Dover, Del., February 28, 1964.

Mr. ALVIN ZISES,
*President, Bankers Leasing Corp.,
Boston, Mass.*

DEAR MR. ZISES: I appreciate your forwarding to me various enclosures in connection with the question of leasing, which I have noted with interest.

I am unalterably opposed to the banks in this State under my supervision, engaging in the business of direct leasing of personal property. I feel that the banks should only participate in the leasing business as bankers.

Sincerely yours,

RANDOLPH HUGHES,
State Bank Commissioner.

STATE OF IDAHO,
DEPARTMENT OF FINANCE,
Boise, February 26, 1964.

Mr. ALVIN ZISES,
*President, Bankers Leasing Corp.,
Boston, Mass.*

DEAR MR. ZISES: Reference is to your letter of February 20, 1964, wherein you furnished material relating to the problem of banks entering the leasing business.

The office of the attorney general for Idaho concluded in an opinion that Idaho State chartered banks could not enter the leasing business.

Most sincerely,

M. A. LAWRENCE.

STATE OF NEW JERSEY,
DEPARTMENT OF BANKING AND INSURANCE,
March 6, 1964.

Mr. ALVIN ZISES,
*President, Bankers Leasing Corp.,
Boston, Mass.*

DEAR MR. ZISES: Thank you for sending the material on leasing by banks.

I am not convinced that our banks should be in the leasing business, and to this end have put myself on record through our National Association of Supervisors of State Banks, of which I am first vice president and a member of the legislative committee, in favor of the legislation sponsored by Representative Multer.

Sincerely yours,

CHARLES R. HOWELL.

Equipment Leasing by Banks

PROBLEMS AND SOLUTIONS

by ALVIN ZISES

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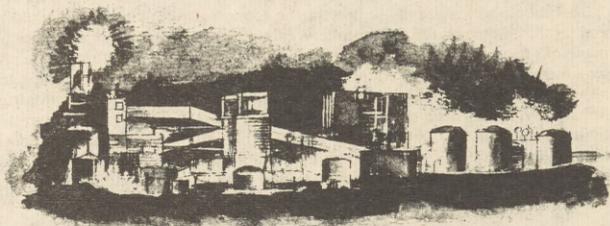
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Archaic rules hamper banks from logical expansion within the business of banking. Pressure to expand now pushes them into a non-banking activity, leasing, under the guise of banking with inherent danger. A solution may be the removal of outdated regulation to correlate banking growth with that of the economy — but within the framework of proper banking functions.

Equipment Leasing by Banks

PROBLEMS AND SOLUTIONS

ALVIN ZISES



WHEN the Chairman of the Board of Governors of the Federal Reserve System described the ruling of the Comptroller of the Currency permitting national banks to underwrite and purchase certain revenue bonds as an "unauthorized attempt to change or to nullify Congressional policy expressed in existing laws," he could well have used the same terms if he were to describe the Comptroller's ruling allowing national banks to own and lease equipment. The Comptroller, in authorizing national banks to become lessors, did so despite a vast body of existing law and basic economics which oppose the direction of this

edict. In fact, attorneys informed the author that they researched in vain for cases to support the Comptroller's action. Legal research in depth uncovered real dangers for banks which own and lease equipment. Contrary to some opinion, attorneys claim, for example, that a lessee, seeking to "break a lease" and offering as a defense that the bank acted beyond the

Mr. Zises is president of a number of leasing companies including Bankers Leasing Corporation, Lease Capital, Inc., and Financial Leasing Corporation. He is a graduate (BCS magna cum laude) of New York University and has spoken and written widely on the topic of leasing.

THE RULE OF LAW

"Some people are suspicious of law and order, as though the rule of law was a mere trick to freeze the status quo. It is quite the opposite. Its observance is the sine qua non of peaceful change. The rule of law is a lesson learned from centuries of human experience, from many mistakes and much suffering. It amounts simply to this: that only by submitting ourselves to obey the law can we reconcile conflicting ambitions and serve the interests of mankind as a whole. Without the rule of law we destroy one another."

— Prime Minister of Great Britain, Sir Alec Douglas-Home.

scope of its powers, may be relieved of his obligation to pay future rents. Some other perils may be the personal liability of bank officers and directors for sanctioning *ultra vires* acts and the penalties imposed by foreign states for failure to observe state law. There may be also dangers to bank customers.

This article will endeavor to present the economic and legal case against the Comptroller's ruling allowing banks to expand into the leasing field. It is written by a member of the leasing fraternity. Consequently, although every effort was made to research the case impartially, some may describe this article as less than objective. Furthermore, the writer is not an attorney; yet much of the color of this portrait is legal. The author, as will be obvious, has leaned heavily upon the research of his legal associates.¹

LEGISLATIVE HISTORY AND POLICY REFUTE THE COMPTROLLER'S LEASING DETERMINATION

Because law is so intertwined with the economics of a people, the historical significance of bank regulation first should be briefly reviewed. When our founding fathers and those who later implemented their doctrines constructed our government, they based their architecture on natural law. They believed in the supremacy of the individual, in free enterprise and competition. In economics as in nature the struggle for existence and survival of the fittest results in natural selection.

Our founding fathers believed that some areas of economic activity were, in the language of the Supreme Court, "clothed with a public interest." F. W. Mueller, Jr., Dean of the College of Commerce of DePaul University in "Structure and Functions of Commercial Banking," stated:

"Public interest plays a much more significant part in the field of finance in general and in banking in

particular than in other types of businesses. Banking is looked upon as being akin to a public utility; that is, it is conceived to be vested with a public interest. Furthermore most (if not all) of the statutory banking limitations have been based upon what appeared in retrospect to be abuses of the kind which could be eliminated or at least reduced by the legislative process. Most of the legislation, therefore, is the product of bitter experience."

Thus, banks were granted a privileged status which gave them certain rights, immunities and limitations in the public interest. Among these privileges was the right to accept deposits of the public's money. These rights, however, recognized the need for regulation in the public good. When a state enacted a law the effect of which prevented any citizen from freely accepting deposits, the supreme court of that state held in an early decision that banking is a quasi-public business and that reasonable regulation could be imposed.

The National Bank Act, Paragraph Seventh

The early history of banking is replete with stories of laxity, wildcat banking, over-extension of credit and bank failures. Banking followed a pattern of excesses followed by losses for depositors, stockholders and, indirectly, the general public. Following an ebb and flow of laxity and abuse the National Currency Act of 1863 was passed by the Federal Congress. Fourteen months after its passage it was amended to clarify effects and ambiguities. Ten years later the title of the measure was changed to "National Bank Act." The National Bank Act as amended created the office of Comptroller of the Currency as the general administrator of national banks and set forth the rules and limitations under which national banks may operate.

The National Bank Act, 12 U.S.C. 24, Paragraph 7 (in part), sets forth the basic powers of national banks, which includes discounting evidences of debt, as follows:

¹ Credit is due Mr. Paul Kirby, General Counsel of Bankers Leasing Corporation, for his guidance and assistance and to Mr. Allen Young for his research.

... to exercise by its board of directors or duly authorized officers or agents, subject to law, all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; by buying and selling exchange, coin, and bullion; by loaning money on personal security; and by obtaining, issuing and circulating notes according to the provisions of this chapter . . ."

In "History of Commercial Banks" by Fayette B. Shaw, Associate Professor of Economics, College of Commerce, DePaul University, the intent of Congress is stated in enacting the National Bank Act:

"Congress also laid down limitations on lending policies. No bank could loan more than 10% of its capital to any one borrower. No bank could be indebted at any time for any amount exceeding its capital stock except for its bank notes, its deposits, liability for bills of exchange drawn against money actually deposited, and liability to stockholders for dividends and reserved profits. Loans on real estate were forbidden, but under certain circumstances the banks were allowed to hold such property. The bank might own real estate in which to carry on its business. It could make no loan with real estate as security, but it could take over property mortgaged in good faith by way of necessity for debts previously contracted; that real estate conveyed to it in satisfaction of debts previously contracted in the course of its dealings, and that purchased under judgment to secure debts owed to the bank was acceptable. No other real estate might be owned; real estate acquired as the result of the loaning process was not to be held longer than five years. Unhappy experience has shown that real estate loans were unliquid in the face of depositors' insistent withdrawals since real estate cannot be sold readily. The purpose of these restrictions was to keep the bank in the commercial banking business — that is, making loans and discounts, receiving deposits, and handling other related transactions — and to prevent it from becoming a non-banking business of any sort."

Later Developments in Bank Regulation

To keep banks in the business of banking and out of riskier ventures, banking laws of the state and federal government continued to develop. Professor of Economics, Donald L. Kemmerer, of the University of Illinois, in "The Federal Reserve System", describes the steps that were taken in the 1930's to regulate banks.

"... there were four laws in particular, enacted

between 1933 and 1935, that changed the framework of the (banking system) and redirected the viewpoints of its policy makers. These were the Banking Acts of 1933 and of 1935, and to a lesser degree the Securities Act of 1933 and the Securities and Exchange Act of 1934. . . . The 1933 law established a temporary Federal Deposit Insurance Corporation, and the 1935 law made it permanent. . . . "Member banks were henceforth forbidden to make interest payment on demand deposits, and they were forbidden to borrow from Federal Reserve Banks for speculative purposes. The elimination of the payment of interest on demand deposits was done partly to offset the cost to the banks of Federal Deposit Insurance. The Federal Reserve Banks were expected to keep themselves informed of the nature of the loans made by member banks in their district. Also the Banking Act of 1933 required that commercial banks and investment banks should no longer be combined as they had been with rather disastrous results in the 1920's."

The obvious purpose of these legal developments was to avoid risking the public's funds. The law recognized early that those privileges granted to banks endowed them with economic advantages which, in competition with ordinary corporations, favor the privileged. Thus, banks are allowed to compete in the lending of money, but are restricted from competing outside their privileged sphere not only to prevent those entrusted with the public's money from risks resulting from the "rough and tumble" of normal business ventures but also to prevent unfair competition. Although competition is a fundamental tenet of our society, limitation on competition is a prime corollary when public interest and special privilege is concerned. Congressman Abraham Multer, member of the House Banking and Currency Committee, in an address before the American Banking Association on October 7, 1963, summarized the regulation and supervision of banks: "Human nature being what it is, no free enterprise system will long survive without proper regulation and supervision of its financial institutions."

NEED FOR GROWTH: PRESSURE TO DEVELOP NEW BANKING ACTIVITIES

However, there was another side to the coin. Fifty to seventy-five years ago ours was essentially a sectional and agricultural economy. Yet, many of our banking laws were promulgated at that time and were based upon the then existent structure. After our nation emerged from the Second World War, it became the capital reservoir for the Free World. Western Europe started to compete with a new and

efficient industrial plant. Emerging nations in other areas began to experience their Industrial Revolution. At home cities spread their influence for hundreds of miles to neighboring counties and states. Advanced methods of communication and transportation brought transcontinental markets within minutes of each other. Industries, formerly local or sectional, became national and international in scope; and their resources and customers spread throughout the country and the Free World. Business enterprises formerly having capital in the millions of dollars grew to capital bases in the billions. As companies grew, their borrowing needs expanded.

All this happened while the business of banking was bound by restrictions, many applicable to a period before the Federal Reserve System was formed, before the Panama Canal was completed and before Ford, General Motors and I.B.M. were conceived. Banks found themselves growing, but nowhere near the rate of industry and the economy. In Texas and Illinois banks were limited to a single bank house with no branch banking allowed. In Massachusetts branching was permitted only within county lines drawn during the period of the Revolutionary War. In the New York metropolitan area, encompassing parts of three states, some small relief was granted for banks to expand within New York state counties adjoining New York City.

In an environment which hampered the growth of banks from paralleling the growth of the economy, rigidities limited the expansion of deposits, and non-financial lenders entered the partial vacuum and competed with commercial banks. Restricted from completely fulfilling their functions within the framework of banking, banks burst into the non-banking area of leasing. It was *Pascal's law*, exerted pressure is transmitted equally in all directions, applied to economics. Unless banks are allowed greater latitude to expand within their own sphere of banking, pressure may well cause banks to expand into other non-banking fields.

Consequently, although the ruling of the Comptroller allowing banks to own and lease equipment may be validly criticized as unsound economics, the endeavors of the Comptroller to allow banks latitude to grow — within the business of banking — in order to help this nation's industry meet its national and international commitments is laudable.

SOME TECHNICAL CONSIDERATIONS

Differences Between an Evidence of Debt and a Lease

Before we examine the legality of the Comptroller's directive it is incumbent upon us to examine the

differences between an "evidence of debt" and a lease. It is also important to distinguish between a true lease contract and one which purports to be a lease but is not. The difference bears on many important questions such as the inherent powers of banks and their doing business in foreign states.

Basic to a true lease is retention of title and ownership in the lessor and the executory concept that the lessee obtains not the ownership but only the use of property from period to period. The lessor incurs a continuing obligation to insure that the lessee has the quiet enjoyment of the property. A lease differs from debt in the myriad of ways it may be written; the types of leases are as flexible as the human mind may devise. Rents may be calculated in many ways: on the cost of the property, its profits, sales, production, mileage, use, or period of availability. Because of its executory or uncompleted nature, the future commitment under the lease, even under a "net" and so-called "noncancelable" lease, is never fixed but subject to contractual and statutory limitations which make the legal liability indeterminate and unpredictable.

On the other hand financing through debt is financing through a fixed, unconditional and absolute obligation of the debtor to the creditor.

Inherent Weakness of Bank-lessor's Position

Describing the nature of a lease obligation a court ruled recently:²

"The obligation to pay rent was not an unconditional one since it was contingent upon the future use and enjoyment of the leased property by Kroh [defendant] . . . the relationship of lessor-lessee is not always coexistent with that of debtor-creditor, since the latter relationship arises only upon the failure of the lessee to pay the rent agreed upon at the time in the future fixed by the lease. An interruption of the peaceable enjoyment and possession of the leased property under certain circumstances would excuse the lessee from the obligation to pay any future rental."

The bankruptcy and similar laws were designed to protect the holders of debt obligations against the claims of lessors; and the law, statutory and case, facilitated this protection of creditors to the detriment of the lessor in many ways: the trustee in bankruptcy or re-organization may disaffirm an executory or lease contract; the lessor, to collect, must prove damages with all the problems that proof of damages entails; the court applies rules to limit damages including the doctrine of frustration (if some supervening event prevents the lessee from enjoying the property for the

² *Evans v. Kroh*, 284 S.W. 2d 329 (Ky. 1955).

purpose intended, the lessee may be relieved of his obligation); the courts have challenged default covenants incompatible with the executory nature of the lease.³

The "Pseudo Lease" or Debt in Lease Guise

For years many banks engaged in transactions which were called "leases" but were leases in name only. In substance they incorporated every element of a debt transaction, of either a conditional sale or mortgage. The "lessee" agreed to save the bank harmless from all losses, counterclaims, or setoffs of whatsoever nature including the bankruptcy of the "lessor". The "lessee" agreed that in bankruptcy it would not take refuge in the special privileges afforded it by the bankruptcy statutes. The "lessee" itself took depreciation on equipment as owner and the "lessor" did not take depreciation. For purposes of state taxation and qualification the "lessee" appeared as an owner. The "lessee" was in fact the owner of the property and the bank did not have any title to the property beyond a possible security interest. As illustrated later, many leases were constructed with a trustee as "lessor". These also were evidences of debt. So long as all interested parties understood and had full disclosure of the true nature of this transaction, it appeared to be an acceptable technique and legally discountable by national banks as an "evidence of debt" under the National Bank Act.

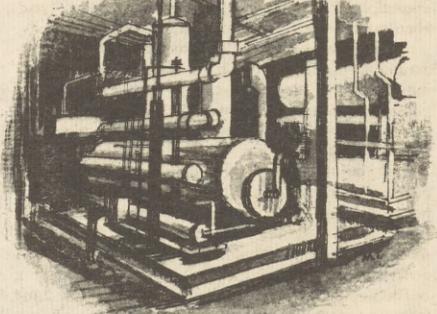
Earlier Requirements of Comptroller as to Evidence of Debt

A few years ago the Comptroller of the Currency was faced with the question of whether or not such a so-called "lease" constituted an "evidence of debt" within the meaning of the National Bank Act which authorizes national banks to discount "promissory notes, drafts, bills of exchange, and other evidences of debt". He concluded that a lease would be an "evidence of debt" if:

- All the obligations of the "lessor" were performed, or the "lessee" agreed to save the bank harmless from all losses, counterclaims, or offsets resulting from the failure of the "lessor" to fulfill its obligation; and
- The "lessee" is unconditionally obligated to pay all of the specified "rentals"; and,
- The "lessee" agreed not to assert any defenses, offsets, or counterclaims he may have against the "lessor" as against the assignee of the "rentals" payable under the "lease".

³ *Kothe, Trustee v. Irving Trust Company*, 280 U.S. 224 (1930).

Under such transaction the "lessee" will be obligated to pay the total amount of the "rents" even if he were deprived of the use of the property. Such an unconditional promise to pay obviously would make the so-called "lease" a debt instrument and the bank may purchase or discount such a "lease" just like a promissory note. However, the instrument is not a lease. Furthermore, the "discounting" and "purchasing" of a lease by a bank does not convey to the bank ownership to the property but merely a security interest.



SOME POSSIBLE CONSEQUENCES OF PSEUDO LEASE

Consequences to Lessee "Borrower" If "Lease" Is Debt

The question arises as to what is the effect if the instrument is not a true lease and is an evidence of indebtedness. As to any "lessee", incurrence of a debt in the form of a so-called "lease" may constitute a breach of indenture restrictions or negative covenants in other debt agreements of the "lessee". Present and contemplated accounting principles require capitalization of the debt on the "lessee's" balance sheet; if the lessee did not capitalize the debt transaction he may be considered guilty of issuing fraudulent statements. It would probably result, in those cases where the "lessee" was engaged under Armed Forces Service Procurement Regulations, in disallowance of the interest portion of the "rental" payments. The Treasury Department might disallow the taking of "rental" deductions by the "lessee" and, as owner, the "lessee" may have to take depreciation on the property. This might result in loss of the deduction for the interest portion of the "rent" where the rate exceeded the allowable legal rate. The lessee may lose the benefits of accelerated depreciation for want of a timely election so to do. If a regulated public utility executed an instrument which purported to be a lease but which was in effect an evidence of indebt-

edness without obtaining Commission approval to issue such evidence of indebtedness, there may be severe penalties to both the "lessee" and investor. In some states the transaction is "void."

Consequences to Bank If "Lease" Is Debt

As to the lessor, if a "lease" is considered a debt, the bank's depreciation deductions would be disallowed and the bank "lessor" may be faced with the possibility of paying income taxes on the entire profits of the "lease" program in the year of the execution of the "lease". If the bank as "lessor" had been taking depreciation on some accelerated basis, it may lose the tax advantage which flowed from such acceleration. If the "lease" is ruled to be a chattel mortgage, the "lessor" may be unable to recover possession of the equipment on the ground that ownership had passed to the "lessee" and the document represented security for a "loan" from the "lessor". At the same time even the secured creditor position of the "lessor" may be destroyed if the "lease", which now has been ruled a mortgage, was not recorded as prescribed by the relevant statutes. In bankruptcy of the "lessee" the "lessor" may be converted to a general creditor of the "lessee".

The consequences of a conditional sale not conforming to local state requirements as to either documentation or rate were portrayed in an article in *The Wall Street Journal* of Wednesday, October 23, 1963. The article reported that the states of Nebraska, Missouri, Washington and Wisconsin may declare void any debt transaction in which the interest rate is higher than the usury limits. It appears that *the purchaser then may not only keep the equipment and refuse to pay the remaining time balances but also sue for recovery of any payments previously made under the contract*. Under the laws of most other states the conditional vendor may lose his security interest in the property and be unable to recover interest if the requirements of law are not met.

Consequently if the instrument is a debt instrument it should be recognized as such and treated accordingly for all purposes. In the remainder of this article we shall address ourselves to the considerable questions which arise under a true lease where a bank acts as lessor.

POWERS OF THE COMPTROLLER AND NATIONAL BANKS

Authority of Comptroller of Currency

In "Checks and Balances" by Thomas W. Thompson we learn:

"within the orbit of government, the Comptroller alone possesses the right to 'create' or charter a bank. In a sense,

he compares to a Supervisor of State Banks, but stands apart from the Chairman of the F.D.I.C. or the Chairman of the Board of Governors of the Federal Reserve System. To measure the significance of his office, the effect of his personality must be weighed . . . the authors of the National Currency Act . . . 'freed' the Comptroller from political implications by having him appointed for a five-year term . . . theoretically, he is answerable to the people through the Congress."

Although the office of the Comptroller has power to interpret banking law, his authority is clearly circumscribed by the terms of law and the National Bank Act.⁴

Powers of National Banks

A series of cases recognizes the fundamental maxim that national banks are prohibited from engaging in activities which are not expressly permitted. Furthermore, the courts have held that incidental powers are those which support and relate directly to those express powers and are so circumscribed.

In an effort to justify the legality of his ruling, the Comptroller's letter of October 22, 1963 declares that national banks "are not limited to the . . . clauses" of Paragraph 7 of 12 U.S.C. 24 of the National Bank Act which list the specific powers granted to national banks. In refutation the courts have consistently determined that the authority of national banks are circumscribed by those powers so enumerated within the Act.⁵ Therefore both the Supreme Court and the

⁴ This principle is implicit in the case of *First National Bank of Capital Hill v. Murray*, 212 Fed. 140 (C.A. 8, 1914) where the Court declared: ". . . his acts within the law are not subject to review by the courts." (italics supplied.)

A similar conclusion is drawn in *Baltimore & Ohio Railroad Company v. Smith*, 36 F. 2d 799 (C.A. 3 1932) that the Comptroller may determine "the policy which national banks should pursue so long as that policy is not unlawful and does not offend against public policy. But when it is unlawful and contrary to public policy, then the courts have jurisdiction . . ." (italics added). The courts have held also in *Inland Waterways Corporation et al. v. Young*, 309 U.S. 517 (1939): "The Comptroller of the Currency, to be sure, must himself move within the orbit of the National Bank Act. Illegality cannot attain legitimacy through practice."

⁵ In a typical pronouncement that statutes conferring power on national banks are to be construed narrowly, the United States Supreme Court in *Texas & Pacific Railway v. Pottorff*, 291 U.S. 245 (1934), through Mr. Justice Brandeis, stated of national banks: "The measure of their powers is the statutory grant; and powers not conferred by Congress are denied . . . moreover, even a practice commonly pursued may not be a necessary one."

To the same effect, *California Bank v. Kennedy*, 161 U.S. 362 (1897); *De Laverne Company v. German Savings Inst.*, 175 U.S. 40 (1889); *Cooper v. Hill*, 94 Fed. 582 (C.A. 8, 1899); *Leonhardt v. Small*, 117 Tenn. 153 (1906); *Bank of Mifflintown v. Bank of Kensington*, 247 Pa. 40 (1914); *Inland Waterways Corp. v. Young*, supra; *O'Connor v. Bankers Trust Co.*, 289 N.Y.S. 252 (1936); *Bank of California v. City of Portland*, P. 2d 273 (1957); *Atherton v. Anderson*, 86 F. 2d 518 (6th Cir. 1936); *Greene County Nat. Farm Assoc. v. Fed. Land Bank*, 57 F. Supp. 752 (1947); affd. 152 F. 2d 214 (1945); *Talmadge v. Pell*, 7 N.Y. (3 Selden) 328 (1852); *Citizen's Bank and Trust v. Harpath National Bank*, 120 Miss. 505 (1919).

state courts have not permitted actions of national banks unless specifically granted. Those activities falling outside the terms of the National Bank Act are prohibited and not justified as "incidental powers" necessary to carry on the business of banking.

Incidental and Non-Incidental Banking Activities

The rationale of the Comptroller of the Currency, in endeavoring to find a way for banks to engage in the commercial activity of leasing equipment, has, as is evident from a reading of his letters, moved from the requirement that a "lease" be an evidence of debt to the thrust that leasing is "incidental" and "necessary to the business of banking." A long series of cases describes those powers of national banks which are "incidental" and "necessary to the business of banking"—and those acts which are not.⁶ The cases reveal that incidental powers are those relating to

ACTS INCIDENTAL TO BANKING

⁶ A savings bank may lease a theater acquired upon foreclosure of a mortgage, but it may not become a partner of the lessee in the operation of the theater: *Cole v. Rome Savings Bank*, 161 N.Y. Supp. 15 (1916). Where a bank's charter allows it to act as an insurance broker for its customers, it may not nevertheless underwrite insurance as a principal: *Alabama Red Cedar Co. v. Tennessee Valley Bank*, 76 So. 980 (Ala., 1917).

A bank may act as agent for its customers in matters incidental to its ordinary business such as obtaining or preserving liens, closing sales, recording instruments, delivering papers, receiving and making payments, etc. But it may not engage in commercial transactions outside the banking business excepting as is necessary to protect its loans. 9 CORPUS JURIS SECUNDUM BANKS AND BANKING §§ 161(a), 162.

A national bank may purchase remaining outstanding stock in a corporation and acquire complete ownership so as to be able to sell it at a more favorable price in liquidation of a loan. *First National Bank v. National Exchange Bank*, 92 U.S. 122 (1875). Similarly a bank may buy an undivided interest in collateral consisting of a cotton mill business in order to protect its lien against the property owned by the business: *Cockrill v. Abeles*, 86 Fed. 505 (C.A. 8, 1898).

A bank may extend money to clean, repair and outfit an abandoned mine which it acquired in settlement of a loan in order to make it more attractive to purchasers: *Cooper v. Hill*, 94 Fed. 582 (C.A. 8, 1899); and similarly it may put a wagon manufacturing company into operation in order to be able to sell it as a going concern: *Atherton et al. v. Anderson*, 86 F. 2d 518 (C.A. 6, 1936); and temporarily operate a grain storage warehouse acquired pursuant to a bad loan: *German National Bank v. Meadowcroft*, 4 Ill. App. 630 (1879).

A bank may also sue for negligent carriage of property title which it acquired in settlement of a debt: *Farmers' and Millers' Bank v. Detroit & Milwaukee R.R. Co.*, 17 Wis. 372 (1863); or buy wheat in order to seed a farm which it acquired as collateral, rather than permit the farm to lie fallow; *First National Bank of Great Bend v. Bannister*, 7 Kan. App. 787 (1898). A bank may also ship goods belonging to a customer on which it had loaned money in its own name for its own protection in case of loss; *Griffin v. Wabash R.R. Co.*, 115 Mo. App. 549 (1906); or, having acquired a stock of lumber by foreclosure, spend money to have the lumber cut into specific sizes to satisfy a customer who was willing to take it off the bank's hands; *Paterson & Edey Lumber Co. v. Bank of Mobile*, 203 Ala. 536 (1919).

lending, taking liens on property incidental to lending, and foreclosing on and promptly disposing of such collateral. Acts not incidental, and consequently illegal for national banks, have been the owning of property with the intent of obtaining earnings therefrom, similar to leasing.

In connection with the issue of whether banks have the implied power to own personal property, national banks have explicit power to acquire real estate. This power is limited to real estate to be used for bank premises and to an amount equal to the amount of the capital stock of the bank, unless the Comptroller approves a larger investment.⁷ Also, under the National Bank Act banks are granted specific authority to engage in the safe deposit business. If Congress intended banks to have power to own personal property (other than the implied power to own personal property for its own use) it would have explicitly set forth such power with appropriate limits on the extent of the power.⁸ A recent federal court decision reconfirms that the ownership and leasing of equip-

ACTS NOT INCIDENTAL TO BANKING

A bank may not speculate for itself and risk its capital in speculative trading nor engage in the business of selling personality. Nor may it enter into alien lines of business or deal in property which it has taken otherwise than as security for indebtedness except for the purpose of protecting its loans. 9 CORPUS JURIS SECUNDUM BANKS AND BANKING, § 167; *Talmadge v. Pell*, 7 N.Y. 328 (1852); *Dyer v. Broadway Central Bank*, 233 N.Y. Supp. 96 (App. Div., 1929); *Dillon, Read & Co. v. Commercial State Bank*, 62 F. 2d 606 (C.A. 3, 1932). Nor may a bank, having acquired a cotton mill through foreclosure, set up a dummy corporation to operate the mill on a more or less permanent basis. *Cockrill v. Abeles*, supra.; nor may it do the same thing with a wagon business. *Birdsell Mfg. Co. v. Anderson*, 104 F. 2d 340 (C.A. 6, 1939); nor may a bank engage generally in the grain warehouse or grain storage business. *German National Bank v. Meadowcroft*, supra.

If a bank acquires a mine through foreclosure, it may put it in condition to sell but may not, failing to find a purchaser, prospect for ore on its own account. *Cooper v. Hill*, supra.; nor may it sell produce on commission even if the proceeds of the sale of the produce are to be applied to debt owed to the bank: *First National Bank of Decatur v. Priest*, 50 Ill. 321 (1869).

A bank may not become a partner in a land development project by acquiring partnership certificates as collateral for a loan: *Merchants' National Bank v. Wehrmann*, 202 U.S. 295 (1905); nor may it become a partner in operation of a vaudeville theater business: *Cole v. Rome Savings Bank*, 161 N.Y. Supp. 15 (1916).

A national bank may not contract to sell and deliver stock in another corporation to a third party, even when the bank does not own the stock itself, but is acting for a customer: *Hotchkin v. Third National Bank of Syracuse*, 219 Mass. 234 (1914).

⁷ 12 U.S.C. Sections 29, 371(d).

⁸ A commercial bank clearly may not engage in the business of selling personal property (every leased item also must ultimately be sold). *First National Bank v. Converse*, 200 U.S. 425; *Cooper v. Hill*, 94 Fed. 582 (8th Cir. 1899); 10 American Jurisprudence 2d 286. While in economic terms leasing, like some forms of wholesaling, performs a financing function, courts have held that leasing operations may not be equated with the business of lending on credit. *State v. Board of Commissioners*, 96 So. 910 (1923); *City of New Orleans v. Disabled Am. Veterans*, 65 So. 2d 796 (1953); *Miller v. Greater Baton Rouge Port Comm.*, 74 So. 2d 387 (1954).

ment is considered a business and a commercial function unrelated and not incidental to banking.⁹

Direct Leasing Contradicts Bank Loan Limitations

The Comptroller's position that no legal limit applied to ownership of property leased by the bank seems to be in contravention of long-standing doctrine. The legal limit concept had been basic to the regulation of banking from early time.¹⁰ If banks are not subject to legal limits on leasing activities, the absence of such limitations is itself evidence that leasing was not contemplated by the Congress as the "business of banking". Under the Comptroller's new policy, a bank may lend its full legal limit to a borrower and, additionally, lease equipment having a cost substantially higher than the bank's limit. Thus the Comptroller's position seems to contravene a settled statutory policy of Congress.

Analogy of State Bank Debt Requirement

We know of no state law which allows a state bank to own and become the lessor of personal property. For example, in New York, under a statute which is substantially the same as that appearing in the National Bank Act, the Superintendent of Banks ruled that a New York bank could not become the owner and lessor of personal property.¹¹ While this ruling

is not binding on national banks, it demonstrates that the ownership and leasing of personal property is not necessary to the business of banking.

STATE REGULATION AND TAXATION OF NATIONAL BANKS

Consequences of Leasing Activity

It has been well established since the middle of the last century that the fact that a national bank has been chartered by the federal government does not exclude its regulation by the states so long as that regulation is not discriminatory.¹² It would be consistent with historic practice or law for a state to exercise dominion over an intrastate activity as leasing if the lessee or property were situated in the foreign state; the ownership and leasing of equipment in most jurisdictions constitutes intrastate business.

bank would receive the legal title of the original lessor in and to the equipment being leased. As a consequence, a purchase by a bank of a true lease would result in a bank becoming lessor of personality, a result which is not compatible with the powers of a New York State bank or trust company. Even if the bank, as lessor, assumed no duties, it would still be the owner of personality at the end of the lease. The fact that such personality might have no economic value does not detract from the fact it would still be responsible therefor as the legal owner thereof." N.Y. Superintendent of Banks, *Supervisory Circular Letter*, C.B. 19, dated December 21, 1959.

¹² The Supreme Court stated in *National Bank v. Commonwealth*, 9 Wall. 353: "National Banks are subject to the laws of the state and are governed in their daily course of business more by the laws of the state than of the nation. All their contracts are governed and construed by state laws. Their acquisition and transfer of property, their right to collect their debts and their liability to be sued for debts, are all based on state law. It is only when the state law incapacitates the banks from discharging their duties to the Government that it becomes unconstitutional."

The scope of state regulation of national bank activities is very wide. The exercise by the federal government of its power of granting immunity from reasonable state regulation is not to be implied. *Commissioner v. Chase Securities Corp.*, 10 N.E. 2d 472. Through its general regulation of commercial activities, state policies have a great effect on national banks. Thus, the Nebraska Loan Act rather than any federal statute was applicable to a national bank which charged excessive rates of interest, where the conditional sales contract provided that all matters relating to the interpretation and performance of the contract should be governed by the laws of the state in which the buyer resided. *Robertson v. Burnett*, 109 N.W. 2d 716. The status of the bank as an instrumentality of the federal government did not exclude the operation of state workmen's compensation laws upon its operations. *Sneed v. Industrial Commission*, 10 N.E. 2d 327. National banks are not excluded from the operation of state anti-monopoly legislation. *Peoples Savings Bank v. Stoddard*, 102 N.W. 2d 777. State statutes limiting the pledging power of borrowers limits the lending powers of a national bank. *Schramm v. Bank of California*, 23 P. 2d 327. Statutes providing for the recovery by states of penalties against a corporation for holding real estate in contravention of state statutes is applicable to national banks and is not in contravention of any federal legislation. *National Bank of Commerce v. State*, 368 P. 2d 997. National banks are subject to state regulation regarding the institution of all legal proceedings, even to the requirement of posting bonds. *First National Bank v. Drexler*, 184 So. 607. Thus, one may assume local jurisdiction will be effective if a national bank domiciled in one state owns and leases property situated in another state.

⁹ In *Cooper Tire and Rubber Company Employee's Retirement Fund v. Commissioner*, 36 T.C. 96, 306 F. 2d 20 (C.A. 6, 1962) the Court of Appeals reaffirmed the Tax Court's decision that:

"... there is a distinction between an investment in securities and an investment in tangible personal property such as machines. Nothing further need be done in the case of an investment in securities in order to realize income but further action is required in the case of an investment in machines. They will produce no income unless used, rented, or sold. The amount of money invested, the manner in which petitioner purchased the industrial machinery (with a \$200,000 loan) and the many years the leasing activity is to cover, all point to petitioner entering a business activity."

¹⁰ For a parallel, note an old decision, *National Bank v. Matthews*, 98 U.S. 621 (1878), in which the court commenting upon the restriction of a bank's investment in realty said:

"The object of the restriction was obviously three-fold. It was to keep the capital of the bank flowing in the daily channels of commerce; to deter them from embarking in hazardous real-estate speculation; and to prevent the accumulation of large masses of such property in their banks..."

In *Anderson v. Ackers*, 7 F. Supp. 924 (D.C. W.D. Ky., 1934), the limit as to the maximum exposure of the bank arising out of the obligations of any person "was for the obvious purpose of preventing the bank from putting too many of its eggs into one basket."

¹¹ "Where a true lease agreement is involved, such bank or trust company must receive, as a legal requirement, the unconditional promise of either the lessee or the lessor to pay a sum or sums certain on a specified date or dates. Such unconditional promise may either take the form of a promissory note of the lessor with an assignment of rentals as security or an agreement on the part of the lessee which in all respects is the equivalent of a promise to pay as contained in a promissory note. In either case, however, the bank may not purchase a true lease even if it contains an unconditional promise on the part of the lessee to pay a sum or sums certain on a specific date or dates, since by such purchase the

Some states prohibit a bank, domiciled in another state, from qualifying as a foreign corporation. If a bank could qualify, the state may seek to exercise jurisdiction not only over the bank's continued ownership and leasing of property but also over lending and other banking activities. If the bank does not qualify, it may be exposed to penalties for failing to qualify to do business in these states; may be deprived of rights to defend suits if not properly qualified; may expose its income and activities other than that of leasing to be subject to state regulation, taxation, or control. *In many states failure to qualify to do business results in the impairment of the enforceability of the lease.*

The author is informed that one bank seeking to own and lease equipment situated in a foreign state has already been informed that it must seek to qualify under the banking laws of the foreign state. To circumvent this problem the bank apparently has decided to offer a pseudo lease. In another state the former commissioner of banks expressed the viewpoint that if an out-of-state bank owned and leased property domiciled within the commissioner's state, the out-of-state bank would require a special charter from the commissioner's state because the out-of-state bank would be engaging in the business of intrastate banking outside the state of its incorporation. Such a charter may be available only upon approval of the state legislature.

A thorough appreciation of the extent to which banking commissioners may attempt to regulate the activity of foreign national banks "doing business" within their state would depend on the attitudes of each commissioner as reflected by his rules and regulations. It cannot be determined solely from a reading of the statutes what position a banking commissioner would take when faced with leasing operations by a foreign-domiciled national bank. Only a comprehensive study of the regulations and cases could indicate that. However, a number of statutes by implication seem to exclude foreign banks from engaging in this type of operation.¹³

Requirement of Bank Qualifying Locally To Do Business

Let us assume for a moment, however, that leasing always had been a time-honored banking practice,

¹³ For example, Washington Statutes, § 30.04.290 provides: "A foreign corporation whose name contains the word 'bank' . . . or whose articles of incorporation empower it to do a banking business and which desires to engage in the business of lending money on mortgage security or in buying and selling exchange, coin, bullion or securities in the state may do so, but only upon filing with the supervisor of banking . . . a certified copy of a resolution of its governing board to the effect that it will not engage in banking or trust business in this state."

that it is now authorized by the specific terms of the National Bank Act, and also authorized for banks both in the state of incorporation and in the state where the chattels are located. Under these circumstances will an out-of-state bank be forced to comply with state statutes regarding qualification of foreign corporations; will the bank be subject to suit in other than its home state; will the bank be taxed by the foreign state? There are relatively few decisions on the question of qualification of national banks under state foreign corporation qualification statutes. Most of them hold that national banks, being instrumentalities of the federal government do not come within the meaning of the statutory term "foreign." However, all such cases are distinguished in that they relate to established and historic banking and lending activities such as lending money on promissory notes, discounting of commercial paper, taking mortgages on property and dealing with deposits.¹⁴

Quite apart from qualification, and assuming still that leasing had become an established banking practice and authorized by specific terms of the National Bank Act, by the home state of the bank and the state

¹⁴ Several courts have held that their state corporation qualifications statutes do not include out-of-state national banks. *Bank of America v. Lima*, 103 F. Supp. 916 (D.C. Mass. 1952); *Steward v. Atlantic National Bank*, 27 F. 2d 224 (Wash., 9th Cir., 1928); *Grayson County State Bank v. Calvert*, 357 S.W. 2d 160 (Tex. 1962).

To be sure, a state may not exclude a federal instrumentality from doing business. Nevertheless, cases distinguish national banks from wholly-owned federal instrumentalities, point out that national banks are essentially profit-making organizations, and hold that the same strict rules which exempt state regulations of federal instrumentalities do not operate with respect to these quasi-public institutions. *Sneed v. Industrial Commission*, 10 N.E. 2d 327 (Ill. 1937). See *Anderson National Bank v. Luckert*, 321 U.S. 233 (1944); *Jennings v. United States Fidelity and Guaranty Co.*, 294 U.S. 559; *First National Bank v. Missouri*, 263 U.S. 640; *Waite v. Dowley*, 94 U.S. 527; *Flood v. City National Bank*, 263 N.W. 321; and *First National Bank v. Industrial Accident Comm.*, 2 P. 2d 347. The foregoing decisions all hold that national banks are subject to state regulatory statutes so long as they do not discriminate against national banks and in favor of state banks. An argument that privately-held institutions with quasi-public functions do not have the same power to disregard state exclusionary policies as does a federally-owned corporation is especially persuasive in light of recent Supreme Court decisions that indicate inter-governmental immunities should be narrowly restricted. See *Graves v. People of New York ex re. O'Keefe*, 306 U.S. 466.

Since the National Bank Act forbids the establishment of out-of-state branches it would appear that a state may exclude an out-of-state national bank, or allow that bank to enter only upon qualification and regulation under the authority of the foreign state. While it is true that many decisions that have passed on the question have held that out-of-state national banks need not qualify to do business, there are courts that read other statutes dealing with foreign corporations to include these national banks. *Robertson v. Burnett*, 109 N.W. 2d 716 (Neb.); *Hills v. Burnett*, 109 N.W. 2d (Neb.). Furthermore, all these cases which exclude out-of-state national banks from the operation of the foreign corporation qualification statutes are not really in point as the operations which banks were performing were orthodox lending activities, and not the wholly different leasing ventures with which we are concerned here.



in which the property is situated, doing a leasing business in a foreign state could well open the out-of-state national bank to suit in inconvenient locations.¹⁵

State Taxation of National Banks

The Federal statutes as to taxation of national banks by no means exclude national banks from taxation in jurisdictions other than that of its domicile. The Supreme Court has held that a tax whose economic burden in fact falls on the customers of the bank is not unconstitutional as a tax upon a federal instrumentality.¹⁶ Sales taxes, use taxes, and similar levies may be imposed legitimately upon leasing operations of national banks and on all collateral operations, such as applications for permits to collect sales and use taxes.¹⁷ The problem of state taxation of commercial lending activities of out-of-state banks was seen as sufficiently serious to prompt Mr. Howard Shepard, then President of The First National City Bank of New York and of the New York Clearing House Association to write Congress asking that a proposed statute treating state taxation of interstate commerce include a specific exemption for the interstate activities of financing institutions.¹⁸

Comptroller's Committee Recognizes Risk of State Regulation and Taxation

The authors of the Report of the *Advisory Committee on Banking to the Comptroller of the Currency*, in sections of the Report unrelated to the recommendation on leasing, recognize the dangers of exposing national banks to out-of-state regulation, taxation and service of suit. On page 161 of the Advisory Report, under the heading of "State Licensing and

Regulation", the Committee wrote: "A number of states have attempted, either directly or indirectly, to subject national banks to state licensing and regulation or coerce them to subject themselves to such licensing and regulation. Problems of state regulation and visitation have arisen not only with regard to the commercial banking activities of the national banks but also in connection with their trust department operations"

In the discussion of state taxation beginning on page 170 of the Committee's Report, concern is expressed over the attempts by some states to impose discriminatory tax treatment on national banks. On pages 184 and 187 of the Report, concern is voiced as to national banks being amenable to service of process in states other than their home location. Nowhere in the Report, however, were these problems associated with the ownership and leasing of equipment. One may well question the depth of that part of the study applicable to the Recommendation that leasing become a lawful banking activity. The Comptroller justifies his ruling in large measure upon this Recommendation.

CHALLENGE TO COMPTROLLER'S LEASE RULING

Who May Raise Question

On November 13, 1963, the *American Banker* published the results of its survey of more than two dozen leading national banks in seven large cities and reported that only a few banks at this time are ready to enter the leasing field because the "problems are many." Some bankers, the survey stated, "doubt the legal soundness of Mr. Saxon's March ruling that puts banks in the leasing business. . . . Bankers in Chicago, for instance, will not say so officially but many look for trouble ahead. A court test of the ruling is certain, they say privately"

Who may challenge the Comptroller's directive? The Comptroller's directive may be upset or challenged by future Comptrollers; by Congress; by a suit of a bank stockholder; possibly by depositors, general creditors or competitors of a bank; by individual state action; and, contrary to some opinion, by a lessee of a bank or the lessee's trustee in bankruptcy.

Because of the consistency with which the banking community and former Comptrollers have held that leasing is not a banking activity, future Comptrollers may change the ruling and return to the practices of the past. The Senate and House Banking and Currency Committees may soon make their positions clear to the Comptroller. Many people close to the Congressional scene have questioned the legal basis for the Comptroller's authorization.

¹⁵ A Federal venue statute requiring suit against a national bank in the district in which it is located has been upheld in Supreme Court decisions; *Mercantile National Bank v. C. H. Langdale*, 374 U.S., 83 S.Ct. 520 (1963) and *Michigan National Bank v. Robertson*, 31 Law Week 3305 (1963). However, these cases covered conditional sales contracts entered into in one state and discounted in another, a traditional debt transaction, and not the ownership of personality locally leased by an out-of-state bank. This principle is implicit in these cases which cite an earlier case *Van Reed v. People's National Bank*, 198 U.S. 554, 557: "National banks are quasi-public institutions, and for the purpose of which they are instituted are national in their character, and, within constitutional limits, are subject to the control of Congress and are not to be interfered with by state legislative or judicial action, except so far as the lawmaking power of the Government may permit." (italics added.)

¹⁶ *Bedford v. Colorado National Bank*, 91 P. 2d 469 (Colo. 1939), aff'd, 310 U.S. 41 (1940).

¹⁷ See *Bedford v. Colorado National Bank*, 91 P. 2d 469 (1939).

¹⁸ Letter from Howard Shepard, July 27, 1959, to Harry Byrd, Committee of Finance, Senate, State Taxation of Interstate Commerce, 1959, p. 176.

*An ultra vires act by a national bank opens the bank to suit by its stockholders.*¹⁹

A loss may result from a number of causes including the sustaining of a challenge of depreciation deductions by the Internal Revenue Service. If the Comptroller's position is not upheld, one of the consequences would be possible exposure of directors to personal liability to the extent that a loss is sustained. Likewise courts have indicated that a cause of action may be open to depositors and general creditors of the bank, with the officers and directors also personally liable for all damages suffered should an *ultra-vires* act result in loss.²⁰ There is some authority upholding a suit for injunctive relief by the competitors of a national bank which is threatening to exercise some power not authorized by national and state banking legislation.²¹ Whenever state policy or a state law is being threatened, the individual states may bring actions against the national bank.²² In defending suits the bank may offer the defense that the bank is endowed with certain privileges as a quasi-public entity and that leasing is an incidental power necessary to the business of banking. If the state is sustained in its action, with the corollary that the bank is engaging in a commercial activity unrelated to banking, then the Comptroller's ruling may be upset.

It has been assumed by some that challenges to *ultra-vires* transactions are limited to the above, and that parties doing business with a national bank are estopped to challenge the legality of the transaction in a suit brought against them. Closer reading of the cases suggest that this is by no means the law and that the question is still open with respect to the executory nature of the business in which banks hope to engage when leasing equipment.²³ So long as the bank was compensated for past use of the equipment,

¹⁹ *Lantry v. Wallace*, 182 U.S. 536, 553 (1901); *Hansell v. Citizens and Southern National Bank*, 98 S.E. 2d 622 (1957).

²⁰ *Stephens v. Overstolz*, 43 Fed. 465.

²¹ *Commercial State Bank v. Gidney*, 174 F. Supp. 770 (1959); *National Bank v. Wayne Oakland Bank*, 252 F. 2d 537.

²² *First National Bank v. Missouri*, 263 U.S. 640 (1924); *Peoples Savings Bank v. Stoddard*, 102 N.W. 2d 777.

²³ Most of the cases which deny private parties standing to challenge the capacity of the banks to engage in certain types of operation under the national banking laws deal with real estate, either in an attempt by a lessee to defeat an action for rent on the ground that leasing real property was not a proper activity of the bank, *Farmers Deposit National Bank v. Western Penn. Fuel Co.*, 64 Atl. 374 (Pa. 1906), or by a mortgagor to prevent the foreclosure of a mortgage on the ground that under banking legislation prevailing before the First World War, national banks could not engage in realty mortgage transactions. *Kerfoot v. Farmers and Merchants Bank*, 218 U.S. 281 (1910); *National Bank v. Whitney*, 103 U.S. 92 (1880); *National Bank v. Matthews*, 98 U.S. 621 (1878). A major factor behind these decisions was a desire by the court to protect the security of real property titles by limiting collateral attacks

the debt due, and received back in kind from the lessee that which was granted in the first instance, not money as would be the case under a debt but the property as is the case under a lease, the bank would have no grounds for complaint if the lessee raised the defense of *ultra vires*.²⁴

DISCUSSION OF SPECIFIC HAZARDS IN DIRECT LEASING

Risks in Commercial Ventures

A risk results when banks engage in a non-banking activity with the problems faced in any commercial venture. The Comptroller's office claims that, so long

on such titles, *Kerfoot v. Farmers and Merchants Bank*, supra; furthermore the courts in the lease cases were bound by the common law rule that a lessee is estopped to deny the title of his lessor, *Farmers Deposit National Bank v. Western Pennsylvania Fuel Co.*, 64 Atl. 374, 375. In the mortgage-promissory note cases the courts were unwilling to penalize the depositors and shareholders of the bank by depriving them of the benefits of a security arrangement when the negotiation of the promissory note was perfectly valid. *National Bank v. Matthews*, 98 U.S. 621, 626 (1878): "Courts . . . are always reluctant to make a decree which will effect a forfeiture. The bank parted with its money in good faith; under these circumstances, defense of *ultra vires* doesn't address itself favorably." The doctrine that *ultra-vires* acts can be challenged only by the Federal Government may very well be limited to real estate cases and has been so conceded by several courts, *McCormick v. Market Bank*, 165 U.S. 538, 553; *First National Bank v. Aldridge*, 92 P. 2d 674 (1930), and it is by no means authority for other types of banking transactions. To be sure, the courts are unwilling to sustain defenses that the bank acted outside of its authority when the contract had already been executed, as for example where the bank is suing on a promissory note representing a loan to one borrower greater than ten per cent of its capital and surplus. *Gold Mining Co. v. National Bank*, 96 U.S. 648 (1877). Clearly in those cases the traditional doctrine applies denying a party standing to challenge an *ultra-vires* act which has already been completed (i.e., the loan of the money); *Thompson v. St. Nicholas National Bank*, 146 U.S. 240 (1892). Should a borrower be able to defeat the bank's suit in a case of an *ultra-vires* loan the borrower would be receiving an undeserved windfall in being relieved of the obligation to repay his debt, and the creditors and shareholders of the bank would be the parties who alone would suffer.

Clearly insofar as a party involved in an equipment leasing transaction attempted to avoid the future obligations of an executory or uncompleted contract of lease, such reasoning would not apply.

²⁴ Bearing on this matter is the Supreme Court case of *Kuehner v. Irving Trust Co.*, 299 U.S. 445, 455 (1937). The Court stated:

"A sufficient ground for the distinction [between a lease and a debt] is that the petitioners [lessors] get back their property. In other words, they have lost merely a bargain for the use of real estate, whereas merchandise creditors, lenders, and others, recover in specie none of the property or money which passed from them to the debtor." (Italics supplied.)

Several Supreme Court railroad cases have held that where a railroad lease was *ultra vires*, such a lease could not be enforced insofar as the lessee had not yet enjoyed its benefits. *McCormick v. Market Bank*, 165 U.S. 538, 550 (1897); *Pennsylvania R.R. v. St. Louis, Alton & Terre Haute R.R.*, 118 U.S. 290 (1886). Railroads like banks are clothed with a public interest.

Indeed, it would seem strange that a transaction which could be voided by the bank in the future on the grounds of absence of capacity could not be similarly voided by the lessee. The doctrine of mutuality of obligation would seem to require that the lessee or his trustee in bankruptcy has such a defense when attempting to "break the lease."

as the bank does not carry inventory, "transactions in which the economic function of the lessor [or business] have been reduced to a minimum were already an important part of the business of banking" [because] "a bank lent money to a lessor [business] solely upon the credit of the lessee [the business' customer] for the purchase of properties specifically requested by the lessee for its immediate possession and use." There are three basic inconsistencies in this logic. Firstly, the Comptroller claims that the lending of money to a business venture which has a minimum of operating functions is justification for a bank to engage in such venture. Secondly, once a bank owns property leased to lessees, the bank incurs the same obligations and risks as any owner of inventory; the bank in fact has a stock in trade. Thirdly, many segments of commercial business do not inventory merchandise but nevertheless perform credit and financial functions. Food brokers, commodity dealers on the exchanges, drop-shipment jobbers, sales agents, catalogue dealers, and motion picture distributors are just a few of the commercial and marketing enterprises which do not stock merchandise and which perform minimum business functions many of a financial or credit nature. Does this mean that national banks may engage in these marketing and distribution activities? Any logic which would support the Comptroller's ruling as to leasing would be equally applicable as to these other business ventures.

Federal Tax Dangers

Federal tax risks face banks in equating depreciation of equipment owned with amortization under lease. Aside from a few classes of mobile assets, the Guideline Lives for Depreciation under Revenue Procedures 62-21 specify the tax lives of most machinery as longer than would be generally acceptable by, or indeed prudent for, banks as a reasonable term over which the cost of the property should be amortized. Most guideline lives of machinery run from 8 to 18 years. For example, amortizing a lease of machinery over a five-year term (probably as long a term as commercial banks should safely and prudently amortize such assets) and depreciating the asset over an eighteen-year tax life would produce taxable income for the bank arising solely out of the difference between amortization and depreciation. The Revenue Service, furthermore, has refused to rule that a lease may be treated for tax purposes as a conditional sale unless the document conformed to the substance of a conditional sale contract.

Risks from Exceeding Legal Loan Limit

Still another risk may be faced by banks as a result of the authorization, in the Comptroller's letters of

April 30 and October 22, which now allows national banks to exceed their legal limits in lease transactions. In the lease program outlined in the Comptroller's letter of April 30, the inquiring national bank may exceed its legal limit by $3\frac{1}{2}$ times. This bank's legal limit is \$30,000 and the net cost of the equipment (after security deposit) is \$100,000. If the bank involved had the normal ratio of deposits to capital and surplus, a few such transactions might seriously affect the liquidity of the bank and its ability to meet the demands of its depositors.

Possibility of Accounting Changes

A danger that may affect the business community is that leasing and debt may be so merged, by the manner in which banks may document such transactions, as to be the same activity in the mind of the business community. If the Department of Defense ultimately feels that leasing and debt are one and the same, Armed Services Procurement Regulations may be so changed that any portion of rent applicable to a financing charge may not be recoverable by defense contractors. The regulations are now under review by the Assistant Secretary of Defense to determine the allowability of rents under pseudo-leases, debt in lease guise.

If the accountants conclude that a true lease and a debt, two separate transactions, are the same, they may insist upon capitalization of all such transactions upon the balance sheet. Present accounting rules (Accounting Research Bulletin #43) require capitalization of "pseudo leases" as evidences of debt on the balance sheet. On November 11, 1963, the American Institute of Certified Public Accountants circulated a proposed new ruling for accounting treatment of leases which states in part: "Some lease agreements are, in fact, installment purchases of property. In such cases, the . . . property and the related obligation should be included in the body of the balance sheet as an asset and a liability. . . ."

A recent Accounting Research Study, No. 4, *Reporting of Leases in Financial Statements*, by Professor John H. Myers, prepared for the American Institute of Public Accountants, suggests that one determine as to whether or not a lease should be capitalized would be if a bank were the lessor. Professor Myers asks: "Is the lessor a major financial institution? Such institutions . . . are in the business of investing money rather than owning and operating assets . . ." Where taxes are levied on total capital rather than on capital stock or net income, the lessee in many states (for example, Texas and Oklahoma) may be taxed on the capitalized "assets" or "liabilities". Capitalizing commitments on the balance sheet also may precipi-

tate defaults under many indentures where indebtedness is defined in balance-sheet terms. Other complications might result.

Problems in Overly Permissive Regulation

The Comptroller's letter of October 22 may precipitate a host of problems for bank officers and directors when it seeks "to allow the initiative of bankers and their counsel to develop the techniques for handling these problems . . . relating to the transaction of business in other states, problems of taxation and of the liabilities resulting from the ownership of property" before setting up statutory or administrative standards.

The Comptroller claims that "There are similar problems in widespread financing of any kind," but *The American Banker* survey seems to refute this claim:

"Banks are finding that leasing involves a Pandora's box of complex legal, tax and accounting problems that defy quick solutions even by their best attorneys and accountants . . . the administrative headaches are many, the guidelines few . . . those involving depreciation allowances and operations across state lines are by far the most difficult."

REMEDIAL MEASURES

Use of Pseudo Lease to Sidestep Problems

To "sidestep" these problems, some banks have planned to own and lease equipment in foreign states without qualifying out-of-state. These banks may claim shelter from control of the foreign state by contending that leasing is an approved banking activity, constitutes interstate business, and that national banks enjoy a privileged status in engaging in interstate business. A constitutional question may arise when the foreign state claims jurisdiction. Other consequences may be faced such as the impairment of the enforceability of the contract.

According to the *American Banker* survey, one bank plans to "write all its leases" in its home state regardless of where the equipment is to be used in the belief that this would get around many of the local taxes. Presumably a bank may conduct its "lease" operations in foreign states under the Federal Interstate Income Tax law enacted in 1959 which provides that no state may impose a net income tax on income derived from the interstate solicitation of orders for "sales" of personal property where approval of the order and shipment is made from a point outside such state. To take shelter under this law, however, a bank must acknowledge that the transaction is not a lease but a sale. A conditional sale is an evidence of debt subject to legal limit requirements. If the transaction does not conform to the statutory requirements of the

state as to form and content of a conditional sales contract, the penalties to the bank may be severe. A lessee, furthermore, should capitalize conditional sales as debt in its accounting reports.

Affiliate Corporations Irregular.

Some banks have suggested forming affiliate corporations the stock of which they will own, or control through officers or directors, for the purpose of owning and leasing equipment in foreign states and avoiding the necessity of the banks themselves qualifying. Not only is such action prohibited by 12 U.S.C. 24, Paragraph 7, but these banks may be taking themselves back to the period of the 1920's when a series of irregularities caused a later wave of legislation. The Bank of the United States which closed its doors on December 11, 1930, had two such affiliates, the Arnat Leasing Company and the Rex Leasing Company. An earlier Comptroller in his Annual Report mentioned bank affiliates in this way: "These ancillary companies are being used with increasing frequency . . . as a means of enabling banks to do, indirectly through their instrumentality, things which they can neither safely or lawfully do directly."

HOW A BANK MAY PARTICIPATE IN LEASING

How may a bank legally and soundly participate in this growing commercial business?

- A bank may continue to discount leases, which are in effect debt, so that there is no ownership in the bank.

- Another form of debt in lease dress may be obtained through the use of a trustee arrangement. Again, it should be made clear to all parties that a trustee relationship results in a debt financing. The Internal Revenue Service has held under Revenue Ruling 55-25 that such arrangement for tax purposes is to be treated as a conditional sale. Further, under a trust arrangement neither the trustee nor the investor acts as owner, and neither depreciates the asset. A major element of ownership is that the owner has title to the equipment and depreciates the asset. A trustee has only a security interest in the property. Another prerequisite of a true owner-lessor arrangement is that the lessor, as owner of equipment in foreign states, qualifies to "do business" within those states where the equipment is located. The trustee arrangement, according to some counsel, may be used to avoid such qualification because the trustee does not carry with him the requisites of true ownership and is not "doing business". He acts only in a fiduciary capacity under a loan arrangement.²⁵ Under any

²⁵*Maulding v. U. S.*, 257 F. 2d 56 (1953); *McLeod-Nash Motors Co. v. Commercial Credit Trust*, 146 N.W. 17 (1932).

arrangement where a "lease" is in fact an evidence of debt, it should be so regarded by all parties, and so treated for all purposes including accounting.

- Lend to lessors in accordance with normal lending practices. Under such conditions the credit of the lessor itself should be determinative. Standards of liquidity, financial ratios, etc., should govern.

- Lend to a "friendly" lessor. In "Equipment Leasing and Commercial Banks" written by Warren A. Law and M. Colyer Crum of the faculty of the Harvard Graduate School of Business for the Association of Reserve City Bankers, the authors state: ". . . This is a very flexible device. Since the lessor is an independent corporation, there is less question of possible violation of state or national banking laws"

Banks have enjoyed close and friendly relationships with customers in many lines of business. By means of loan agreements having restrictive covenants, a bank may protect itself more completely through lending to a lessor than through a direct lease. Among the covenants in such an agreement would be that the lessor shall be qualified to do business in those states where required; shall make available to the bank all its financial data; shall maintain sufficient insurance protection; shall engage in none other than the equipment leasing business; shall borrow from none other than the bank (controlling which companies may become lessees); shall incur no other debts or obligations nor sell any of its accounts receivable; shall refrain from mortgaging or encumbering any of the leased property, etc. By these and other provisions a bank can exercise close and continual control over the activities of a friendly lessor. Mortgages may be obtained on each unit of equipment and rents may be assigned directly to the bank as additional security for the loan.

There are a number of real economic and legal advantages for a bank operating through a "friendly" lessor:

- ▲ The problem of an *ultra vires* attack is avoided because the bank lends money to the lessor on a traditional basis.
- ▲ The friendly lessor would qualify in foreign states and avoid problems that the bank might incur.
- ▲ The bank has the advantage of having two names on the paper instead of only one. The lessor is obligated under a loan agreement, the lessee under a lease. The lessor's capital and income help support the transaction.

- ▲ The documentation between lessor and bank would be an absolute and unconditional evidence of debt rather than the inferior commitment of a lease. The loan agreement would be supplemented by an assignment of rents and a mortgage on the equipment.

- ▲ Longer-lived assets may be leased without problems accruing to the bank. Bank policy may not allow an amortization period sufficiently long to parallel the life of the equipment. If the bank owned the property, it would find difficulty in participating out an interest in the ownership to the term lender. On the other hand, assuming a sound lessee, a bank would have little difficulty in participating its loan to the lessor to an institutional lender with the participant taking the longer maturities of the loan.

- ▲ The bank would enjoy flexibility in periods of stringent money supply because it would have the opportunity of participating out a major portion of its loans to the lessor during such times. On the other hand, during periods of monetary ease the bank could take a larger portion of the loans within its own portfolio and participate out a smaller portion. Banks that lease directly may find that at times they have an inordinately large share of their funds in illiquid long-term lease financing whereas the friendly lessor relationship provides much greater flexibility for the bank's participation of its loan portfolio.

- ▲ The bank may receive fees from the lessor to supplement its interest income. The fees would be for banking services such as arranging loan participation, etc., and may accord a bank greater leverage if applied as a percentage of all loans to the lessor including those participated.

CONCLUSION

Almost as to confirm that leasing is not a banking activity, a spokesman in the office of the Comptroller is quoted by the *American Banker* as saying in regard to depreciation, local taxes and other leasing problems, "These are not banking questions."

If the rule of law is to be upheld, the impetus must come from that one group to which the Comptroller is answerable, the Congress of the United States. A number of Congressmen have already expressed concern as to the ruling's legal basis. In a May 15, 1963 hearing, Congressmen Multer, Bolton and Brock of the House Banking and Currency Subcommittee on Bank Supervision and Insurance took issue with

the Comptroller on both the economics and legality of the ruling. Others on both the Senate and House Banking and Currency Committees have become aware of the problem. If, however, Congress delays making known its position, most assuredly the courts will not. The possibilities for challenge by so many parties are too numerous, and the manner in which some banks may proceed makes challenges certain.

Although believing that leasing may be an *ultra vires* activity at present, some bankers claim that by the time the courts make their determinations banks will be offering lease programs on a wide front. Thus, in a number of years leasing will have become a generally accepted banking practice and courts will refuse to overturn such transactions which through practice have become "necessary to banking." The Supreme Court has rejected such proposition in the past, stating that, "Illegality cannot obtain legitimacy through practice,"²⁶ and "... even a practice commonly pursued may not be a necessary one."²⁷ By such logic any party who chose to break the law could

do so with impunity by offering the defense that his illegal act became legal merely as a function of the time interval between the date of the act and the date of the court decision. The rule of law would become a mockery.

Although banks enjoy a privileged status in receiving the public's deposits but submit to regulation for the public's protection, it is unlikely that the courts will allow banks, in the conduct of an ordinary commercial venture such as leasing, to enjoy a similar sanctuary. The Comptroller has authorized banks to assume the obligations of ownership. The implications of this approval seem to acknowledge that national banks would incur the same obligations as any owner and lessor of personal property including, for example, those lessor obligations due local authorities. Before the problem becomes a thicket of controversy and litigation, before banks, business and the public suffer, Congress should clarify its policy and position.²⁸

²⁶ *Inland Waterways Corporation et al.*, cited at note 4, *supra*.

²⁷ *Texas and Pacific Railway*, cited at note 5, *supra*.

²⁸ As this article goes to press *The American Banker* of January 16, 1964, announced that Representative Abraham Multer of New York, Committee on Banking and Currency, is filing a bill to prevent national banks from engaging in the leasing business. H.R. 9822

"Large banks are very different from small banks . . . they have more money."

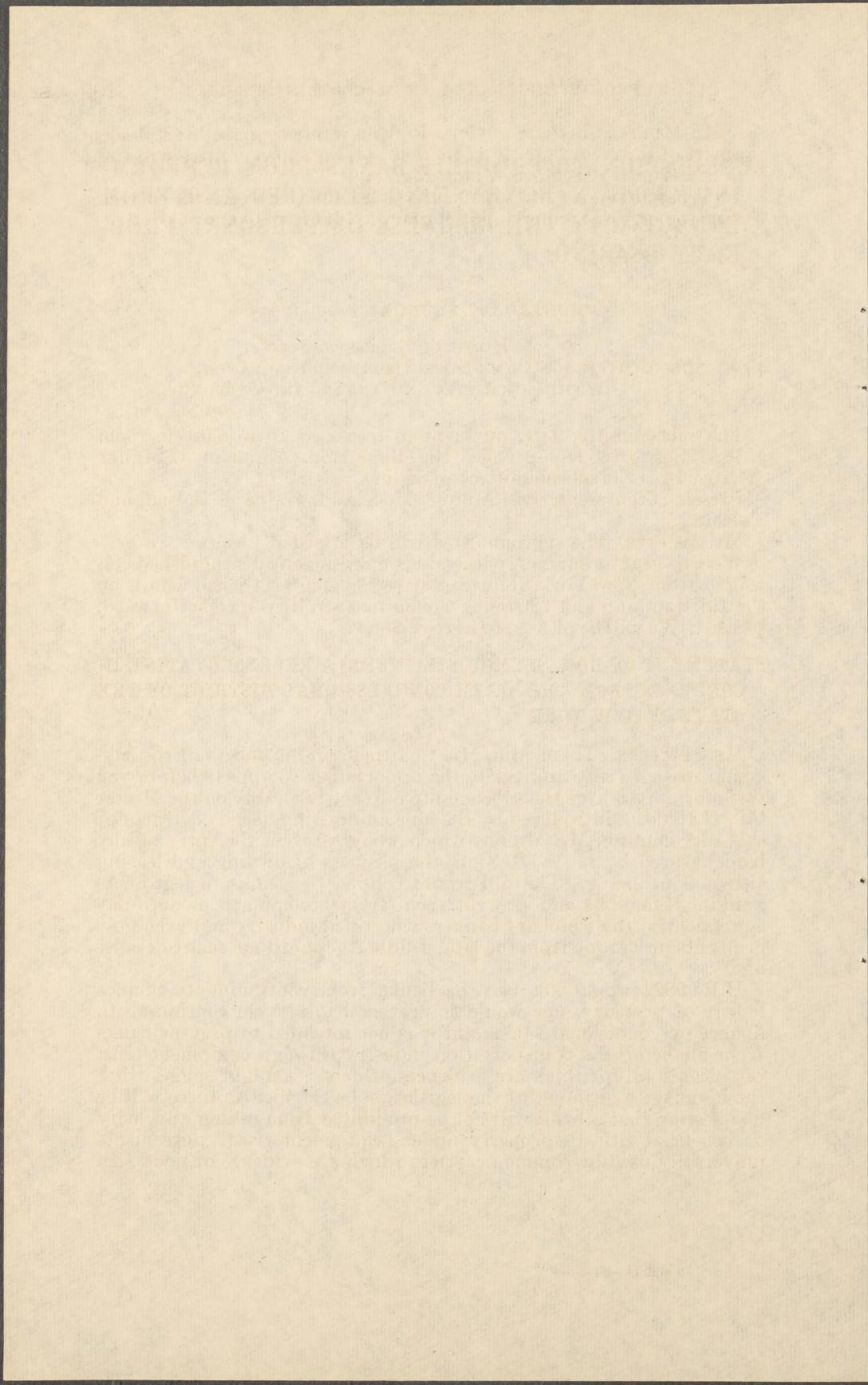
— F. Scott Fitzgerald.

News item from The New York Times, July 18, 1963, on the reaction of the banking industry to the suggestion of compulsory disclosure by banks of certain financial information:

"The banks characterized stockholder information as "red tape" and "unnecessary paper work." Too much knowledge for bank stockholders might lead to public criticism and irreverent discussion of management policies."

Mr. MULTER. Is there anyone else who wants to make his statement a part of the record now? If there is not, the subcommittee will stand in recess until 10 tomorrow morning.

(Whereupon, at 12:15 p.m., the subcommittee recessed, to reconvene tomorrow, Wednesday, February 26, 1964, at 10 a.m.)



LEGISLATION TO PROHIBIT BANKS FROM PERFORMING CERTAIN NONBANKING SERVICES AND FROM ENGAGING IN THE BUSINESS OF PERSONAL PROPERTY LEASING

WEDNESDAY, FEBRUARY 26, 1964

**HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON BANK SUPERVISION AND INSURANCE
OF THE COMMITTEE ON BANKING AND CURRENCY,
Washington, D.C.**

The subcommittee met, pursuant to recess, at 10:15 a.m., in room 1310, Longworth House Office Building, Hon. Abraham J. Multer (chairman of the subcommittee) presiding.

Present: Representatives Multer, Moorhead, Halpern, Bolton, and Talcott.

Mr. MULTER. The subcommittee will be in order, please.

We will hear as our first witness this morning our distinguished colleague from New York, Representative Seymour Halpern, who is on the full Banking and Currency Committee. Will you come forward, please? We will be pleased to hear you now.

STATEMENT OF HON. SEYMOUR HALPERN, A REPRESENTATIVE IN CONGRESS FROM THE SIXTH CONGRESSIONAL DISTRICT OF THE STATE OF NEW YORK

Mr. HALPERN. Thank you, Mr. Chairman and members of the subcommittee. I truly appreciate the opportunity to appear before you this morning to urge the subcommittee to act favorably on the Multer bill, H.R. 9822, introduced by the able and distinguished chairman of this subcommittee, Mr. Multer, which would prevent the entry of any bank insured by the FDIC into the business of owning and leasing personal property. The bill would confine the banks to legitimate banking functions and prevent them from becoming a modern-day equivalent of the merchant bankers who ruled industry and even governments in Europe from the late Middle Ages until not many decades ago.

H.R. 9822 would not bar the banks from continuing to finance lessors of property, nor would it prevent banks from continuing to finance on conditional sales; and it is not intended to prevent banks from financing the transportation industry through equipment trust certificates, all of which are evidences of debt. I might suggest that the language and intent of the legislation be clarified so there will be no question that a bank will not be prohibited from taking a security or beneficial title to property under "equipment trust" agreements universally used by common carriers which are evidence of debt. In

short, it is the intent of this bill to allow banks to continue to finance industry, without them becoming the owners of industry.

Mr. Chairman, the legislation before us would overrule a decision by the Comptroller of the Currency which would allow the national banks to become owners and lessors of personal property.

The reason given by those who favor this position of authorizing the banks to become lessors are: (1) that many lessors who are financed by the banks perform no function other than retailing credit, and thus increase the cost of credit; and (2) that leasing is necessary to the business of banking because it is necessary.

Those who support this view assert that leasing personal property is necessary to the business of banking and is a lawful exercise of the powers of a national bank; but, Mr. Chairman, I have never heard them cite a single legal precedent to support this position. In a recent exchange of correspondence, which I would like to submit for the record, I asked the Comptroller the legal basis for his ruling. He finds an absence of words about leasing in the statute, and, therefore, asserts that leasing is lawful. This conclusion can be reached only by relying on a supposition that what is not expressly forbidden may be done even though it is totally unlike all the usual banking activities which are expressly authorized. I respectfully submit that this is an unreasonable and fallacious type of argument, and should be clearly overcome by approval of the bill before us.

Mr. Chairman, if it is indeed true that some lessors who are financed by banks do not form any function other than that of expensive retailing of credit, then the remedy is not to be found by putting banks into an unlawful business which may endanger their depositors and their stockholders. The remedy may possibly be found in tax legislation which would equalize any differences in the amount deductible by a purchase and a conditional sale and a lessee; or it may be found elsewhere. But it is not to be found in authorizing banks to purchase, own, and lease personal property to their customers.

If the bill before us is not approved, and banks are permitted to own and lease personal property, they will be able to finance industrial or other operations which are not possible under present legal limits on the amount of credit they may extend to one party. The banks organized under the National Bank Act and banks organized under State laws are limited in the amount they may loan to any one borrower; the limit is a reasonable percentage of their capital accounts. Those who hold the banks may lease personal property also hold that these legal limits do not apply when banks act as lessors. This reasoning would allow all banks, small or large, to expand, by in effect removing their legal limits—a real danger to depositors and the public.

If a bank is unable to assist a potential customer with a loan, because its legal limit is too small, it can induce the customer to ask for a lease arrangement. The bank thus will go beyond the limits which all legislative bodies have imposed with respect to the size of credit granted; and to make the deal even more precarious for the depositors and stockholders, the bank will assume the risks of leasing the property as owner. If such deals are successful, the banks' strategic power over the economic system will be magnified; where they are unsuccessful, the banks' injury to the economic system, through over-expansion and consequent loss, also is magnified. It may be recalled

that, in the unfortunate years of bank security affiliates, during the 1920's, one of the largest banks to fail, the Bank of the United States, had two leasing affiliates as well as security affiliates.

Mr. Chairman, economic progress does not require unsoundness on the part of the banks; on the contrary, economic progress can continue only if the banks remain sound. To remain sound, they must stay within the confines of the powers established by Congress over the years after long and extensive study of the needs, the problems, and the reasonable limits of activities on the part of the banks. To insure continued soundness, the present situation, whereby banks may become owners and lessors of personal property, must be corrected by Mr. Multer's bill, H.R. 9822. This will protect the economic health of the banks, the stockholders and depositors and, indeed, the general economy. Accordingly, I urge the subcommittee to approve this most desirable legislation, and I express to you, Mr. Chairman, and to the members of the subcommittee, my sincere appreciation for this opportunity to appear before you and state my views on this important and timely problem for our banking community.

Mr. MULTER. Thank you very much for your very fine statement, Mr. Halpern.

You have indicated that this would apply to banks that are insured by the FDIC?

Mr. HALPERN. I meant those insured by the FDIC as well as others.

Mr. MULTER. The language of the bill is much broader than that. If this bill is enacted in its present form it would apply to all banks, except State banks that are not members of the Federal Reserve System or insured by the FDIC. In other words, all national banks would be covered, all banks that are members of the Federal Reserve System would be covered and all banks that are insured by the FDIC would be covered.

Mr. HALPERN. I would say all to the better.

Mr. MULTER. I think that it would be unfair to cover some of the banks and not to include all of the banks that are subject to Federal jurisdiction.

Mr. HALPERN. Certainly.

Mr. MULTER. There are some legislative restrictions on how far we can go. Your testimony brings up the question, If it is all right for banks to lease personal property, why is it not all right for them to lease real property? Why should not the banks be permitted to buy real estate and lease it?

Mr. HALPERN. The law does not allow them to deal in real estate.

Mr. MULTER. Except property owned for bank purposes.

Mr. HALPERN. That's right; for the bank's purposes only.

Mr. MULTER. The banks can buy a building or erect a building for their own banking use.

Mr. HALPERN. Not for the purpose of leasing to others.

Mr. MULTER. I am excluding the situation of a bank which occupies space in a building it owns, and which rents to others office space in the building it does not require for its own use. Let us assume the bank went into the real estate market and bought an office or industrial building which it did not intend to occupy, and leased it to a business firm.

Mr. HALPERN. That is prohibited.

Mr. MULTER. I think the law presently prohibits such practice. To the same extent that the law prohibits banks from owning and leasing real property it prohibits similar dealing in personal property. The law does not give banks the expressed right to deal in personal property. Banks have the right to lend money on real estate, within limits. But if the regulation by the Comptroller permitting banks to own and lease personal property is correct, why cannot he use the same regulation to cover real estate?

Mr. HALPERN. That is one of the fears.

Mr. BOLTON. I wonder if you could ask the staff to ascertain the status of the law on real estate? I am under the impression that at the very least there is a specific provision in the law which permits them to own real estate for banking purposes. But there is not such a provision, such a specific provision regarding personal property, I do not believe. Again, therefore, on a logical basis, with the exception being specifically in the law, I would think, at least, that the understood rule is that they cannot own the real estate for other purposes, but I would appreciate the staff checking into that.

Mr. MULTER. Mr. Beller, will you do some research on that for us?

Mr. BELLER. Yes, sir.

Mr. MULTER. Please give us the benefit of that by the time we get into executive session.

(The information referred to follows:)

BANK OWNERSHIP OF REAL ESTATE

(12 U.S.C. 29)

"A national banking association may purchase, hold, and convey real estate for the following purposes, and for no others:

"First. Such as shall be necessary for its accommodation in the transaction of its business.

"Second. Such as shall be mortgaged to it in good faith by way of security for debts previously contracted.

"Third. Such as shall be conveyed to it in satisfaction of debts previously contracted in the course of its dealings.

"Fourth. Such as it shall purchase at sales under judgments, decrees, or mortgages held by the association, or shall purchase to secure debts due to it.

"But no such association shall hold the possession of any real estate under mortgage, or the title and possession of any real estate purchased to secure any debts due it, for a longer period than five years."

The Comptroller has ruled that real estate necessary to the accommodation of the bank's business includes real estate upon which the bank buildings are located as well as parking facilities and data processing centers necessary in the transaction of the bank's business. Banks may hold real estate for future banking use where the bank in good faith expects to utilize such property as bank premises.

The Comptroller also has ruled that a bank may retain or transfer to a subsidiary or affiliate for use in the business of the bank, subsidiary or affiliate, real estate acquired by the bank under the last paragraph of 12 U.S.C. 29. The bank may also comply with this paragraph by disposal of real estate so acquired, under an arrangement by which the bank will realize additional compensation upon the ultimate disposition of the property by the transferee where the bank has been unable to dispose of the real estate, except at an unreasonably low price resulting in a substantial loss to the bank, and there is reason to believe a substantially higher price is obtainable for such real estate within a reasonable period.

Mr. TALCOTT. I am a little misapprehensive, because my understanding of what the banks want to do with regard to leasing or deal-

ing with personal property is that they do not want to get into the full-scale leasing business like in automobile rentals, for example, of leasing, repairing, and maintaining—greasing, oiling, cleaning, and doing all of that sort of thing. Banks are interested only in the financial arrangement with a particular customer to assist him in his financing problems, rather than in his ownership, operating and maintenance problems. If I am in error, I would like to have the specific issue clarified.

Mr. HALPERN. I believe that you are in error. They are definitely taking legal title and then leasing. They are buying the property and leasing it to their customers, not just assisting customers with financing.

Mr. TALCOTT. What type of property?

Mr. HALPERN. Well, all types. It could be everything from railroad cars to heavy machinery.

Mr. TALCOTT. Then they are actually maintaining the property?

Mr. HALPERN. In some cases.

Mr. TALCOTT. They are doing the repairs and maintenance work?

Mr. HALPERN. I do not know the exact extent of that, but they do get title to the property and lease it to their customers.

Mr. TALCOTT. This is my question: What are they doing, what do they want to do—specifically, what is our problem here—what is troubling us? If banks are getting into the full-scale rental business, I think that we would find great opposition to it.

Mr. HALPERN. They are in the leasing business. I think that so far as some of the technical aspects to which you have referred are concerned, such as the extent of the servicing, there is a representative here from one of the banks who is leasing, and I believe that he can answer that question.

Mr. TALCOTT. For instance, if a businessman wanted to buy a computing machine, a concrete mixer, and he did not want to buy it himself, he might seek out a bank or some other financier in the community—

Mr. HALPERN. In present practice, the businessman would own the equipment, but the bank would be financing it. That is business they do now.

Mr. TALCOTT. That is what I would like to clarify.

Mr. MULTER. I think the bank witnesses will be able to tell us in greater detail how they operate. The fear has been expressed by the automobile and equipment industries that this practice means that the banks will get into the department store business and the heavy equipment business and all types of equipment business, including the office equipment business. The banks are prepared to buy anything their customer needs and lease it to him instead of financing the customer.

Mr. TALCOTT. Many people seem to be suspicious of banks, but we should not borrow too much trouble until we understand the problem.

Mr. MULTER. Let us not downgrade the banks. They have done a good job in this country. We ought not to be suspicious of them.

Mr. MOORHEAD. Would I be correct in my understanding that this bill, if enacted, would not prevent a bank from lending money to a leasing company on the security of the leases of that company?

Mr. HALPERN. No. That is perfectly legitimate banking business.

Mr. MULTER. That is the traditional method of financing.

Mr. BOLTON. So that the record is clear and we know where we are, there is no question that this bill would not interfere with the bank's right to loan money on equipment and take back a chattel mortgage.

Mr. MULTER. Either on a chattel mortgage or on a conditional sales agreement basis, whether title was passed or not. There is no intent to interfere with the banks' traditional methods of financing, whether as trustee owners under a trust agreement until the loan is paid, or as trustees for other lenders, or in connection with their own loans. Whether the financing involves a conditional sales agreement, where title is retained by the seller, and the bank then takes it from the seller, as security, or there is a chattel mortgage, where title passes to the chattel mortgagee, there is no attempt in this bill to interfere with those traditional methods of financing or extending credit.

Mr. BOLTON. This would be directed toward the banks as the owner in engaging in business other than financing which involved ownership?

Mr. HALPERN. That is correct.

Mr. MULTER. The banks will tell us that this leasing practice is just a change of a method of financing, but I think that this is more than a change of a method of financing. Most States have usury laws, and if banks purchase personal property and lease it to their customers they can easily use this method to evade the usury laws. This is not a change of financing method; it is an entirely new business activity. It is the business of buying equipment and other personal property, and leasing it. The rental income is the result of a business activity, it is not the interest for the use of money.

Mr. BOLTON. If I may, Mr. Chairman, I would like to compliment our colleague on his statement. He has made a very forceful presentation. And I, for one, can say with an entirely open mind I will be interested in hearing the other side. Personally, your presentation should be commended, because you have done a very good job.

Mr. HALPERN. Thank you.

Mr. MOORHEAD. I would like to associate myself with those remarks, because I think that our colleague, Mr. Halpern, has really put his finger on the issue that is before the subcommittee and he is rendering the greatest possible service to the subcommittee in doing so. I commend you.

Mr. HALPERN. Thank you.

Mr. MULTER. The correspondence that you refer to will be made a part of the record.

Mr. HALPERN. I have an exchange of correspondence with the Comptroller in which I took up, as I mentioned in my testimony, the ruling to permit the banks to go into the leasing business. That ruling is based on an omission in the law, rather than anything specific in the law. And in view of the empty basis of that ruling I think that it is a bad precedent to permit the banks to go into the leasing or into any other kinds of business. I will be glad to submit the full exchange of correspondence with the Comptroller.

Mr. MULTER. To anticipate what the banks may tell us, I believe that they will say that the Comptroller's ruling is limited to instances where the bank purchases property and leases it to the customer at the specific request of the customer. Is there any such limitation in the Comptroller's regulation?

Mr. HALPERN. The Comptroller's letter of March 18, 1963, which informed the banks that they could own and lease personal property does refer to property acquired at the request of the customer. I do know that there are small banks in the country which are investing a major portion of their reserves into the purchase of this equipment and leasing it. I think that this is a dire threat to the stockholders and depositors of the banks. I don't feel it was ever intended that they go into this type of business. This is serious and I feel the subcommittee ought to look into every phase of this matter.

Mr. MULTER. Certainly, this is a means and a method to evade any regulation such as we have had from time to time limiting lending to a certain percentage of the cost or the value of the property limiting the term of each loan on the aggregate amount of a class of loans. If banks may buy and lease personal property they will pay the full value to purchase the property and then lease it to their customer. Assuming that a regulation limits banks to a 3-year term on financing by chattel mortgages or conditional sales agreements, under leasing arrangements banks could lease for a 5- or 10-year term, could they not?

Mr. HALPERN. That is exactly it. I think I point that out in my testimony.

Mr. MULTER. Thank you.

(The correspondence referred to follows:)

COMPTROLLER OF THE CURRENCY,
TREASURY DEPARTMENT,
Washington, D.C., January 29, 1964.

HON. SEYMOUR HALPERN,
U.S. House of Representatives,
Washington, D.C.

DEAR MR. HALPERN: Further reference is made to your letter of November 12, 1963, in which you express serious concern as to the legality of the conclusions contained in the Comptroller's letters of March 18 and October 22, 1963, authorizing national banks to engage in the ownership and leasing of personal property.

You suggest that there exists a most serious problem with "regard to the inequity of competition between the national bank lessors and existing business organizations." You state that "the national banks would have access to the depositors funds to carry on their leasing business, a source of money obviously denied to their competitors." You also suggest that "national banks would face serious problems with respect to Federal and State taxation on any personal property owned by them [and] used in leasing transactions, as well as complex difficulties with the corporate qualification requirements, licensing, taxation, and service of process in the various States where a national bank might be held to be doing business as a result of its leasing activities." Finally, you take issue with the conclusion of this Office that national banks, under paragraph 7, 12 U.S.C. 24, have the authority to engage in the direct leasing of personal property and you state that it is this legal question which causes you the most concern.

The question whether the national banks would become "unfairly" competitive under this authority has been carefully considered by this Office. Throughout our private enterprise economy, under the influence of competitive forces, there is a constant search for improved means both of production and distribution. It is not "unfair" for any entrepreneur to devise less costly or more effective means of serving consumers—that is indeed the basic aim we seek under our private enterprise system. Our study of lease financing indicated that transactions in which the economic function of the lessor had been reduced to a minimum were already an important part of the business of banking. In these transactions a bank lent money to a lessor solely upon the credit of a lessee for the purchase of property specifically requested by the lessee for its immediate possession and use. The lessor acted solely as a holder of title and as a nominal debtor. He was a relatively expensive retailer of bank credit necessary only

because a lease transaction required an owner and lessor of property, and because the bank supervisors required an evidence of debt. If national banks are able, under this authority, to provide a less costly means of financing the distribution of commodities and services, that can only be to the advantage of the consuming public. It is the consumer, and not any particular class of producers or distributors, who ought to be safeguarded.

All of the problems which you have mentioned with respect to taxation on personal property owned by national banks and used in leasing transactions, as well as complex difficulties with the corporate qualifications requirements, licensing, taxation, and service of process in the various States where a national bank might be held to be doing business as a result of its leasing activities were carefully considered prior to the letter of March 18, 1963, and have been carefully reviewed on a number of occasions and especially while the letter of October 22, 1963, was being prepared. As stated in the letter of October 22, 1963, these problems are similar to those which exist in connection with widespread financing of any kind. Thus far, however, banks proposing to engage in these activities have demonstrated that they are aware of these problems and are prepared to meet them in a variety of ways.

This Office has given careful study over an extended period of time to the question of a national bank's authority to engage in the direct leasing of personal property. This study resulted in our letter of March 18, 1963. Paragraph 7 of 12 U.S.C. 24 clearly authorizes a national bank to exercise "all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating * * * evidences of debt; * * *." The use of a semicolon at the end of the first clause of the paragraph indicates that the "business of banking" is not limited to the transactions described in the succeeding clauses. It is not necessary to fit lease financing into the narrow confines of the negotiation of an evidence of debt. It is, in fact, necessary to the business of banking to recognize as was stated in the letter of March 18, 1963, that "the leasing by the bank of personal property acquired upon the specific request of and for the use of its customer, and the incurring of such additional obligations as may be incident to becoming an owner of personal property and the lessor thereof, is a lawful exercise of the powers of a national bank and necessary to the business of banking."

Sincerely,

JAMES J. SAXON,
Comptroller of the Currency.

HOUSE OF REPRESENTATIVES,
Washington, D.C., November 12, 1963.

Re the Comptroller's letter of March 18, 1963, authorizing national banks to engage in the ownership and leasing of personal property.

HON. JAMES J. SAXON,
Comptroller of the Currency,
Washington, D.C.

DEAR MR. SAXON: I am writing to express my serious concern, as a member of the Banking and Currency Committee of the House of Representatives, with the legality of the conclusions of your above-cited letter advising the presidents of the national banks that they may, under existing law, acquire title to personal property and lease such property to customers.

In advising the presidents of the national banks you state that "The leasing by the bank of personal property acquired upon the specific request of and for the use of its customer, and the incurring of such additional obligations as may be incident to becoming an owner of personal property and the lessor thereof, is a lawful exercise of the powers of a national bank and necessary to the business of banking. Such direct leasing is, with respect to its banking aspects, substantially the same as the present practice of financing personal property acquisition through a separate lessor. It is our conclusion therefore that direct lease transactions, as above described constitute legal and proper banking activities for national banks."

As I am sure you are aware, opposition to the conclusions expressed in your letter has been voiced by representatives of personal property leasing organizations, who have questioned not only the legality of the views expressed in the

letter, but have also brought to your attention the dubious wisdom of the proposal from the standpoints of sound banking and fair competition between the national banks and commercial leasing organizations.

While I am writing principally to inquire into the legal basis upon which you justify the conclusions of your March 18 letter, I nevertheless would like to suggest that a most serious problem exists with regard to the inequity of competition between the proposed national bank-lessors and existing leasing organizations. The national banks would have access to depositors' funds to carry on their leasing business, a source of money obviously denied to their competitors.

Additionally, the national banks would face serious problems with respect to Federal and State taxation on any personal property owned by them used in leasing transactions, as well as complex difficulties with the corporate qualification requirements, licensing, taxation, and service of process in the various States where a national bank might be held to be doing business as a result of its leasing activities.

Nevertheless, serious as these problems of competition and sound business practice are, it is the legal problem which causes me the most concern. The National Bank Act (12 U.S.C. 24, clause 7) sets forth the authority of the national banks as follows: "To exercise by its board of directors or duly authorized officers or agents, subject to law, all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, coin, and bullion; by loaning money on personal security; and by obtaining issuing and circulating notes according to the provisions of this title."

Such authority includes discounting of evidence of debt, and I am aware that under this authority banks have traditionally financed conditional sales, chattel mortgages, and other evidences of debt which had the form only of leases. However, in these circumstances, the "lessee" possessed all the legal attributes of ownership of the "leased" goods and could generally acquire full title by the payment of a nominal sum at the end of the "lease," while the "lessor" had an unqualified right to receive the total "lease" payments.

In contrast to such an essentially deferred purchasing arrangement, the lease contemplated by your letter of March 18 is a true lease, which would involve the national banks owning and leasing personal property and exercising all the duties and responsibilities of such ownership and business activity.

I look in vain for any authority for such a practice in the authorizing sections of the National Bank Act. On the contrary, I believe that the statute, as strictly construed by the courts, forbids ownership and leasing of business equipment, automobiles, or any other personal property by national banks. I know of no legal authority for the position that owning and leasing personal property is an incidental power of national banks which is "necessary to the business of banking." The courts have held that "national banks may take personal property as security for loans, or as security for bills of exchange purchased by them, but national banks have no power whatever to deal in merchandise of any kind, or in stocks or bonds" *Leonhardt v. Small*, 117 Tenn. 153 (1906). The U.S. Supreme Court came to the same conclusion in *First National Bank v. National Exchange Bank*, 92 U.S. 122 (1875), where the Court said "Authority is thus given to transact such a banking business as is specified, and all incidental powers necessary to carry it on are granted * * * dealing in stocks is not expressly prohibited; but such a prohibition is implied from the failure to grant the power * * *." Additional cases are cited for the same proposition at 7 American Jurisprudence, section 172.

I am not concerned with whatever personality must be taken over to protect the banks on such transactions as defaulted notes, for these are true banking transactions in the first instance. But the principle is clear that national banks are prohibited from engaging in any activity not granted by the National Banking Act. This is as it should be, for the protection of depositors and the general public, and in accord with the authority of Congress to establish the limits of activities by the national banks.

As previously stated, I am deeply concerned by what I believe be the lack of authority for the Comptroller's letter of March 18, 1963, permitting national

banks to own and lease personal property. I would, accordingly, greatly appreciate it if you would consider the questions I have raised herein and advise me at your earliest convenience regarding the legal authority upon which the March 18 letter was based.

With kindest regards.

Sincerely,

SEYMOUR HALPERN, *Member of Congress.*

Mr. MULTER. Our next witness will be Mr. Cooper. Will you come forward, sir, and identify yourself for the record and your affiliation and introduce your colleagues who are with you.

STATEMENT OF G. EDWARD COOPER, CHAIRMAN, BANK MANAGEMENT COMMITTEE, THE AMERICAN BANKERS ASSOCIATION; ACCOMPANIED BY CHARLES W. McCOY, PRESIDENT, LOUISIANA NATIONAL BANK, BATON ROUGE, LA.; AND CHARLES R. McNEILL, DIRECTOR, WASHINGTON OFFICE, THE AMERICAN BANKERS ASSOCIATION

Mr. COOPER. Mr. Chairman and members of the subcommittee, my name is G. Edward Cooper. I am chairman of the Bank Management Committee of the American Bankers Association and executive vice president of the Philadelphia National Bank, Philadelphia, Pa. I am accompanied here today by Mr. Charles W. McCoy, president of the Louisiana National Bank of Baton Rouge, La., and on my left Mr. Charles R. McNeill, director of the Washington office of the American Bankers Association.

In view of the fact that I have a statement to present on both bills, and in view of the questions of previous witnesses, I would ask your permission to have Mr. Robert D. Syer, vice president of the Bank of America, join us. He is scheduled to be the next witness. It may help the committee in its questioning.

Mr. MULTER. Certainly. Mr. Syer, will you please come up and identify yourself for the record?

Mr. SYER. My name is Robert D. Syer, and I am a vice president of the Bank of America in charge of the bank's leasing division.

Mr. MULTER. We are pleased to have all of you gentlemen here with us.

Mr. Cooper, you may proceed either by putting your full statement into the record, reading it, or proceed as you please. If you put your complete statement in the record, then you may summarize it. And then you may call upon any of your associates to answer questions that you cannot answer yourself.

Mr. COOPER. Mr. Chairman, we appreciate the opportunity to appear before your subcommittee on H.R. 9548 and H.R. 9822. Speaking first to H.R. 9548, the American Bankers Association is strongly opposed to this bill, which proposes the establishment of broadly defined restrictions on the services which federally insured banks may perform for their customers.

Under the terms of this bill a bank would be prohibited from extending to its depositors, borrowers, or other customers any service, whether performed manually, or by machine, which is not a "necessary incident" to the proper discharge of the bank's functions as a depository, lender, trustee, or agent. This applies to any service. The testimony yesterday was centered around computer operations,

but there are many other situations unrelated to computer systems which we will cover later in our statement.

This prohibition would apply to all banks, large and small, national or State chartered, commercial or mutual savings banks insured by the Federal Deposit Insurance Corporation. So broad and far reaching are the prohibitions contemplated in this legislation that it is virtually impossible to determine with any precision the multiplicity of the established service relationships between banks and their customers which would be affected, in fact invalidated, were H.R. 9548 to be enacted.

It should be noted that the bill itself makes no serious effort to specify the particular services which banks would heretofore be proscribed from offering to their customers. Instead H.R. 9548 proposes to leave this monumental task of construction and interpretation to the three Federal bank supervisory agencies to be spelled out at some later date in administrative rules and regulations.

Mr. Chairman, there are today nearly 14,000 insured commercial banks in the United States whose services are made available to the public through over 27,000 banking offices. The customers of these institutions include every conceivable type, category, and class of individual, association, and business enterprise—from the individual who may desire only a minimum of banking service to the multimillion-dollar corporation with its subsidiaries and affiliates, which looks to the bank not only as a depository but also as a lender, a financial consultant, a transfer agent for its securities, and perhaps as a trustee for its employee pension program. With an industry whose clientele is so varied and diversified we believe it is not possible to establish a body of rigid and inflexible rules and regulations designed to apply to all banks—the unit bank and the multioffice bank, the cattleman's bank and the industrial bank, the suburban bank and the metropolitan bank—which will specify which customer services are a "necessary incident" to normal bank functions and which services are not—permitting the former and prohibiting the latter. Any effort to devise and enforce such a body of rules and regulations can only result in arbitrary and impractical results which would assuredly operate to the detriment of those who look to banks for financially associated services.

It is the role and purpose of banks to serve the financial and commercial transactional needs of the general public. If we acknowledge, as we must, that the financial needs of both individuals and businesses are constantly undergoing change how can we seriously propose that the nature and scope of the services which are to meet these financial needs shall remain static and immutable.

I might digress to say that I have been in this business of banking for 38 years, and through that time there have been ever-increasing demands on the part of customers for new and different types of services. In the last 5 years these demands, particularly from corporate customer, these requests for service have greatly accelerated.

Traditionally those seeking banking services have looked to their local financial institutions for more than just simple and stereotyped deposit and lending functions. And banks have historically provided more. Take, for example, the multitude of banks in the agricultural sectors of this country which employ personnel specially qualified to

advise with their customers on such matters as developing techniques in soil conservation, crop improvement, and livestock feeding. Are such services a "necessary incident" to the depository or lending functions of these banks? As a general rule the answer would be "no." But should these services, nonetheless, be made available? The American Bankers Association believes that banks have an obligation to provide auxiliary services of this type and we are convinced that the overwhelming majority of bank customers would concur in this view.

If we agree that agricultural consultation is a normal and desirable auxiliary service for a "country bank," is it then any less desirable that a metropolitan bank which specializes in accounts receivable financing should be prepared to provide its business customer with accounts receivable recordkeeping if they choose to obtain this additional service from their bank? As a direct parallel to the provision of agriculture consultation by "country banks" today we find a growing number of metropolitan banks providing their corporate customers with "management science" services. What these illustrations point up is that what may be desirable or needed for one community may not be for another. But this is not a decision that can be made in advance by statutory restrictions and it cannot be prejudged in rigid administrative rules and regulations. The desirability of a banking institution providing certain auxiliary services to its routine banking functions can only be properly and fairly judged in the context of the financial needs which a particular bank is called upon to service. The American Bankers Association, therefore, sincerely believes that it is far wiser to permit the Federal and State bank supervisory agencies to deal with specific bank service problems through their general regulatory and supervisory practices and procedures. If a bank is clearly engaged in a service or a profitmaking enterprise which bears no reasonable or practical relationship to its fundamental banking functions, we are satisfied that Federal and State bank supervisory agencies have the present legal authority to prevent such practices and we are confident that this authority will continue to be exercised in the best interests of banking and the general public.

In this connection we are not aware that any State or Federal bank regulatory agency is asking for any special regulatory authority of the type proposed in H.R. 9548 due to any concern that banks are presently placing their overall financial position in jeopardy through the provision of auxiliary services to their functions as a depository, lender, trustee, or agent. As a matter of fact there can be no doubt as to the present authority of such agencies to cause such services to be discontinued, if there is, in fact, evidence that the provision of such services threatens the solvency or financial stability of any banking institution. For it is a primary function of all bank supervisory agencies through their examination and reporting procedures to identify and eliminate any unsafe or unsound practices engaged in by banks which have the potential to impair or undermine their overall soundness.

Another aspect of this proposed legislation which must not be overlooked is the potentially adverse effect its literal application could have on correspondent banking relations. Today many small banks obtain a variety of services from their city correspondents which may

not be a "necessary incident" to the performance of their legal functions as depository, lender, trustee, or agent. Such services include bookkeeping and recordkeeping for demand deposit accounts, savings accounts, mortgage servicing, installment loan accounting, et cetera. Recently associated with certain of these services is the reporting of interest and dividends to the Internal Revenue Service and to customers. Other services, and most important to the country bank correspondent, are of an administrative nature such as investment advisory, market research, management and personnel training. Included in the foregoing are services provided on a widespread basis through the efficiency and economy permitted by the advent of automatic data-processing equipment. Many small banks at present cannot afford such equipment. Likewise many small banks are located in areas which do not have the local service bureaus equipped with automatic data-processing machines. Yet these banks desire to participate in and profit from the benefits available through automation. It is only natural therefore that they have sought these auxiliary services from their city correspondent banks.

The country bank is obtaining this business service from an institution with which it regular deals and from an institution which understands the problems and needs of a banking institution in general and more particularly the problems and needs of a specific bank which may have been a correspondent customer for a generation. The American Bankers Association cannot believe that it is the desire of Congress to destroy such longstanding and essential business relationships.

Enactment of this legislation would also interfere with the installation of automatic data-processing equipment by small- and medium-sized banks. Many of these banks are able to install such equipment because they can use the excess machine capacity for financially related services for their customers. If limited to servicing the banks needs only, many banks would find it financially prohibitive to purchase or lease such equipment.

If the commercial banking system is to service individual, corporate, and correspondent bank accounts adequately and efficiently, every banking institution within that system must be constantly alert to the emergence of new techniques and services which are vital to the continued growth and well-being of our national economy. In keeping with this obligation to service and progress, a sizable number of banking institutions are installing automated equipment to be utilized in carrying out their day-to-day recordkeeping and administrative responsibilities.

With the advent of these technological advances and improvements it is now possible for banks to provide long-established services more quickly, more accurately, and more economically. It has also been possible for banks to advance and improve the character of long-established services. Illustrative of the improvements available through automation are the changes which have occurred in payroll services to business organizations. For many years banks have provided payroll services to corporations and other businesses in which the bank through a series of bookkeeping transactions credits net salary amounts to the bank accounts of officers and employees of the corporation and at the same time debits the corporate account for the aggregate sum of these salaries. With the advances available through

automation it is now possible for a bank to accept gross salary schedules from a business and to make the necessary computation of deductions for taxes and employee benefits thus arriving at the net salary figures from which the credits and debits to the various accounts are then made. By providing this thoroughly integrated payroll service it is now possible for an automated bank to provide its corporation customers with all of the necessary salary and wage reports which may be required by its employees and the Internal Revenue Service.

Another service which has undergone dramatic improvement through automation is that termed "account reconciliation." It is a service which has been performed by some banks for a good many years. Account reconciliation is nothing more than the preparation of a customer's demand deposit statement in a manner which permits the customer to determine more quickly which of his check payments are still outstanding. The usual procedure is for the bank to send a statement of account to the customer with paid and canceled checks sorted and listed in numerical sequence. Such a listing immediately pinpoints the serial number of checks still outstanding and the statement presented in this form permits the customer or his accountant to very rapidly determine the current balance in a particular demand account. With automated equipment for the sorting and sequential listing of checks required for account reconciliation, it is now possible for banks to make this service more widely available and at a substantially lower cost than was previously possible with a manual system.

These are but two examples of the advancement available to banks and their customers through automated systems. These two services are clearly associated with routine banking functions and we believe bear a practical and useful relationship to such functions. But it is not at all clear that such services are a "necessary incident" to the performance of the functions of a bank as a depository, lender, trustee, or agent. It seems to us highly questionable that such improvements as these in bank customer services should be jettisoned, but such a result is altogether possible if H.R. 9548 were to be enacted.

As noted in the foregoing discussion of "integrated payroll service" and "account reconciliation" both of these services are associated with the functions performed by banks as a depository. This association with traditional bank functions is typical of the vast majority of bookkeeping, clerical, and recordkeeping functions now being offered by commercial banks to their customers. Basically they involve merely the processing and organization of financial data as opposed to the rendering of advisory services or auditing functions such as those normally provided by members of the accounting profession.

While these business services are generally bank-oriented or related to a traditional banking function, it is likewise true that some of these services are available and obtainable from business institutions other than banks. Many banking customers do in fact obtain these services from business enterprises other than banks. It is perhaps this competitive feature which has caused certain business groups to seek and support legislation aimed at denying banks the right to offer these auxiliary financial services to their customers. The American Bankers Association views with great concern any suggestion that bank customer services should be arbitrarily and artificially circumscribed simply because banks are found to be competing with other institutions in offering certain services. Any such proscription against one class of

business and in favor of another seems to us to be in sharp conflict with a fundamental precept of our competitive, free-enterprise economic system, which allows the public freedom of choice among organizations offering the same types of services.

If we are to maximize the benefits to the general public from the technological advances that are being achieved in the broad field of automatic data processing, it is essential that these services be made available through the greatest number of sources possible. Certainly in the area of financial transactions there is no more logical source for these services than the commercial banks of the United States. If banks are denied the privilege of providing such financially associated services, it is the general public which will suffer. For this reason, more than any other, the American Bankers Association earnestly recommends against the adoption of H.R. 9548.

In summary, the proposed legislation would, if enacted:

First, legislate that which should be determined—and reconsidered from time to time—by the bank supervisory agencies (this in fact is being done today in bank examination);

Second, require definition of “banking service” and “nonbanking service” which at best could be only arbitrary and as a result cause considerable confusion;

Third, it would deprive the business community of modern and complete banking services; and

Fourth, it would deprive small banks throughout the country of many services of their correspondent banks.

That concludes my statement with regard to H.R. 9548, on behalf of the American Bankers Association and we now wish to proceed with a statement concerning the other bill, H.R. 9822.

Mr. MULTER. I suggest that you do so.

Mr. COOPER. Mr. Chairman, I should now like to comment briefly on H.R. 9822, a bill which proposes to prohibit any federally insured bank from entering directly into the leasing of personal property as the owners and lessor of such property. The American Bankers Association respectfully recommends against the adoption of this legislation.

The reasons for opposing the enactment of H.R. 9822 are substantially similar to the objections which we have raised to the adoption of H.R. 9548. Here again it is the view of the American Bankers Association that H.R. 9822 would impose an unnecessarily rigid and narrow limitation on the ability of commercial banks to fully serve the commercial and financial needs of the areas in which they operate. We believe a far better approach is to place reliance on the regulatory and supervisory processes and procedures of Federal and State banking agencies to deal with any imprudent exercise of personal property leasing powers by specific banks. We question the desirability of regulating specific types of transactions by statute.

The use of the “financial lease” as a credit device or financing instrument is a comparatively recent development. There are several reasons for a business to prefer the leasing of equipment and other personal property over borrowing for outright purchase, but the most frequently stressed is that it frees working capital for other uses which may be more productive.

From the very early stages of development of equipment leasing commercial banks participated indirectly in equipment lease financing

arrangements. They have assisted in developing lease agreements, so as to make them "bankable," and they have made loans in various forms to equipment leasing firms. The entry of commercial banks into the direct leasing of equipment and other personal property has been stimulated by an administrative ruling of the Comptroller of the Currency which concludes that such arrangements are permissible for national banks. This construction of the national banking laws was issued by the Comptroller of the Currency in a letter to all national banks dated March 18, 1963. Prior to the Comptroller's ruling national banks confined their involvement in equipment leasing to the financing of equipment leased by a bank customer from a leasing company—either on the basis of a chattel mortgage and the assignment of rental executed by the lessor, or on the assignment of the lease to the bank.

It should be clearly understood that the ruling of the Comptroller does not grant to national banks an unlimited authority to enter into all types of direct leasing of personal property. The Comptroller in his initial ruling and in subsequent letters commenting on that ruling has made it unquestionably clear that the authority of national banks to engage in direct lease financing transactions is entirely a financing power and in no sense a merchandising power. National banks may not purchase equipment or other commodities for stock and hold them for eventual anticipated lease or sale. They may purchase only on the specific request of a customer who wishes to have the full and immediate use of a specific item of equipment on a lease basis.

The American Bankers Association concurs with the view of the Comptroller of the Currency that direct leasing is a bona fide financial service which commercial banks should be permitted to provide in response to the credit needs of their customers. For this reason the American Bankers Association respectfully recommends against the enactment of H.R. 9822. Thank you.

Mr. MULTER. I hope, Mr. Cooper, that I do not embarrass the American Bankers Association when I take a sentence at the top of page 9, verbatim from your statement, and use it in support of H.R. 258, to wit, that the American Bankers Association indicates vigorous opposition to H.R. 9548 on the ground that it eliminates competition, while at the same time your association opposes enlarging the opportunity for savings and loan associations and savings banks to compete for savings with the commercial banks. I would like to have your comments in the light of what you say here in opposition to this bill, about the fundamental precept of competitive free enterprise economic system as it bears on thrift institutions.

Mr. McNEILL. If I may I would like to comment briefly on that, since I was concerned with the testimony referred to. Our comments on that bill have to be associated with the general need to maintain the safety and stability of our monetary and financial system particularly in connection with the operation of depository and lending functions. Mr. Chairman, as you yourself have stated on many occasions, banking generally has to be very closely supervised both as to its depository and lending functions. Our position on these bills to which you refer is that if other institutions are to be afforded the same type of depository and lending functions then in the interest of the national economy they should also be subjected to the same type of regulation, supervision, and taxation.

Mr. MULTER. This is just dragging something in to befog the issue. We are not dealing with taxation at all. We are not concerned with the question of whether or not they should pay more or less taxes. You present that question to the Committee on Ways and Means almost every year. You have been getting so-called tax equalization from that committee, despite the resistance of the mutuals and co-operatives. That is not the issue here.

Do you believe in the free enterprise system or do you not? Do you believe in the free enterprise system to the extent of keeping enterprise free in the banking industry? Do the commercial banks believe in keeping all competition out while at the same time urging that they have more power and authority to do things that are not part of the banking function? The commercial banks want more power to compete in the mortgage market with the thrift institutions. But when it comes to this bill, the commercial banks say, "never mind what we say about keeping competition out. We want to do this job because we can do it as well as the others, and never mind about keeping competition out." Do I appraise what you have said here in opposition to this bill correctly?

Mr. McNEILL. If I may make one more comment, I did not refer to the tax measure at all. I agree that we have advocated such taxation. And I also agree that it is properly before the Ways and Means Committee. My reference in my original response to your question was in terms of bank supervision on questions of liquidity, reserve requirements, and related matters.

Mr. MULTER. Without intending to get into a conflict with the witness, Mr. Cooper says: "it should be left to supervision," and on the other side you say: "never mind the supervision." Where do we draw the line?

Mr. McNEILL. We are asking for supervision in both cases. So far as changing authority as to the mutual savings banks, we are asking for the same kind of regulation.

Mr. MULTER. I cannot think of anything that lays down the supervisory standards to a greater extent than H.R. 258.

Mr. BOLTON. If I may.

Mr. MULTER. Mr. Bolton?

Mr. BOLTON. I have two comments. I think the comment on taxation is not a reflection upon the witness.

Mr. MULTER. Oh, no.

Mr. BOLTON. It is upon the methods with which the Congress works, because from the standpoint of either the savings and loan associations or the banks, it is a total picture. It is not a segmented picture as we have to consider legislation here in the House.

Secondly, I would respectfully direct the chairman's attention to the fact that H.R. 258 is not under consideration this morning.

Mr. MULTER. While it is not before this subcommittee now we will go into executive session on H.R. 258 tomorrow. We do have testimony of the American Bankers Association before this same subcommittee to the opposite effect.

Mr. BOLTON. I agree, but not in this hearing.

Mr. TALCOTT. The difficulty here seems to be to cope with every bill.

Mr. MULTER. I am in complete agreement with you. I am pointing out what the American Bankers Association has done traditionally.

A witness will come in prepared to talk on one bill, and when asked to comment on the testimony of another witness of the American Bankers Association in conflict with his testimony on another bill, he is unable to comment.

Mr. TALCOTT. That is true of Congressmen, too. [Laughter.]

Mr. COOPER. If I may, the savings and loan associations have asked for permission to become a part of the bank service corporations and we have not objected to their being authorized to form bank service corporations. We have felt that they should have the right to do so, but under their own service corporation, not otherwise.

Mr. MULTER. Did the American Bankers Association take a position on the recent change in the law in the State of New York permitting savings and loan associations to call themselves banks?

Mr. McNEILL. The association traditionally has not entered into legislative hearings in the States. Any action there would have been taken by the New York State Bankers Association and I am not familiar with what they did.

Mr. MULTER. Let us discuss the details of your testimony, Mr. Cooper.

On page 3 of your statement you refer to "management science services." What are "management science services"?

Mr. COOPER. Mr. Chairman, I should like to call on my associate, Mr. McCoy who has first-hand information on this particular question and he can elaborate on it.

Mr. McCoy. My name is Charles McCoy. I am president of the Louisiana National Bank in Baton Rouge, La. I would like first of all to say that we feel that we are somewhat of a small bank, with 167 employees, \$78 million of deposits. We are especially small when it comes to computer complexes.

Two years ago we were confronted with this problem and we placed an order for a computer that was delivered one year later, but at the time we knew that we could not justify its expense on the bank's work alone. We would have to do correspondent deposit accounting to justify this added expense.

Mr. MULTER. You say "correspondent." Does that mean other banks?

Mr. McCoy. Yes, sir. To date we are doing it for only one, with another bank going on the first of March.

Soon after we received this equipment we received an unsolicited request from a large petrochemical industry in Baton Rouge, La., asking us if we would do their payroll for them. This payroll was being made up by the service bureau in New Orleans 90 miles away. The reason the request came to us was twofold. First of all, the payroll had been delivered late to the company on several occasions; therefore, embarrassing them with their employees and causing some union troubles.

Secondly, the service bureau was not capable with the equipment that they had of making the distribution as to labor cost of plant to the departments and to jobs. We were requested to make 13 deductions from the pay; also the various distributions.

This employer has about 650 employees. We make up payrolls for some of them on a weekly basis and some of them on twice a month basis. These are checks which are delivered back to the company

which they, in turn, deliver to their employees. Our most recent case of being solicited by a company was a large chemical company in Baton Rouge, La., who came to us and said that they were buying a plastic division of another chemical company which included three plants. This successor company did not have equipment that was compatible with the computer complex that was being used in the predecessor company. They told us that we could handle this job, because our equipment was compatible. It would speed up the merger by from 5 or 6 months. They were able to take it over in 30 days because we were able to handle the work.

This service includes 42 management reports that go to management each month.

Mr. MULTER. What is the nature of these reports?

Mr. McCoy. Covering accounts receivable, inventory control, plant output, plant inventory, et cetera. It is all programed. It was programed by the predecessor company. We just lifted the program, handed to our computers, and we are doing the work that was previously done by the predecessor company.

I would like to say that all of the work that we do—and we do quite a large amount of work, trying to justify the cost of the computer that it costs us in enabling us to service our customers, is to give them the advantage of that computer and the like. And all of the jobs that we do are for fees. There is nothing done otherwise.

Secondly, we run no ads. We have not advertised this service. It has all been by referrals. The referrals are now in such a volume that we are able to pick and choose.

There is a service bureau in Baton Rouge that is operated by a doctor. It is the only one in Baton Rouge. He bought some equipment having in mind doing his own work on it and then he offered the service to other doctors. He tried to branch out into other fields.

The other service bureau in the State of Louisiana, other than in New Orleans, was one in Lafayette which was an insurance company who once again, like the bank, was trying to get back some of its cost. They have since found it impractical and have withdrawn from the service work.

You asked one question that Mr. Cooper has asked me to comment on.

We have an alumina plant in our area. They produce alumina from bauxite which is converted into aluminum. They have come to us asking us to work with them on a regression problem. This is very technical, way over my head, way over the heads of any of the people that we have, but this problem is being worked out at the laboratory at LSU and we will program and operate it. This company cannot justify a computer complex, but when this problem is worked out we will then give them the reports that will let them control the production of alumina. And it has been stated to us that with this new process, which is very scientific or very technical, they can hope to increase the production of alumina by as much as 15 percent.

Mr. MULTER. So that as a result of your computer service you are now going to get in the alumina business, too?

Mr. McCoy. We are not going to get into the alumina business, but we are in the data processing business.

Mr. MULTER. Did I understand you to say that this insurance company purchased a computer and was unable to sell its excess requirements for this computer and had to give it up?

Mr. McCoy. Yes, sir. I do not know whether they bought or leased the computer, but they have now withdrawn from the service field.

Mr. MULTER. Did they give it up because the superintendent of insurance told them that it was not within the law?

Mr. McCoy. They did it from a financial point of view.

Mr. MULTER. They could not attract enough customers, then?

Mr. McCoy. That was it, plus that they were not willing to pay the price for the people to operate the computer. We hired some of their people.

Mr. MULTER. How long have you been in the banking business, sir?

Mr. McCoy. Twenty-five years.

Mr. MULTER. You believe that data processing is a banking function?

Mr. McCoy. I honestly believe it is; yes, sir.

Mr. MULTER. This is a service which banks should sell?

Mr. McCoy. That is my contention.

Mr. MULTER. Is it a necessary corollary that banks should not render this as a free service to their customers?

Mr. McCoy. Let me say that it is up to each individual bank how they want to operate it. Our bank feels that it is something that should be done for a fee. We did not solicit the business. One company came to us and offered a substantial deposit which, based upon the income from the deposit, would have paid us an amount equivalent to our charge for the service. Our theory has been that we will charge a fee and we will not look to the balances carried to offset it.

Mr. MULTER. Is the fee based on earning a profit or merely to cover the cost and the maintenance of the computers?

Mr. McCoy. It is hard to determine that because of the unused time and the amount of bank work that is being done on the computer. We tried to take our costs and add a profit margin. We do not know exactly at this point when we are not 100 percent of capacity whether that profit margin goes to helping us get back our costs.

Mr. Cooper. There are some banks who feel that the compensation from balances is the proper way of recovering the cost. And there are some who are operating on a combination of the balances maintained and a fee. The pricing policy within the bank is, of course, determined by the management. We believe that management is responsible to the board and for the overall results and controlling the supervision of it.

Mr. MULTER. That is the next question I am getting to. The law prohibits banks from paying interest on demand accounts. If you were the banking supervisory authority, would you authorize a bank to render this kind of service to a bank's customer without charge?

Mr. Cooper. With some charge, some compensation, either on the balance or a fee or combination thereof.

Mr. MULTER. That is the very point. Banks may not pay interest on demand accounts, but if an account carries a certain balance the bank will give such service to the account for nothing. Would you request approval of that?

Mr. Cooper. If it is a service.

Mr. McCoy. By all means. I think that we are performing services for our customers. We do not interpret it as a payment of interest on demand deposits. Let us take loan services. We counsel with borrowers. We advise them about loans. Some people could say, "You have spent 10 hours with this customer; therefore, that is a compensation on his demand deposit." We do not look at it that way.

Mr. COOPER. Individuals are now being required to pay for certain services. Such a service is collection of checks and paying the checks.

Mr. MULTER. You are charging for the service. He is paying for the service.

Mr. COOPER. Some is by compensating balances and if the balances are not sufficient to compensate, then there is a fee. Basically, the service is part of the service of the bank.

Mr. MULTER. May I ask Mr. Syer to answer the same question? If you were a bank supervisor would you approve of this service being rendered without charge?

Mr. SYER. This is not my field at all. I prefer not to answer it.

Mr. MULTER. Very good.

Mr. BOLTON. May I ask you two gentlemen just one question? What percentage of your computer time is utilized on purely bank records?

Mr. COOPER. The greatest proportion of ours would be for the banks. We have some outside services. I would guess that at the moment it would be 2 to 1—two-thirds on our own and one-third for other services.

Mr. BOLTON. How about you, sir?

Mr. McCoy. This gets into a sticky field. We have a machine that feeds checks into the computer. We do not use that machine for any noncustomer services. But on the computer itself right now we still have some unused time that we are trying to sell. Right now it is about 25 percent bank work and 75 percent outside work.

Let me add this, when we went into this we were told by knowledgeable people that a bank had to have, approximately, some place around 40,000 checking accounts to justify the computer. In some banks, depending upon the other services that they put on the computer, it could be considerably less than that. We have 17,000 checking accounts.

Mr. BOLTON. In other words, could I take it from your statement that you have made this investment as a banker in contemplation that there would be a very large growth in the size of the bank or that if you had it to do over again you would get a smaller computer?

Mr. McCoy. No. To answer your first question we can add that without adding overhead.

Mr. BOLTON. I understand that, sir.

Mr. McCoy. As to the second question, we would still get the same computer, because we still are hoping to do more demand deposit accounting for correspondent banks. This is something that has taken a little time. We know banks whose equipment is not yet obsolete who cannot discard the present equipment, but when it becomes obsolete they will ask for the service and send their deposit accounting to a correspondent. We hope and we feel that this will increase the business in the future.

Mr. BOLTON. I think, gentlemen, that you have to help this committee face the dilemma that it is in—at least, one member is in. As a

matter of policy, in my thinking, if you will let me digress for a moment, whether it be in this matter or any other connected with the financial field, it is my effort to retain the control of the financial resources of our country so as to permit the growth to the point that size is necessary, but to prevent too great a concentration of financial power in any one institution.

The thing that I would hope that you could get across to us, in this computer side of this business, is why the banks should be in, as you have testified, sir, the data-processing business where the bank is using 25 or even 40 percent of its facility, as contrasted to the data advisory business or any other similar corollary of the banking business.

Mr. McNEILL. I want to make it clear what I think from the remarks that Mr. McCoy made before intended to convey to you and I just want to reemphasize that from the point of view of his bank he would not have gone to automatic data processing if he had to plan that the equipment would be used only for internal bank services. There were no available sources for this type of service in his community if he had to look to a machine which would handle only his bank operations.

Mr. BOLTON. I would only argue with that, that if this were a necessary function which would assist the bank, he could have financed a loan and stimulated the development of a data-processing company, which would have accomplished the same thing. This is possible.

Mr. McCoy. Without the bank's work on it to begin with I don't think that it would have been a good loan. At the time we went into this there was not enough data-processing work, other than what we thought our own would generate, to substantiate a service bureau.

I would also like to add one further statement, that ours is primarily a community of national concerns, the largest petrochemical companies in the country have plants in Baton Rouge. We have no loans to these organizations. They do not borrow locally. I do not look upon, let us say, Standard Oil of New Jersey, which has one of its largest refineries there—I do not look upon any data service that we would do for them as being a captive type of proposition. That just is not in my scheme of thinking.

Mr. MULTER. What is the capitalization of your bank?

Mr. McCoy. The capitalization—we are \$2 million capital and \$3.5 million in surplus.

Mr. MULTER. How expensive was the computer?

Mr. McCoy. We have it on a leased basis. You want to know what the lease is?

Mr. MULTER. Yes.

Mr. McCoy. It is \$11,500 a month.

Mr. MULTER. That is a large sum.

Mr. McCoy. At the time that we placed the order it was the smallest machine made by the manufacturers that we ordered it from.

Mr. MULTER. This was custom built to your specifications?

Mr. McCoy. They custom build all of them to a degree, but they take one basic instrument and then change it with modifications.

Mr. MULTER. How long have you had this equipment?

Mr. McCoy. We have had it now for 13 months.

Mr. TALCOTT. Are you trying to suggest that banks are justified in developing any type of machine or equipment for use in the bank, and

then to use it for getting additional business? To take an extreme example, a newspaper printing press might be of considerable value to a bank. You certainly would not be justified in getting into the commercial newspaper or printing business, would you?

Mr. McCoy. What I would like to say is that, as I stated previously, we felt that by getting this machine we could offer demand deposit automatic data processing to correspondent banks in our area which we thought we were in the job of servicing.

Mr. Talcott. You were not able to do that to your complete satisfaction within your bank, and you now want to service other people; namely, the depositors who might be in smaller businesses, such as doctors and dentists?

Mr. McCoy. We are not doing it for doctors and dentists. In fact, I was interested in the testimony given yesterday. We have had quite a few certified public accountants who have come to us with their problems wanting us to handle them. We have had public accountants come, too. Frankly speaking, most of the jobs they presented are too small for us to handle on an economical basis for the customer. We feel that a payroll has to consist of 150 employees to justify the use of our computer.

Mr. Bolton. Let me state this with reference to the question, which is similar to that of my colleague. The banks feel it necessary in order to make reports, to turn out investment estimates and current market analyses and reports on a rather large scale. If because of the progress of the printing business a bank was forced to put in a large press that it could only use up to 25 percent of its capacity, would you feel that the bank was warranted in going into the printing business for its customers, and for those who came to it in order to get printing done for a fee or for a deposit?

Mr. Talcott. For a fee.

Mr. Bolton. This is a problem that we face in our thinking I will say quite frankly.

Mr. Cooper. That is one of the problems of the bill—the terrific problem of trying to define whether it is a necessary incident. We have talked about data processing which is associated with banks. And most of this has come to us from the corporations, the customers, asking for this service. We have worked with the customers, with their lines of credit, and loans, so far as the progress of the companies are concerned. And as a corollary, an associated project, we can let the management of the company know this information, we can furnish them with this information, which gives them a better knowledge to do a better job. We have contributed, therefore, to the economic well being of the community when we do that.

We are not, as was suggested yesterday, engaged in the practice of accounting. We are providing purely recordkeeping and data processing services. We are not taking the reports and analyzing them or giving technical advice and the like, which is the work of the professionals who work with the corporations.

Mr. Multer. Can we work together to solve this problem? Mr. Bolton and Mr. Talcott have touched upon the problem and have highlighted it. Historically the private banker was engaged in many enterprises. He was the merchant in the town or the community who decided to become a banker, too. There were no laws or regulations

saying what he could and could not do. He ran his multifarious business enterprises and was the banker, too. As time went on the community found it necessary to enact laws and regulations to restrict his activities.

Today the banker has no right to do anything except what the rules and regulations say he may do as a banker. That, in very broad terms is the current situation.

Instead of looking at this bill from the viewpoint that banks cannot do anything except what is specifically authorized, let us view it the other way. Banks are properly restricted to banking business and permitted to do only those things that are banking functions. Let banks remain in the banking business, but exclude them from other business or commercial enterprises. Can we get the cooperation from banks to write a bill which will keep them in the banking business and eliminate them from other activities. When we enacted a bill permitting banks to buy computers most of the opposition was from independent bankers, and some from commercial firms. They said that if we let you do this you are going to be selling these services to the public. The law as enacted limits this service to banks and for banking purposes, and is not for servicing the general public. That is the law on the books.

The reports and the debate on this bill will show that it was intended to permit banks to use this equipment for their own use and to service other banks. It was not intended by that law to prohibit banks from rendering this service to other banks.

We could eliminate one of your objections if we should write a statement into the bill that nothing in this bill shall be construed to prohibit or prevent a bank from servicing another bank. That will take care of your correspondent problem. But your bank now services commercial enterprises. Your banking correspondents business is not sufficient to fill up the machine time. If we allow you to service other banks, can we not make sure that your bank will limit its activities to the banking business and keep you out of commercial enterprises?

Mr. COOPER. Mr. Chairman, that does not meet the problem of the country banks giving agricultural services. Such services are probably not a necessary incident for depository function. Is this bill directed to the computer or to all services, to all purposes?

Mr. MULTER. Frankly you have raised something that I did not contemplate. I did not know that there were country banks performing the functions of the Department of Agriculture in giving agricultural services to farmers in that field. I know that country banks handle farm loans. I know that they offer financing advice, but that is no different than similar advice by banks to commercial enterprises in a big city. This bill does not prohibit the banker from giving financial advice. That is what a banker is expected to give.

Mr. TALCOTT. The city banker cannot give the farmer adequate advice.

Mr. MULTER. I understand that some city banks help farmers more than farm banks do. But whether it is the farm bank giving the farmer advice, or the city bank giving the city man advice, this is not prohibited. I do not, and I do not think that any member of this subcommittee would say to a banker, "you cannot give financial advice."

Mr. BOLTON. I think that where we are up against this question—I do not think but what I would agree with the gentleman that the language in the bill is a little broad, because as I mentioned yesterday there are banks which have found, because of the type of loans that they make, et cetera, that they almost get into the management consultant business in order to protect their loans. Perhaps they would object to that term being applied to it. Therefore, I think that the gentleman's point is very good.

Mr. MULTER. Is this in advance of the loan becoming delinquent or after it has become delinquent. It would make a difference. If it is after, then the banks must go in to try to save the loan.

Mr. BOLTON. I think it is entirely dependent upon the valuation of the loan by the bank. Speaking frankly and bluntly, as a fellow new in the newspaper business, I went to a bank that had the reputation for being one of the few banks in the country that made newspaper loans. And I sat down and I spent 2 or 3 days with them. I did not make any loan at that bank, because they wanted part of my back teeth, but if I had they would have provided, in addition to the other services, what I would call management evaluation services which would have permitted me on a management level to gage my enterprise in the way I saw it against other newspapers with whom they had loans; and, therefore, I would have had this expert advice. I do agree that the language in the bill as it is presently drawn raises these sideline question which I am sure were not in the chairman's mind when the bill was drafted.

Mr. MULTER. That is the benefit that we get from these public hearings. We are free to exchange ideas and then we come up with a bill that will be satisfactory to all concerned, having in mind that one who is being regulated is not always satisfied with the regulation. Banks would like to have a free hand. This must be a strictly regulated business. We would like to enact a bill that is fair and proper.

The Comptroller of the Currency has ruled completely different than any previous Comptroller in this area. If tomorrow the present Comptroller were to resign, his successor might issue a different ruling on the subject. At present many State bank supervisors prohibit State banks from engaging in these activities contrary to the Comptroller's ruling. We have a situation where national bank examiners approve certain bank actions under the Comptroller's ruling and the State bank examiners disapprove the same actions by State banks and have done so for a long time.

On this very problem New York State banks are urging the State legislature to pass a law similar to the Comptroller's ruling to permit them to engage in these activities. They are not succeeding thus far. How do we resolve this situation? We want a dual banking system which will permit the State banker and the national banker to compete fairly, and to be subject to the same standards. We do not wish to impose our judgment on the banks' officials who are running the banks. However, there should be similar standards for both the State and the national banks so that each will know the areas in which they may function and compete fairly. How do we meet that situation unless we have a bill which accomplishes that result?

Mr. McNEILL. It is our suggestion in the testimony, that we feel that the banks should be regulated, that it is a matter that should be done by regulation and not something that requires new statutes.

Mr. MULTER. How can we handle the situation without legislation, to eliminate the diversity of regulations on the State and National levels? How can we handle the situation of the present Comptroller ruling one way and his successor's ruling another way? How do we address ourselves to those questions?

Mr. McNEILL. As long as we have State and National banks I think that there will be diversity as between the State and Federal supervision. I do not think that is necessarily a bad thing.

Mr. MULTER. Is this the kind of freedom of diversity we want?

Mr. TALCOTT. Perhaps they should have diversity of freedom.

Mr. MULTER. Should the State banks be prohibited from buying property and leasing it while the national banks are permitted to do so? Is that the controversy you want?

Mr. McNEILL. My suggestion is that the State bank should be governed by State laws and the National banks by Federal laws. And they will be interpreted in each case by their bank supervisors.

Mr. MULTER. We are now dealing with this precise problem. Should there be a diversity of ruling on the state and National levels?

Mr. McNEILL. I see no reason why there should not be.

Mr. COOPER. The bill directs the supervisory authority to establish the necessary regulations, so that you ask them to do that.

Mr. BOLTON. I think that this problem here is one that presents an excellent possibility for overall public good that can be done by the Congress. The Congress has a responsibility of looking at these statutes as they exist, whether it be under the regulation or a lack of regulation by the regulatory authority, seeing whether it is in keeping with its desires.

Mr. MULTER. I would favor establishing uniform standards throughout the country, with regulations that are within the four corners of the statute. This is no different, in my opinion, than the matter of branching. As of today no national bank may branch except to the extent that it is permitted by State law. There is now a movement afoot, as there has been for a long time, to try to change that, so that national banks can branch no matter what the State law may be. The same situation is involved here. Are we going to have this fight between the State banks and the National banks, or are we going to set standards which will be followed by all of them? There are State banks that are not in the Federal Reserve System, but they are not many. There will be some divergence between National and nonmember State banks. We can set standards for national banks. There are some 14,000 banks in the country in the Federal Reserve System or that are insured or are national banks. Not all banks are in the Federal Reserve System. Is it not wise that we get together on the language of a bill, which will be right for all concerned?

Mr. McNEILL. We would respectfully submit that it is not necessary for the Congress to go to that extent to provide uniformity in all banking regulatory standards. It is certainly essential that we have regulation. We agree with that. We do not think that it is necessary in every banking activity to provide uniform State and National bank laws.

If I may refer to the particular bill at hand I would respectfully like to submit a somewhat different interpretation of the Bank Service Corporation Act to that which the Chairman has referred to. It

is our understanding that at that time it was desired to make available to the smaller and medium sized banks an opportunity for a choice of obtaining automatic data-processing services, so that they would be able either to go to their correspondent bank, as many are doing or to finance it themselves on a lease basis, to go to a service corporation, if one were available, or if they wanted to join together to provide the services on a cooperative basis among the group of banks they could do so. The Congress in considering this proposal for a joint effort by a number of banks decided that the services provided by such a corporation should be limited to services provided to banks. It is my understanding that this was only in reference to a bank service corporation.

I also understood that your committee and the Senate committee agreed that after this act had been in operation for sometime you desired to review it, to see whether in practice these bank service corporations could be operated successfully, if they were limited to provide services only to banks and could not furnish excess capacity service to others. And we maintain that in order to do the job in this area it is necessary to have some freedom to go outside of the banking field to provide these services. If there should be any abuses—if banks are going beyond the reasonable operations—they will be observed by the bank examiners and the bank supervisory authorities then have the power to curb unsafe and unsound banking practices. For this reason the bank supervisory authorities should be the ones that Congress should look for recommendations to whether additional legislation is needed.

Mr. MULTER. I respect your views, Mr. McNeill, but it is my very firm recollection that many people called on me at the time we were considering the Bank Servicing Corporation Act and held up the red flag of danger. They were very afraid that if the banks went into the computer business and acquired this equipment, that they would shortly be selling these services to the general public. I then said: "If that happens, Congress will surely pass a bill to prohibit banks from selling such services. The banks will be kept in the banking business." We are right there now. The issue the committee must determine is whether we will let the banks get into this data-processing business. If we let them do that and the leasing business, I see no stopping them. They might just as well be department stores with banking as an adjunct to their other activities. Department stores were once doing a banking business. Banks objected and succeeded in stopping this with the result that very few if any department stores have any banking departments today. Even Macy's discontinued its banking deposit practice. It was the largest in the business. Banks fought that practice.

That is my view. I do not know whether the rest of the committee goes along with it or not. This will be determined when we get into executive session.

Mr. McCoy. Might I make one point in regard to payrolls? This is nothing that the banks have not been doing for years. We have been requested by customers to do so. They would bring in envelopes with the net pay and ask, "Would you please put the cash in it"? And would you do this and do that? All we are doing now with the payrolls is using a faster, more expeditious way of doing the same work.

Mr. MULTER. You were doing that manually when I got my first job in a bank in 1918. Nobody on this committee wants you to stop doing payrolls. I certainly do not desire it. But when you get beyond that—when you get to the point of making up income tax returns and making other reports for industry, I think that you are going too far afield from banking.

Mr. COOPER. As to the question of income tax returns that came up yesterday, I want to be sure to make it clear that banks are not making up income tax returns. We are making informational reports.

Mr. MULTER. In that connection, somebody raised the question, it may have been Mr. Armstrong, that it might help to insert the words, depository, lending trustee or agent in the bill. Nothing in this bill is intended to foreclose a bank from acting as a trustee or an agent, or to do the necessary work as trustee or agent—filing the income tax returns and preparing the returns and getting legal advice of house counsel as to what they can and cannot do. There is no intention to interfere with the bank's function as a trustee or an agent. But we do not want banks selling these services or giving these services away as compensation for carrying an account. The purpose of the bill is to prohibit other than the strictly banking functions.

Mr. Syer has been here all morning and I want his testimony on the record before we close today.

Mr. McCoy. I would like to make one brief comment. We are performing outside services right now for the Federal Government in filing this form No. 1099.

Mr. MULTER. That comment could result in a long discussion on matters outside these bills. Let us not get into that. That is for another time.

Mr. TALCOTT. And we should get the Government out of business.

Mr. MULTER. Except for the Federal banks.

Mr. TALCOTT. The problem is that Mr. Syer has been here for 2 days and we only have 15 minutes for him to testify.

Mr. MULTER. I think that he will be able to run over a little bit if the bells ring. We will be glad to hear you now, Mr. Syer.

STATEMENT OF ROBERT D. SYER, VICE PRESIDENT, BANK OF AMERICA, N.T. & S.A., LOS ANGELES, CALIF.

Mr. SYER. Mr. Chairman and members of the subcommittee, my name is Robert D. Syer of Los Angeles, Calif. I am a vice president of the Bank of America in charge of the bank's leasing division. I am grateful to the subcommittee for the opportunity to make a statement in opposition to H.R. 9822.

The proponents of this bill argue that the leasing of personal property is not traditionally a part of the banking business and, therefore, banks should be forbidden to do it by statute. Our answer to this argument is that if the banking industry is not to stagnate it must be permitted to explore continuously new types of services in order to fulfill the needs of our expanding economy. For example, many voices were raised in protest when the banks first began to engage in consumer lending and it was then argued that consumer lending was not traditional banking. Practically all banks now engage in consumer lending and I submit that the making available of funds for consumer lending through banking channels has been a substantial contributing

factor in the growth of our major industries such as the automobile industry, home appliances, radio and television. Direct leasing is no different. Merely because the direct leasing method of financing is new to banks is not a sound reason for prohibiting the use of the method.

During the past 10 years many industries found that there were definite advantages to them to lease production equipment and other personal property instead of purchasing it. The use of the leasing method freed substantial amounts of working capital for expansion purposes. The demand for leasing was thus created by the businessman and banks were called upon to finance the leasing transactions indirectly.

The Comptroller of the Currency requested his advisory committee of bankers to study the question of whether the banks should engage in direct leasing. The committee recommended to the Comptroller that the banks should be permitted to purchase personal property at the request of a customer and lease it to him. The Comptroller approved and the banks then began to engage in direct leasing.

Banking is a highly regulated industry but the objectives of most banking regulations adopted over the years are related to the safety of the depositor's money and the soundness of the general economy of the country. The permission given by the Comptroller of the Currency last March for national banks to purchase personal property at the request of a customer and lease it to the customer does not impair, in any way, the safety of the depositor's money. On the contrary, our experience has demonstrated clearly that direct leasing by banks is a useful tool filling a definite need and substantially contributing to the industrial growth of the country.

It is important to note that the banks are not permitted under this ruling of the Comptroller to stockpile quantities of personal property but can only purchase for lease when requested to do so by a customer.

The type of leasing that the Comptroller has authorized—so-called financial leasing—is but another means of furnishing term credit to the lessee. The transaction takes the legal form of a lease because there are advantages in particular cases to the use of this form in preference to other forms of credit. However, the underlying purpose is no different from financing a borrower by means of a term loan secured by a chattel mortgage. The basic function of any bank is to use its deposits to make credit available to its borrowers, and leasing is merely another sound means of accomplishing this function.

It has been suggested that the banks are in some way intruding upon the rights of private leasing companies. It seems to us that inasmuch as this is basically a financial transaction, the banks have as much right as anyone to enter into this type of business. The same argument was raised in the 1930's when the banks first began to enter the financial business traditionally occupied by nonbanking finance companies. The objections proved to be groundless and finance companies continue to prosper. We can exist side by side with the leasing companies and the competition is healthy and sound. We anticipate that the leasing companies will continue to prosper and will continue to receive sophisticated and well-rounded services from those banks which also engage directly in leasing.

It is becoming abundantly clear, in the operation of the leasing activity of our bank, that we are able to render better financial serv-

ice because we are engaged in direct leasing. In many instances we were able to supply additional working capital or capital for other purposes to our good customers through the vehicle of leasing, where we might not have been able to satisfy the same requirements had we been excluded from direct lease financing. This is particularly true where the credit situation of the lessee is somewhat complex and one with which we have lived over a good number of years. Thus it seems obvious that the right should be reserved to all banks to offer a "complete" banking service.

Finally, the need for additional jobs has been universally recognized. Additional jobs are produced only by increasing the gross national product. An example of the Government's policy of encouraging expansion of industry is the 7 percent investment tax credit made available in connection with the acquiring of new production equipment. Similarly the banking service of direct leasing makes it possible for our customers to take advantage of the use of new production equipment without the necessity for large capital investment. The authority to lease is certainly a useful tool designed to help accomplish the goal of increasing our gross national product. We submit that there is no necessity for legislation forbidding the banks from using leasing as a financial tool.

We therefore respectfully submit that H.R. 9822 should not be enacted as law.

Thank you.

Mr. MULTER. Thank you, Mr. Syer. There is a difference of opinion as to which came first. I think that consumer lending and non-bank finance company lending came into being because the banks were not fully performing their function and supplying the demand. When banks got around to that point, after having found out that the consumer lending and accounts receivable discounting is good, safe, and profitable business, they went into that business, and they are doing that business today and that is good. If nonbank finance companies and consumer and personal loan companies are falling by the wayside because of bank competition, that is good. It is good for the public, because the borrowers are avoiding extortionate rates of interest. In addition, the lending and banking functions are being carried on by well-supervised banking institutions, rather than by nonbank finance companies which are not regulated to the same extent.

In the second paragraph, on page 3 of your statement, you state:

The transaction takes the legal form of a lease because there are advantages in particular cases to the use of this form in preference to other forms of credit.

Will you elaborate on that, please, and tell us what are the advantages in these particular cases?

Mr. SYER. We can go into several examples, but let us take the example of a company which has run out its string, so to speak, in terms of debenture borrowing, for example, as to the amount of capital investment that it can make. Almost the only way in which they can further expand there is by leasing, without modifying their debentures.

Mr. BOLTON. They could do it by a chattel mortgage.

Mr. SYER. No. There they would be owning the property.

Mr. BOLTON. Therefore, you mean that their credit is so far restricted that they cannot come up with that?

Mr. SYER. If they are long-term borrowers they cannot. Their long-term credit agreements may specifically provide restrictions on capital investment. But having used up the one they may want to go to the other.

Mr. MULTER. Let us explore that for a moment.

Mr. BOLTON. This could be done with the permission of the indenture holder.

Mr. SYER. No, the indenture may be sound. You have a ratio of fixed capital against your indenture, or whatever it is. You may have it in a combination. If you exhaust the one, the only course that you have left is that you must get additional money.

Mr. MULTER. If I walked in to your bank with an indenture prohibiting that kind of transaction would you then buy some equipment and lease it to me, and thereby evade the limitation?

Mr. SYER. Mr. Chairman, I do not think that you are evading.

Mr. MULTER. You are just getting around it?

Mr. SYER. You are not just getting around it. You are making the credit available for the production of goods that you want to use.

Mr. MULTER. As a sound banker would you help me get around that instrument and that obligation in that way?

Mr. BOLTON. It might be with the approval of the indenture holders.

Mr. MULTER. If it is with approval, that is another story. If you cannot get the approval of the lender, would you still buy equipment and lease it to me?

Mr. SYER. Have you ever tried, Mr. Chairman, and I am sure that you have, to amend one of those indentures? By the time you get through amending it you have not any use for it.

Mr. MULTER. I do not have to amend it—if I get their consent, I can do it. If this is a proposition that you as a sound banker can say is a good, sound financial transaction, why would I not go along with it?

Mr. SYER. It is a very cumbersome thing to do. I have done it. You can spend months and years trying to get it amended. Let us say that you have a dozen individuals lending money mixed up in it.

Mr. MULTER. Does the usury law in the State of California apply to corporations? Is there a limit to the rate of interest that a corporation can be charged?

Mr. SYER. Yes, 10 percent.

Mr. MULTER. In some States private corporations are exempt from the usury laws. I know there are many States where that is not so. I think that Florida is one and California, I understand, is another State in which corporations may not be charged more than a certain fixed rate of interest.

Mr. SYER. Are you referring to the lease rentals which we might have?

Mr. MULTER. If a corporation applied to your bank in California to borrow \$100,000 you could only charge a maximum interest rate permitted by statute.

Mr. SYER. No. National banks, with certain minor exceptions, are exempted from the California usury laws.

Mr. MULTER. If I wanted to borrow \$100,000 from your bank, assuming that I am a corporation, the interest rate is 10 percent, that is the maximum that you can charge?

Mr. SYER. No; that is not so.

Mr. MULTER. But if you buy \$100,000 worth of trucks for me, you can charge me much more than the 10-percent rate. You can give me a 10-year lease on the trucks and charge me \$15,000 a year.

Mr. SYER. That is a different concept.

Mr. MULTER. Certainly it is a different concept. But you can very easily evade the statute by using this concept, can you not? If you own the property and you lease it to me, you can charge me anything you please for the rental. You can recover the full cost and other charges, and as much as you want by way of profit without regard to the usury laws.

Mr. TALCOTT. This would be an attempt to get around the usury law and I think it might be held usurious, if the interest was usurious, regardless of the scheme.

Mr. MULTER. Which law is going to take precedence? The State law or the law under which this national bank is operating with the regulation of the Comptroller which says "you may enter into these buy-lease deals?"

Mr. TALCOTT. The usury law is the law of the State.

Mr. BOLTON. They control the rate of interest.

Mr. MULTER. This type of contract is an out-and-out purchase of the property which is leased to the user. Is the Comptroller going to say, "this is all right, provided you show me that your return is not in excess of your allowable interest rate?" What do you say about that?

Mr. SYER. That is theoretical, because I can assure you that we will not get into that.

Mr. MULTER. I might agree with you, so far as your bank is concerned, but how about other banks? I do not want to cast any blanket condemnation on banks, but there are good bankers and there are, unfortunately, some bankers who are not so good. I am using "good" in a very loose way. It is an all-inclusive term. That is why we need these laws and regulations.

Mr. BOLTON. Going back to your statement, Mr. Syer, "because there are particular advantages in particular cases for the use of this form," in addition to the one that you described, is not the major reason the fact that a corporation can deduct the entire lease structure payments and process them on a different depreciation basis?

Mr. SYER. I think what you are particularly thinking of is Government contracts.

Mr. BOLTON. I am thinking of any kind of equipment.

Mr. SYER. And I think that earlier there were some very substantial ones. Let us take back 5 or even—10 years ago. I would say that those are becoming less and less meaningful as we go along, because of the position of the IRS as to their position as to what appears to be legal, that is, just by using the lease method it should not be a method of reducing the tax.

Mr. BOLTON. I have made constant reference to the printing business, and I apologize for that. A press is depreciated something like 24 or 27 years by the IRS. On the other hand, you could lease the press for a term of 5 years, and with the constant changing day by day in the printing technology this certainly contemplates a new piece of costly equipment to replace it.

Mr. SYER. Technical changes are made as well as other changes. Apparently it is quite common in that industry.

Mr. BOLTON. That is because of the profit structure being so low.

Mr. HALPERN. To get to the very heart of this subject, Mr. Chairman, I refer to the ruling of the Comptroller. As I interpret the Comptroller's ruling, he says that a bank can purchase personal property for simultaneous leasing. This is important. There are no limits set forth in the ruling. As a matter of fact, the Comptroller says that banks are not permitted to stockpile. Well, no leasing company ever stockpiled the item, whether it be trucks or heavy machinery which were purchased solely for a specific lease arrangement. That is the leasing business. That is the very concept of the leasing business.

Mr. MULTER. That is true in the automobile business.

Mr. TALCOTT. And typewriter leasing.

Mr. HALPERN. I am talking about leasing for business use. I am sure that a leasing company does not have a lot of cars in reserve for quantity leasing purposes. They go out and buy them and then lease them.

Mr. MULTER. I have in mind Hertz and some of the others.

Mr. HALPERN. I am not referring to individual leases for personal use. Of course an outfit like Hertz keeps a reserve for short-term use. I'm talking about long-term leases. Take a business firm that might of necessity need 500 cars on a lease basis. The leasing company, and now some banks, purchase them because they need them. That is the whole concept of the leasing business as we view it here. So the fact is that the Comptroller's ruling is as broad as the entire leasing industry. Am I correct in that interpretation?

Mr. SYER. We have not stockpiled any equipment.

Mr. HALPERN. The leasing company doesn't stockpile either, other than in case of daily or weekly turnover, such as Hertz.

Mr. SYER. In the case of automobiles?

Mr. HALPERN. Or any leasable equipment.

Mr. SYER. The automobile dealers are also leasing companies.

Mr. MULTER. I do not think that it matters whether you stockpile or do not stockpile. If I come into the bank and say, "I want \$100,000 worth of trucks," you buy them for that and you lease them to me, this is a direct evasion of your responsibility to appraise my borrowing ability. If I go to the bank and say, "I am buying \$100,000 worth of trucks and intend to lease them to a user and I want to discount this lease or to use it as security for a loan, would you lend me \$100,000 against this \$100,000 cost"? You would not. You would insist that if I am the purchaser that I have at least a 25-percent or maybe a 20-percent equity in the vehicles, and then the bank might finance part of the difference.

Mr. SYER. I have to take exception to that, because depending on the credit rating of the lessee, would depend the question of whether 100 percent was advanced or 80 percent or 75 percent or some other percentage.

Mr. MULTER. If I am a borrower seeking \$100,000, with which to buy a fleet of trucks you would appraise my financial statement, evaluate my business and the project to determine what I am going to earn and my ability to repay. If you decide to extend the loan, you would lend to me on my credit. That would be a short-term loan, is that right?

Mr. SYER. It may be considerably extended. It might be for 5 years and it might be for 7 years.

Mr. MULTER. Provided that my credit standing is good and the projection is good and so forth.

Mr. SYER. Yes.

Mr. MULTER. When I ask you to buy \$100,000 worth of trucks which you are going to buy and lease to me, what are you going to evaluate?

Mr. SYER. Your credit.

Mr. MULTER. You will evaluate my credit again?

Mr. SYER. Certainly.

Mr. MULTER. Then why go through the business of owning the trucks?

Mr. TALCOTT. There are several other legal and practical reasons.

Mr. MULTER. I would like to know what the other reasons are.

Mr. SYER. We have been talking about them. There may be, as I said before, the question of whether it fits in with other things that the company may have which makes it by far the simplest way to go about it.

Mr. MULTER. In the Bank of America, with its tremendous size, this may never occur. But in a smaller bank this might be an easy way to avoid the limitation on the maximum loan the bank can make to one company. The bank buys \$100,000 worth of trucks, and adds it to their asset column, do they not? The trucks become part of its assets?

Mr. SYER. A part of the assets—no question about it.

Mr. MULTER. What happens to its loan limitation? Let us assume that we are dealing with a bank that has a capital of \$500,000 and is to buy \$200,000 worth of trucks for its customer. What happens to the limitation on the maximum amount that it can lend to one customer?

Mr. SYER. The Comptroller made the specific ruling indicating the proportion and said that the limits did not apply.

Mr. MULTER. In other words, this \$500,000 capital bank is able to buy \$200,000 worth of equipment for one customer?

Mr. SYER. He had a specific example very similar to what you state. He then went on to add that prudence would dictate how big an investment in one customer's business should be.

Mr. MULTER. Here is one Congressman who is not going to let any bank use prudence to evade the statutory limits on the maximum loan any bank may make.

Mr. SYER. I am merely repeating what the Comptroller said.

Mr. MULTER. That points up that we need some legislation of this kind.

Mr. HALPERN. Mr. Chairman, if you will yield for one second.

Mr. MULTER. Yes.

Mr. HALPERN. Are leasing and lending exactly the same in your concept?

Mr. SYER. No.

Mr. HALPERN. What legal authority do you have to lease property, to own and lease property, other than the Comptroller's ruling?

Mr. SYER. Nothing other than the ruling of the Comptroller. Now, wait, I said nothing. Obviously, we would not have as a bank acted

without outside counsel having given an opinion with respect to the Comptroller's opinion, which was done.

Mr. BOLTON. May I ask this question, I think that you would gather from—at least I have not talked to my colleagues about this, but I would gather—that if I were in your shoes, from the temper of the questions, that the legislation as it is proposed would probably receive an affirmative consideration from the committee without further hearings and study. Is the leasing mechanism of financing sufficiently important in the commercial world today to receive the serious type of consideration which would be required for the rewriting or the adopting of many of the laws which now pertain to other types of commercial transactions?

Mr. SYER. If they were included in the banking business?

Mr. BOLTON. Right.

Mr. SYER. Yes, I would say yes. If I may take just one minute to give you an example of why it would occur to us that the banking business can do this job and do it very well, I am speaking of a small company, small in general terms, that is in the electronic business. Many of these have expanded very rapidly, as you may know. This particular company has been banking with us ever since its inception, which was a matter of 5 years or so. At the time that we were asked to consider purchasing for them, in this case it was a buy-and-lease-back, to enter into a buy-and-lease-back arrangement, we had this situation already existing. Our SBIC owned \$500,000 worth of debentures of this company. We had a \$4 million loan against the Government contracts, and a \$1 million revolving inventory loan. And then the company needed additional working capital. And how were we going to do it on a reasonable basis?

Mr. BOLTON. It sounds to me as if you were in a little difficulty, that you were in a little deep.

Mr. SYER. With that type of credit, I think that we, as a banker, had a better chance of knowing the ramifications and everything about this company to decide this proposition than anyone else, or to say: "Just because you want to do it this way, do not talk to us any more." But it is a different kind of financial transaction and it does not fit within the purview of making funds available for their use.

Mr. BOLTON. The reason I asked the question is that I do not think that anybody on this committee wants to interfere, as a matter of fact, let us put it in the positive, we want to help in the development of sound credit transactions in this country, but I think we feel our responsibility that soundness within broad limits is required.

Mr. SYER. Yes, I must say to the committee that such a regulation, if it were put into effect by the Federal Reserve Board on a buy-and-lease agreement, would not be subject to those terms, if such were put into effect as to such a regulation, in fixing the amount of the down-payment and fixing the term of the lease, of the loan.

Certainly, the bank examiner still has the right to decide he does not like what he looks at.

Mr. MULTER. As a banker you have a right to tell the bank examiner "This is within the four corners of the statute and the regulations. I am the banker and this is my sound judgment." You can say that.

Mr. SYER. Right.

Mr. TALCOTT. I do not think that we have had enough hearings on this issue. Leasing is a fast-developing technique, both for ownership and financing, that is really exploding.

Mr. SYER. If I may offer one other comment. As you probably know, this bank was the first bank, at least the principal bank to enter this business. I have received inquiries in stacks this high [indicating] from both large and small banks. We have been talked to by representatives of one of the principal national banks, in one of the larger States, who sent a team of men out to confer with us in Los Angeles. In contemplation of going ahead with it, they have talked to us. So, really, I think that in answer to both questions, very substantial interest has been had on the part of banks all over the country in this proposition in finding out what to do.

Mr. MULTER. Let me remind you—I do not know whether you know it or not—but it was the Bank of America that told the bank examiners to mind their own business when you were making small business loans, and very few other banks were doing it, and the bank examiners were objecting to it. But that is another question, too.

Mr. TALCOTT. We all have looked to the banks to do so many things for us. They advise the Red Cross, Community Chest, local government. If you are starting a business, a new organization, civic or commercial, you go to the bank. So when the businessmen have a need for leasing, the people go to the banks for leasing help and advice as for all of these different things.

Mr. MULTER. Along the lines of what was said about needing additional hearings, if we get any requests from anybody who wants to be heard, we will try to accommodate them. In the meantime we have had requests from others, including the National Automobile Dealers Association, for permission to file statements. We will keep the record open for at least 2 weeks to receive statements from all of those who have indicated the desire to submit a statement. If there is anyone else who wants to be heard for or against either of these bills we will try to accommodate him.

Mr. TALCOTT. I would like to ask Mr. Syer some more questions; but we do not have the time now.

Mr. MULTER. Can you come back again?

Mr. TALCOTT. I do not want to impose upon him to return to Washington. He has to travel 5,000 miles.

Mr. MULTER. I assume that you gentlemen will agree to answer any questions that may be submitted to you by any member who has any questions and addresses them to you in writing, and that you will answer such questions and we will add them to the record. If additional hearings are indicated we will have them. In the meantime, the committee will stand in recess subject to the call of the Chair. We thank you gentlemen for coming here.

Mr. BOLTON. May I join in that to thank them very much.

Mr. MULTER. Yes. At this point in the record I should like to insert several letters and statements that have been or will be submitted to the subcommittee.

The committee stands in recess subject to the call of the Chair. Thank you.

(The letters and statements referred to follows:)

BANK OF AMERICA,
NATIONAL TRUST AND SAVINGS ASSOCIATION,
San Francisco, Calif., March 9, 1964.

HON. ABRAHAM MULTER,
*House of Representatives,
Washington, D.C.*

MY DEAR MR. MULTER: I appreciate this opportunity to submit the following information to amplify my testimony of February 26, 1964, before the Subcommittee on Bank Supervision and Insurance. It is believed the attached actual examples of lease transactions entered into by this bank will be interesting and informative for the committee.

1. A relatively small newspaper business which had been a customer for over 10 years approached the bank to buy and lease to the company additional equipment. The company had previously leased presses and other equipment and had been advised by its public accountant that leasing was advantageous. The company desired to lease from the bank to keep its financial transactions at one source. Its other transactions with the bank included real estate loans, unsecured loans and substantial deposit balances. As a result of this lease transaction the company was able to further expand its capacity without undue strain upon its financial position.

2. This case involves a large manufacturer which has been a customer of this and other banks for some time. The bank has been the agent for a group of eight banks making very substantial open credit available to this company. The company desired to prepay a subordinated debenture inasmuch as the conversion privileges inherent in the debenture concerned them with respect to control of the company. As the lead bank, we were thoroughly familiar with the entire operation of the company and its financing and by means of a buy and lease back transaction were able to make the funds available to accomplish the retiring of the debt to which the subordinated debenture related. With all of the special provisions inherent to a complicated credit such as this one it is unlikely that the Bank of America or any other bank would have been able to solve this particular situation without the facility of direct leasing.

3. This case involved a large distributor of automobiles servicing some 70-odd dealers in the southern California and Arizona areas. This company had been a customer of the bank of many years and prior to entering into a leasing arrangement, was indebted to the bank in the approximate amount of \$1,400,000 and substantial account balances were maintained. The company arranged to lease from the bank Burroughs tape punch adders to be installed at each dealer location functioning as a new parts inventory control system. Some of the advantages were reduction of inventory and increased inventory turnover with improved gross profit margins through reduced markdowns and improved customer service. The total investment required was \$220,000 and the company's accountants and tax counsel advised that the leasing method be used, particularly with a provision permitting the distributor to sublease the equipment to its dealers. The result of this method of financing was to conserve working capital and place the company in a position to benefit from the advantages enumerated above.

There is hope that this information will be helpful to the committee, and additional copies of this letter have been provided should you care to pass them on to the members.

Sincerely yours,

R. D. SYER, *Vice President.*

PERLMAN, LYONS & EMMERGLICK,
Washington, D.C., March 4, 1964.

HON. ABRAHAM J. MULTER,
*Chairman, Subcommittee on Bank Supervision and Insurance,
Committee on Banking and Currency,
House of Representatives, Washington, D.C.*

DEAR CONGRESSMAN MULTER: As you know, I am counsel for the American Automotive Leasing Association, and, in accordance with your suggestion, I am writing this letter with the request that it be included in the record of the hear-

ings before your subcommittee on H.R. 9822, a bill to prohibit banks from engaging in the business of personal property leasing. The American Automotive Leasing Association favors the enactment of H.R. 9822.

At the hearing before your subcommittee on Wednesday, February 26, 1964, some references were made to the fact that the ruling of the Comptroller of the Currency, contained in his letter of March 18, 1963, which authorized national banks to purchase personal property for leasing purposes, authorized such purchases only at the specific request of and for the use of a customer and did not permit national banks to stockpile quantities of personal property for leasing purposes generally. While this description of the scope of the Comptroller's ruling is entirely accurate, I believe that an erroneous implication may have been left in the record to the effect that the Comptroller's ruling was a narrow one and authorized national banks to engage only in a limited segment of the personal property leasing business.

As Congressman Halpern noted, all leasing companies purchase property only to satisfy specific lease requirements and do not stock or inventory property generally for leasing purposes, and this is true, not only with respect to equipment leasing, but also with respect to automotive leasing. It has been estimated that the members of the American Automotive Leasing Association do between two-thirds and three-fourths of the automotive leasing in the country, and, so far as I am aware, no company stocks or inventories vehicles generally for leasing purposes. It is only when a leasing arrangement with a lessee has been consummated that an automotive leasing company purchases the vehicles from automobile dealers in order to satisfy the requirements of the lease. Depending largely on where the vehicles are to be delivered to, or used by, the lessee, these purchases may take place anywhere in the country. When the vehicles are returned from lease, they are not held in stock for leasing again, but are disposed of, usually at wholesale at various used-car markets throughout the country. What is true of equipment leasing is equally true of automotive leasing; neither type of leasing involves stockpiling of inventories. The Comptroller's ruling is, therefore, merely descriptive of the leasing industry, and the ruling, far from being narrow or limited, authorizes national banks to engage in the leasing business in the same manner and to the same extent as any commercial leasing company.

Fleet leasing of motor vehicles should not be confused with daily or short-term rental of individual motor vehicles. The rent-a-car operations at airports, hotels, etc., obviously require a supply of automobiles on hand, but this is no part of the leasing business. Automotive leasing companies do not engage in the rent-a-car business, although some few large corporations, such as the Hertz Corp., engage in both businesses. But, even here, the operations are conducted in separate corporate divisions, headed by separate corporate officers.

Finally, there appeared to be an assumption at the hearing that the Comptroller has authorized only a certain type of leasing, "so-called financial leasing." I am not entirely sure what this phrase means, but I assume that it refers to nonmaintenance leasing, as contrasted with maintenance leasing. There is certainly nothing in the Comptroller's March 18 ruling expressly prohibiting a national bank from providing maintenance in connection with a lease, but in any event, at least insofar as automotive leasing is concerned, the providing of maintenance creates no great problem. In such lease arrangements, the lessor merely authorizes the lessee to have the vehicle serviced and repaired when and where that is required, and such expenses as are incurred are paid for by the lessee. But the lessor does not maintain service facilities throughout the country for this purpose; he does not go into the repair business. The service and repairs are obtained at garages at such places throughout the country where the vehicle may happen to be at any given time, and the expenses incurred are merely for the lessor's account. The problems for banks are not created by maintenance as distinguished from nonmaintenance leasing. The problems are created by the fact of ownership of the vehicles by the lessor, and they are essentially the same whether maintenance is provided or not. Many of these problems are summarized in the statement filed by Mr. Alvin Zises on behalf of the Association of Equipment Lessors, Inc., and there is no need to repeat them here. I would only add that a seemingly trifling matter such as traffic and parking tickets can become burdensome and time consuming for a leasing company where vehicles bearing license plates issued in its name are operated by lessees throughout the country.

It is my opinion that the Comptroller's ruling has purported to authorize national banks to engage in the leasing business in essentially the same manner

as commercial leasing companies and that all of the problems which confront such commercial leasing companies will confront the national banks. The ruling of the Comptroller is not a restricted one designed to insulate the banks from any of these problems.

We appreciate very much the opportunity to submit this statement for the record on behalf of the American Automotive Leasing Association.

Sincerely yours,

ELLIS LYONS,
Attorney for the American Automotive Leasing Association.

SPORTS DATA CORP.,
New York, N.Y., February 19, 1964.

HON. ABRAHAM J. MULTER,
*New House Office Building,
Washington, D.C.*

DEAR SIR: I read a recent article in the New York Times regarding "sideline services" offered by banks in the data processing field, and feel obliged to cite an additional instance of this practice.

My firm performs the task of computing golf handicaps electronically for most of the leading country clubs in the northeastern section of the country. This past fall we suffered the loss of most of our subscribers in the Philadelphia area when a local bank offered the similar service at 25 percent of our sales price. I also know of a like situation in Atlanta, Ga., where a local bank is performing handicap computing services at no charge at all.

I am most interested in your proposed legislation and will cooperate by detailing this brief note.

Please call on me for any additional information.

Very truly yours,

FRANKLIN KNOBEL, *President.*

JEROME F. COMEAU PROFESSIONAL BUSINESS SERVICES,
Portland, Oreg., March 19, 1964.

Representative ABRAHAM J. MULTER,
*House Banking and Currency Committee,
U.S. House of Representatives, Washington, D.C.*

DEAR MR. MULTER: My attention was recently directed to a brief article in a trade magazine which indicated that you have introduced a bill in the House Banking and Currency Committee which would restrict national bank organizations from entering the field of electronic data processing services for commercial and professional businesses. If it is possible to secure a reprint of the text of your bill, I would sincerely appreciate receiving it.

In basic principle, I am opposed to large financial organizations entering into direct competition with small service firms who are currently able to adequately satisfy the demand in the areas of billing of accounts receivable and allied services. In the west coast area, we hear of banks investigating the purchase of electronic data-processing equipment with capacity that appears far in excess of that required to handle existing requirements, and reasonable expansion requirements. This would indicate that the added cost of this equipment can only be recovered through sale of its services to outside organizations not directly associated with the banking industry.

I am very pleased to learn of your bill, and have today written to Senator Wayne Morse and Representative Edith Greene asking that they give consideration to its support.

Sincerely yours,

JEROME F. COMEAU.
FINANCIAL SERVICES, INC.,
Glen Rock, N.J., March 25, 1964.

Re H.R. 9548.

HON. ABRAHAM J. MULTER,
*House of Representatives,
Washington, D.C.*

DEAR MR. MULTER: In reading the American Banker the other day, I learned of a bill being presented by you in regard to accounting services being rendered by banking institutions, which I believe holds a great deal of merit.

I am president of Financial Services, Inc., an electronic data processing bureau specializing in providing over 100 banking institutions with a combined asset of \$8 billion with accounting services. I have been providing this type of service for the past 10 years and as far as I know, there is not another bureau in the country who limits their activity to banking institutions only. Many times, over the years, we have been competing with service bureaus who regard this type of service as only one of many services provided by them, and the competition has been relatively small.

In the past 4 or 5 years, many banks have been installing large computers, and after installation have found themselves overautomated. In order to offset this, the banks have tried to utilize their spare time on their computers by offering accounting services to their customers and allow credit for compensating balances or to encourage new compensating balances in the case of a new customer which would reduce the price of their services accordingly. We in private business cannot hope to compete pricewise with this type of service, inasmuch as the bank is using idle time and allowing built-in reductions for compensating balances maintained in their bank.

I feel that in the years to come, if the banks are permitted to continue this type of service, there is no doubt that they will be in the service bureau business. We do not feel that this is fair competition, inasmuch as the banking industry under the disguise of the word "service" are going a great deal beyond the normal reaches of banking services when they charge a reduced billing based on compensating balances which must be maintained because of our present banking setup which forces all other banking institutions, other than commercial banks, to draw all of their checks on a commercial bank.

If I can be of any assistance to help further the process of your bill, please do not hesitate to call upon me.

Very truly yours,

HAROLD V. SCHUNKE, *President.*

MONTEBELLO, CALIF., *March 5, 1964.*

Re H.R. 9548, prohibits banks from performing certain nonbanking services.

Hon. ABE MULTER,
Congressman, District of New York,
House Office Building,
Washington, D.C.

DEAR MR. MULTER: We would like to inquire as to the present status of your bill and its prospects for passage in the near future. We are vitally interested in the outcome of this proposed legislation.

The Medac system, providing automated billing and accounting services to the medical profession, has been designed, developed, and patented over the last 3 years and is now installed in numerous doctors' offices in the Los Angeles area. We believe that entry into type of accounting service by the banking industry is totally unrelated to its primary banking functions.

We are currently faced with the imminent invasion in this field by the Bank of America. Banking being highly competitive, we have reason to believe that the United California Bank, Wells Fargo, Crocker-Citizens National Bank and the Security First National Bank are making diligent plans to enter into the same type service and will be announcing their intentions shortly in order to meet the competition we have in this State. It becomes very obvious that a price war among these giants competing with each other can place the future of our business in dire jeopardy.

Any information that you can forward to us or any suggestions as to action that might be taken on our part to further enhance the hearing of this bill before the House would be most appreciated.

Sincerely yours,

FRED L. JONES.

[Article from the Wall Street Journal, Jan. 6, 1964]

BANK OF AMERICA OPENS PATIENT BILLING SERVICE FOR DOCTORS, DENTISTS

AUTOMATED ACCOUNTING SYSTEM OFFERED TO 30,000 PHYSICIANS, 11,000 DENTISTS
IN CALIFORNIA

(By a Wall Street Journal staff reporter)

SAN FRANCISCO.—Bank of America offered to take over the billing of patients for California physicians and dentists.

The service will use the statewide bank's network of computers and automated bookkeeping equipment. The bank already handles such jobs as making up payrolls, aside from the regular banking functions adapted to machine processing.

The bank has been experimenting with the billing service for a year, according to Frank M. Dana, executive vice president. It found that it could reduce bookkeeping time for the 20 doctors enrolled in the experiment to about 4 hours a month, from as much as 22 hours previously.

The service will be offered to an estimated 30,000 licensed physicians and 11,000 dentists in California, at a price to be announced later.

The service will prepare and mail monthly statements to patients; prepare reports, including daily transactions and balances and a monthly analysis of a client's patient accounts; report the number of patients seen; list all new patients and closed accounts; report delinquent accounts in 30-, 60-, and 90-day categories; and provide averages of fees received, patients seen per day, and hourly compensation.

The doctors will send information over data transmission telephone lines linking their offices to the bank's computers. On calling the computer center, a nurse or receptionist receives a dial tone to begin transmission. She inserts the patient's card into the terminal at the phone and punches the particular service code number and the amount to be charged on a keyboard. The computer records the information on magnetic tape and each month the bank mails a statement to the patient. Bank of America will install and maintain the data telephone, with the phone's cost to be included in the service price.

[From the Wall Street Journal, Jan. 6, 1964]

To All California Physicians and Dentists:

Now Bank of America announces a professional billing service designed especially for you. Under this new program, 25 seconds per patient is all your staff needs to handle all your bookkeeping. The bank does everything else electronically: Bills, analyzes, and controls your accounts. Patient billing and payments identified with your name only. You receive a confirming report daily, an itemized summary monthly. Save time, trouble, money, contact any branch, today.

BANK OF AMERICA.

INDIANAPOLIS, IND., February 14, 1964.

Hon. RICHARD L. ROUDEBUSH,
House of Representatives, Washington, D.C.

DEAR SIR: For several months some of the larger banks in Indiana, particularly in the Indianapolis area, have been advertising the fact that they now have the equipment to do machine recordkeeping for public business firms. I further note that an increasing number of banks throughout the country are also trying to get into the act.

In fact, an Indianapolis bank, when conferring with one of my clients concerning a line of credit and the transfer of their checking account from another bank, tried to sell their data processing service, starting with payroll work.

To me, this is a serious encroachment into the field of professional account-

ants who are trained and equipped to perform accounting service. So-called accounting services by banks lack the professional competence and judgment available from independent practicing accountants. How can mechanized services qualify a financial statement with the same degree of skill that an independent auditor might show? For years, credit departments have been insisting on financial statements from outside sources, now they propose to provide such data to themselves by mechanical means. Is it not also entirely possible that one function by a bank may not influence some other function.

I believe the banks have a duty to perform and that they should stay in the banking business. I am pleased that one of our able representatives feel that some action should be taken to clarify the functions of our banks. I commend to you H.R. 9548 by the Honorable Abraham J. Multer, of New York, for study. Many thousand independent accountants will be affected by lack of action in this bill. I hope you will support the measure.

Sincerely,

GLEN V. HUESTON.

HARRY EWING & ASSOCIATES,
SALEM, OREG., March 10, 1964.

HON. WALTER NORBLAD,
House of Representatives, Washington, D.C.

DEAR REPRESENTATIVE NORBLAD: This letter is written to express my feelings regarding the Multer bill concerning the stopping of banks from providing accounting services.

The increasing number of banks throughout the country seem to be invading the public accounting field, and, as an accountant, I feel that accounting services by banks would lack the professional competence and judgment available from independent practicing accountants.

This is a serious encroachment into the field of professional accounting, for accountants are trained and equipped to perform accounting services. Therefore, I would appreciate your giving consideration to this letter concerning this important bill being brought before the House of Representatives.

Respectfully yours,

HARRY EWING, *Public Accountant.*

THE DATA CENTER CORP.,
Los Angeles, Calif., April 10, 1964.

CONGRESSMAN MULTER,
House of Representatives, Washington, D.C.

DEAR CONGRESSMAN MULTER: We have read, with great interest, the contents of your bills, H.R. 9822 and H.R. 9548.

As members of the data-processing industry, we are behind the spirit of these bills entirely and wish to be on record as supporting your activities in obtaining passage of these bills.

Very truly yours,

HERBERT J. GROELINGER, *President.*

PASADENA, CALIF., April 16, 1964.

HON. ABRAHAM J. MULTER,
House of Representatives, Washington, D.C.

DEAR CONGRESSMAN MULTER: We have taken the liberty of enclosing a photostatic copy of an ad which appeared in the Wall Street Journal on April 6, 1964, which we believe to be self-explanatory.

After reading the ad we are sure you can see that it is rather a misleading advertisement in that it infers that they are not only doing accounts receivable but also general ledger and giving out profit and loss statements. We also noticed that they refer to the Bank of America Business Service Center. If this is a separate corporation it would appear that they are in violation of H.R. 8874. You will also note there is an inference at the bottom of the page that they are members of the Federal Deposit Insurance Corporation. This would suggest that the client using this service would also incur insurance coverage.

We might point out that there are licensed public accounting firms in this area who can do this work; however, their fee would be slightly higher than the banks as they are not allowed to act as a banking organization and as



Data transmitter attached to telephone sends billing information to Bank of America Business Services Center.

An important announcement for California physicians and dentists:

A new electronic billing service from Bank of America

Under this new program, 25 seconds per patient is all the time required for your staff to record fees and charges. Bank of America does the rest electronically. It even receives your payments if you wish, and credits them to your account.

How does it work?

When this service is installed you receive a desk-top data transmitter which connects to your telephone wire. It's simple to operate. Your nurse or receptionist will be instructed how to insert the pre-punched cards and work the keys. At the end of each day she can send all the necessary bookkeeping information to Bank of America's Business Services Center in a matter of minutes.

If your daily volume does not warrant installation of a transmitter in your office, you can deliver the accounting material to your local Bank of America branch, or mail it to a Bank of America Business Services Center. The processing will be the same—quick, economical and completely confidential.

Complete records

You receive a detailed statement of each day's transactions, showing current balance on all accounts due; services and charges per patient for the day; remittances collected and credited to your account; and information on new accounts, accounts closed and accounts receivable. At the end of each

month you receive a complete statement of the month's transactions, showing payments in 30, 60 and 90-day categories.

Special reports

Full analyses of your individual or group practice are automatically provided. These reports show total number of patients, kinds of treatment and other valuable statistics.

Billing service

Each month Bank of America sends a detailed statement to each of your patients in your name (the name of the bank does not appear on these statements). As an optional feature, the bank will receive payments for you, addressed to a Post Office box in your name. These payments will be credited to the patient's account and deposited in your account at the bank.

Save time and money

Bank of America's new professional billing service allows you to devote all of your time to your patients, frees your office personnel to assist you and assures income control. If you would like to know more about this time-and-money-saving new accounting system, contact any branch of Bank of America.



A new electronic billing service from Bank of America

An important development in electronic banking and payments

Under the new program, the service is available to all the major banks in the United States. The program is a result of a joint effort by the major banks to provide a more efficient and economical way of handling their business.

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a result acquire the client's deposits to be used in the lending of funds in order to facilitate additional earnings.

It would appear from the ad that the banks do not feel that H.R. 9548 is going to affect them very much as they seem to be continually "tooling up" for entering the accounting profession.

We hope this material may have some effect on the committee's deliberation and a favorable passage of your bill H.R. 9548. Could this be a fair trade commission violation?

Very truly yours,

ROBERT A. GRAY.

BANKERS LEASING CORP.,
Boston, Mass., April 27, 1964.

HON. ABRAHAM J. MULTER,
Chairman, Subcommittee on Bank Supervision and Insurance, Committee on Banking and Currency, House of Representatives, Washington, D.C.

DEAR REPRESENTATIVE MULTER: The letter to you from the Comptroller of the Currency dated April 8, 1964, regarding H.R. 9822 is incorrect in its basic assumption.

The basis of the Comptroller's contention is found in his third paragraph on page 1 in which he claims that "Congress in 1864 wisely did not attempt to define the business of banking as it then existed."

This statement and the assumptions which flow from it are in contravention of fact, economics, and law.

Fact.—Under the National Bank Act, 12 U.S.C. 24, Paragraph 7, Congress meticulously defined banking "powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; by buying and selling exchange, coin, and bullion; by loaning money on personal security; and by obtaining, issuing and circulating notes according to the provisions of this chapter * * *."

When banks sought to engage in the safe deposit business, this power was written into the National Bank Act. Thus the business of banking was carefully and specifically defined.

Economics.—In "History of Commercial Banks" by Fayette B. Shaw, associate professor of economics, College of Commerce, DePaul University, the intent of Congress is stated in enacting the National Bank Act:

"Congress also laid down limitations on lending policies * * * the purpose of these restrictions was to keep the bank in the commercial banking business—that is, making loans and discounts, receiving deposits, and handling other related transactions—and to prevent it from becoming a nonbanking business of any sort."

The obvious purpose of these well-defined limitations and restrictions was to avoid risking the public's funds. The laws of banking were carefully and meticulously defined to prevent banks from operating outside their privileged sphere, to prevent those entrusted with the public's funds from risking them in business ventures.

Law.—There is a basic rule of law which bears upon the issue, "inclusio unius est exclusio alterius." This doctrine means that where a statute such as the National Bank Act, 12 U.S.C. 24, paragraph 7, enumerates specific powers within the law, the law is to be construed as excluding from its effect all those matters not expressly enumerated. This principle has frequently been applied by the Supreme Court in connection with the National Bank Act and especially with reference to the powers which may be exercised by national banks. In *California Bank v. Kennedy*, 167 U.S. 362 (1897), the Supreme Court said at pages 366-367:

"* * * It is settled that the United States statutes relative to national banks constitute the measure of the authority of such corporations, and they cannot rightfully exercise any powers except those expressly granted * * *."

In *DeLaverne Company v. German Savings Inst.*, 175 U.S. 40 (1889), the Supreme Court observed at pages 54-55:

"But as the powers of corporations, created by legislative act, are limited to such as the Act expressly confers, and the enumeration of these implies the exclusion of all others. * * *"

One of the most recent pronouncements of the U.S. Supreme Court on the subject occurred in *Texas and Pacific Railway v. Potoroff*, 291 U.S. 245 (1943), where Mr. Justice Brandeis addressed himself to the same question. Said Mr. Justice Brandeis of national banks:

"The measure of their powers is the statutory grant; and powers not conferred by Congress are denied * * * moreover, even a practice commonly pursued may not be a necessary one."

In *Cooper v. Hill*, 94 Fed. 582 (C.A. 8, 1899), the Supreme Court said at page 584:

"The statutes of the United States have a measure of the powers of national banks, and these corporations can lawfully exercise none but those they are expressly granted. * * *"

We therefore submit that the contention of the Comptroller in his letter of April 8, 1964, is incorrect factually, economically, and legally.

Sincerely,

ALVIN ZISES, *President.*

(Whereupon, at 12:15 p.m., the subcommittee was in recess, to reconvene subject to the call of the Chair.)





