# NOTES

## BANKS AND BANKING: CONFLICT IN FEDERAL COURTS AS TO THE EXTENT STATE LAW STANDARDS CONTROL IN ESTABLISHING NATIONAL BANK BRANCHES

SECTION 36 (c) (1) of the National Bank Act permits a national bank to establish branches *within the city of the parent bank* "if such establishment and operation are at the time expressly authorized to State banks by the law of the State."[1] The quoted clause is also contained in section 36 (c) (2) which authorizes the establishment of national branches *at any point in the state,* expressly subject, however, to those restrictions on *location* which are imposed on state banks by state law.[2] In separate cases involving the establishment of national branch banks within the city of the parent bank, two federal district courts have expressed conflicting views as to the effect of state law limitations upon national branch banking.

Both decisions involved the law of Utah, which forbids branches for its state banks in cities with at least one bank unless the branch would take over an existing bank.[3] In each case, the Comptroller of the Currency had authorized a national bank to establish a branch in the city of its principal office, even though it would not be taking over an existing bank. In *Walker Bank & Trust Co. v. Saxon,*[4] a

[1] McFadden Act § 7 (c), 44 Stat. 1228 (1927), as amended, 12 U.S.C. § 36 (c) (1) (1958).

[2] 48 Stat. 189 (1933), as amended, 12 U.S.C. § 36 (c) (2) (1958).

The authority of Congress to establish and regulate national banks derives from powers delegated by U.S. CONST. art. I, § 8. See McCulloch v. Maryland, 17 U.S. (4 Wheat.) 315, 406 (1819). State law cannot regulate national banks except to the extent that Congress permits. Mercantile Nat'l Bank v. Langdeau, 371 U.S. 555, 558-59 (1963); Van Reed v. People's Nat'l Bank, 198 U.S. 554, 557 (1905); Davis v. Elmira Savings Bank, 161 U.S. 275, 283 (1896).

[3] UTAH CODE ANN. § 7-3-6 (Supp. 1963). This limitation is not applicable to cities of the first class, which are those having at least 90,000 inhabitants. *Ibid.*; UTAH CODE ANN. § 10-1-1 (1953).

For Utah's definition of "existing bank," see note 4 *infra.*

[4] 234 F. Supp. 74 (N.D. Utah 1964). Although there were branches of nonlocal banks, the national bank was the only unit bank in the city of Logan. The branches did not qualify under Utah law as banks already existing in that city, but the national bank itself qualified; hence state law required the proposed branch to take over an existing bank. Walker Bank & Trust Co. v. Taylor, 15 Utah 2d 234, 236-37, 390 P.2d 592, 594-95 (1964).

The parent of one of the branches in Logan brought a declaratory judgment proceeding to determine whether the Comptroller of the Currency had violated his

federal district court in Utah held that once a state has expressly authorized branch banking, the precise limitations imposed on state banks are inapplicable to national banks seeking to establish branches within the city of the principal office. Three months later, a federal district court in the District of Columbia held in *Commercial Security Bank v. Saxon*[5] that since a state bank could not establish a branch without taking over an existing bank, the National Bank Act incorporated the same state law limitation for national banks.

*Walker* reasoned that the first two subdivisions of section 36 (c) were designed to fulfill separate purposes and should be accorded independent legal significance.[6] Therefore, once the state legislature has expressly authorized branch banking, a national bank may establish a branch within its city without regard to specific state requirements.[7] *Commercial Security,* on the other hand, insists that the common purpose of both subdivisions was to establish competitive equality between national and state banks, requiring that the provisions be read *in pari materia.*[8] The most effective means of achieving equality within the dual banking system would be to make state law the standard in every situation.[9]

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authority under the National Bank Act. Plaintiff-bank's standing to challenge the Comptroller's decision had been firmly established in earlier decisions. National Bank v. Wayne Oakland Bank, 252 F.2d 537 (6th Cir.), *cert. denied,* 358 U.S. 830 (1958). At one time it was thought that the complainant bank had to institute suit before the Comptroller had issued the certificate of authorization. Commercial State Bank v. Gidney, 174 F. Supp. 770 (D.D.C. 1959), *aff'd,* 278 F.2d 871 (D.C. Cir. 1960). See Bell, *Branches of National Banks—Recent Cases on Review of Decisions of Comptroller of the Currency,* 16 BUS. LAW. 386, 387 (1961). However, it was subsequently held that an action could be maintained even after the branch was conducting business. Union Savings Bank v. Saxon, 335 F.2d 718 (D.C. Cir. 1964), *affirming* 209 F. Supp. 319 (D.D.C. 1962).

[5] 236 F. Supp. 457 (D.D.C. 1964). The proposed branch was to be in the city of Ogden where four principal bank offices and two branches already existed.

[6] 234 F. Supp. at 78 & n.9. Specific language makes state restrictions on location a requirement for branches outside the city of the main office. See text accompanying note 2 *supra.* Such language is not used with reference to branches within the bank's principal city. See text accompanying note 1 *supra.*

[7] Although *Walker* is apparently a case of first impression, other cases have interpreted § 36 (c) as not binding national banks absolutely to requirements and definitions of state law. See Union Savings Bank v. Saxon, 335 F.2d 718 (D.C. Cir. 1964), *affirming* 209 F. Supp. 319 (D.D.C. 1962) (state definition of "village" not controlling); Rushton v. Michigan Nat'l Bank, 298 Mich. 417, 299 N.W. 129 (1941) (approval of state commissioner unnecessary). Compare Camden Trust Co. v. Gidney, 301 F.2d 521 (D.C. Cir.), *cert. denied,* 369 U.S. 886 (1962), which failed to refer to state law in defining a "branch bank" as opposed to a new bank.

[8] 236 F. Supp. at 461. See Commercial State Bank v. Gidney, 174 F. Supp. 770, 774 (D.D.C. 1959) (dictum), *aff'd,* 278 F.2d 871 (D.C. Cir. 1960).

[9] See South Dakota v. National Bank, 219 F. Supp. 842, 846 (D.S.D. 1963); *cf.* 38 TUL. L. REV. 162, 165 (1963).

The National Bank Act originally contained no mention of bank branches,[10] and the Supreme Court interpreted this silence to mean that national banks were precluded from having branch offices.[11] Consequently, in a state which allowed branches for its banks it was considered more advantageous to stay out of the national system.[12] The McFadden Act of 1927,[13] which constitutes the substance of the present section 36 (c) (1), was intended to make national banking more attractive.[14] The committee reports accompanying this bill, however, did not indicate whether the limited extension contemplated therein was to require merely a general state branching authorization, or if express state law limitations would be also incorporated into section 36 (c) (1).[15]

As this act restricted national branches to the cities of the bank's main office, some felt that Congress had not done enough.[16] In 1932, the Senate Committee on Banking and Currency offered an amendment which would have allowed state-wide branching unfettered by state law.[17] Opposition to this proposal[18] resulted in the submission of two amendments authorizing state-wide branches only in states where such branching was permitted for state banks[19] and according to the exact location restrictions imposed by the state statute.[20]

[10] REV. STAT. § 5190 (2d ed. 1878). See WESTERFIELD, HISTORICAL SURVEY OF BRANCH BANKING IN THE UNITED STATES 10 (1939).

[11] First Nat'l Bank v. Missouri, 263 U.S. 640, 657 (1924).

[12] Congress was aware of the competitive inequality that worked against national banks and recognized its duty to remedy the situation. See H.R. REP. No. 83, 69th Cong., 1st Sess. 7 (1963).

[13] McFadden Act § 7 (c), 44 Stat. 1228 (1927), as amended, 12 U.S.C. § 36 (c) (1) (1958).

[14] See Comment, 32 U. CHI. L. REV. 148, 159 (1964); Comment, 8 VILL. L. REV. 209, 214 (1963) (Congress was anxious to halt the growing conversion of national banks to state banks); Note, 66 YALE L.J. 1093-94 (1957).

[15] The committee reports are susceptible to conflicting inferences. *Compare* H.R. REP. No. 83, *supra* note 12, at 4, *with* S. REP. No. 473, 69th Cong., 1st Sess. 10 (1926). *Walker* construed both reports to be consistent with its decision, 234 F. Supp. at 78 n.11, but certain language in the Senate Report implied that national branching within a city would be prohibited whenever state banks could not have branches within that city.

[16] See Comment, 8 VILL. L. REV. 209, 215 (1963).

[17] S. REP. No. 584, 72d Cong., 1st Sess. 16 (1932).

[18] The only articulated reason for the opposition was a concern for infringing upon the states' sovereign prerogative. See notes 28-29 *infra* and accompanying text.

[19] 76 CONG. REC. 2079 (1933) (amendment offered by Senator Bratton).

[20] *Ibid.* (amendment offered by Senator Blaine). Senator Bratton stated that this proposal did not conflict with his amendment. *Ibid.* The Blaine amendment was the only proposal which would have clarified the uncertainty as to how extensively state law was to control, but it made no reference to the provisions in § 36 (c) (1).

Senator Vandenberg later presented an amendment that would have permitted branch banks in any city not already having a bank, or if the branch would take over

These amendments became the essence of present section 36 (c) (2),[21] while the substance of section 36 (c) (1) was re-enacted without discussion.[22]

If the purpose of the 1933 Act was to create competitive equality between state and national banks, then the rationale of *Commercial Security* was correct. Nevertheless, considering that this act created two subdivisions within section 36 (c), and that exact state standards were explicitly required by the second, the logical inference is that Congress did intend different degrees of adherence to state law under each provision. If the intent were otherwise, section 36 (c) (1) would serve no purpose. The reference in section 36 (c) (2) to a location at any point within the state would obviously include a point within the city of the principal office covered by section 36 (c) (1).

*Walker* speculates that the reason for stricter adherence to state law under the second clause is that this provision broke from the long established policy of limiting national branches to the cities of the principal office. Thus, it could be expected that branches at other locations within the state would have to fulfill additional conditions.[23] Nevertheless, the authorization for national branches in the principal office cities was authorized by section 36 (c) (1) only six years earlier,[24] and can hardly be categorized as a long standing policy.[25] A better rationale would be that clause (2) represents a broader departure from the history of non-branching than clause (1), and for this reason required greater limitations.

Another equally plausible explanation for this distinction is that Congress was motivated by the need for extended banking facilities instead of intending to establish competitive equality between state and national banks, but realized that oversaturation of a particular community with new unit banks might eventually have a destruc-

an existing banking facility. 75 CONG. REC. 9908 (1932); 76 CONG. REC. 2206 (1933). This was withdrawn when the Bratton amendment passed. *Id.* at 2208.

[21] See note 2 *supra* and accompanying text.

[22] Senator Wheeler thought that branching should be allowed only in those states having legislation expressly dealing with the subject. He speculated that where a state statute was silent on the matter this would be construed as permission for branches. 76 CONG. REC. 1997 (1933). To rule out this possibility, the 1933 re-enactment of clause (1) substituted "expressly authorized" for "permitted" in the McFadden Act. This alteration indicates that the re-enactment of the first clause with the passage of § 36 (c) (2) was not merely an oversight.

[23] 234 F. Supp. at 78-79 n.11.

[24] See text accompanying notes 10-15 *supra.*

[25] In any event, one would not expect Congress to have felt bound by past policy during the crucial depression period.

tive effect on banking competition.[26] The best means of alleviating the banking service deficiency, therefore, was to allow existing banks within a city to expand through branch offices. As the problem for other towns in the state could be handled in the same manner—by authorizing branches for the banks of that particular town, there would be less need for branches of banks from another town. This would explain a more restrictive congressional attitude toward intra-state branching than intra-city branching.

Although this assumes that the purpose of Congress was to meet the banking needs of communities, the statute prevents complete satisfaction of that end by requiring some sort of state authorization. Since some states forbid branching of any kind[27] there may be areas within those states in need of extended branching services that, by the terms of the federal and state laws, will be denied branch banks. The incorporation of state law into section 36 (c), therefore, would have to be explained in terms of another federal policy. In the debates prior to the Act of 1933, some concern was expressed that establishing national branches in all states might infringe upon the sovereign prerogative of those states which, as manifested in the state statute, did not desire branch banking.[28] Thus, an intent to alleviate particular banking service deficiencies was reconciled with a deference for the states' public policy by incorporating the reference to state authorization in section 36 (c).[29] Nevertheless, the congressional debates and reports, by centering upon the attributes and disadvantages of branch banking, never discussed the question whether this means a state's general attitude toward branching or

[26] See Comment, 32 U. CHI. L. REV. 148, 159 (1964).

[27] 2 COLO. REV. STAT. ANN. § 14-1-63 (1953); FLA. STAT. ANN. § 659.06 (Supp. 1964); ILL. ANN. STAT. ch. 16 1/2, § 106 (Smith-Hurd 1963); MINN. STAT. ANN. § 48.34 (1946); VERNON'S ANN. CIV. STAT. (Tex.) art. 342-903 (Supp. 1964); W. VA. CODE ANN. § 3131 (1961). In one state the statute is silent as to state branching, WYO. STAT. ANN. ch. 13, §§ 13-1 to 13-211 (Supp. 1963), hence branching is not expressly authorized as required by § 36 (c). See note 22 *supra*.

Other states which do not authorize hranching permit detached drive-in windows within prescribed distances from the main office. ARK. STAT. ANN. § 67-340 (Supp. 1963); KAN. GEN. STAT. ANN. § 9-1111 (Supp. 1961); MO. ANN. STAT. § 362.107 (Supp. 1964); MONT. REV. CODES ANN. § 5-1028 (Supp. 1963); NEB. REV. STAT. § 8-1, 105 (1962); OKLA. STAT. ANN. tit. 6, § 461 (Supp. 1964).

[28] See 76 CONG. REC. 1997 (1933) (remarks of Senator Wheeler).

[29] Consistent with federal respect for state policy, any change in the banking laws should be sought from the state legislatures, rather than at the federal level. *But see* Comment, 38 NOTRE DAME LAW. 315, 324-25 (1963). The Utah legislature has expressly declared continued branch bank operations to be in accordance with the public policy of that state. UTAH CODE ANN. § 7-3-6.1 (Supp. 1963).

its specific policy toward conditions under which a branch may exist.[30]

These cases may be viewed against a broader controversy in financial circles. Those who urge a permissive policy with regard to the establishment of national bank branches argue that restrictive banking regulations discourage initiative and competition, thereby reducing the economic contributions of banks to the growth of cities.[31] Comptroller of the Currency Saxon contends that the prohibitive power of the states protects monopolies and threatens the basic structure of the dual banking system.[32] On the other hand, small, independent state banks fear an inability to survive the competitive advantage given to larger banks by easing of restrictions on branching.[33] While competition may be a stimulus to more progressive and efficient banking practices, it will not fulfill this function if it effects a decrease in the number of competing unit banks,[34] thus enabling the larger banks to dominate the field.[35]

[30] See Comment, 32 U. CHI. L. REV. 148, 159 (1964).

Whether the National Bank Act requires adherence to the narrower policies of states would have been at issue in Broad Street Trust Co. v. Gidney & Philadelphia Nat'l Bank, Civil No. 2265-59, D.D.C., Aug. 15, 1959, discussed in Bell, *supra* note 4, at 387 n.4, 388-89, where the complainant bank contended that the Comptroller of the Currency was to follow the same criteria as the state supervisor would in authorizing branches. However, this case was withdrawn before decision. See also Rushton v. Michigan Nat'l Bank, 298 Mich. 417, 437, 299 N.W. 129, 136 (1941), where the national bank did not have to apply to the state commissioner as required by the state law. See note 7 *supra*.

[31] Sheehan, *What's Rocking Those Rocks, the Banks?*, Fortune, Oct. 1963, p. 108, 110-11. Banks with branches are said to be more responsive to population expansion, in that they draw on the capital resources of a larger area than do single unit banks. Comment, 38 NOTRE DAME LAW. 315, 323 (1963). See WESTERFIELD, *op. cit. supra* note 10, at 38-39. Harfield, *Legal Restraints on Expanding Banking Facilities, Competition and The Public Interest*, 14 BUS. LAW. 1016 (1959) (branches create many possible sources for deposit); Legislation, 48 HARV. L. REV. 659, 672 (1935).

[32] Chicago Daily Tribune, Sept. 25, 1962, § F (Sports-Business), p. 5, col. 1. Mr. Saxon was apparently fearful of unilateral control by the states over all banking operations. His critics, however, contend that his policies favor exclusive banking control in the hands of the federal government. Walker, *The Dual Banking System—Its Strengths and Weaknesses*, Banking, Nov. 1962, p. 55, 137 (defense of multi-control of dual banking structure as system of checks and balances).

[33] See N.Y. Times, Sept. 25, 1962, p. 49, col. 1; 75 CONG. REC. 9981-82 (1932) (remarks of Senator Norbeck). *Contra*, Harfield, *supra* note 31, at 1027 (competition lies in quality of services to which size of bank is not a decisive factor).

The American Bankers Association has adopted a conservative attitude toward branch banking and opposes change of the existing banking law. See Wall Street Journal, Sept. 27, 1962, p. 10, col. 3.

[34] Comment, 71 YALE L.J. 502 (1962) (competition only exists if bank users may choose among a number of banking institutions).

[35] *Contra*, ALHADEFF, MONOPOLY AND COMPETITION IN BANKING 24 (1954) (while eliminating competitors, branching would not increase amount of monopoly).

It is suggested that dominance by larger banks is a desirable result if it means that

In light of the several alternatives and congressional vagueness, the conflict faced in *Walker* and *Commercial Security* cannot be resolved by resort to congressional intent. There is a strong probability that future adjudication[36] will entail an undisclosed weighing of the need for extended national bank services against the fear of national bank dominance. The situation is clearly ripe for legislative action[37] which should, *inter alia,* clarify the primary purpose of national branching. As the justification for the existence of national banks is not simply that they provide a form of competition for state banks, it is submitted that the concern of Congress should be with the means by which national banks fulfill particular banking needs.

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a strong bank will stand in the place of small, weak banks. Gruis, *Antitrust Laws And Their Application To Banking,* 24 GEO. WASH. L. REV. 89, 105 (1955).

[36] The appeal of *Walker* has been docketed in the Tenth Circuit, No. 7981. Letter from Mr. Robert B. Cartwright, Chief Deputy Clerk for the Tenth Circuit Court of Appeals.

[37] It has been suggested that there is little chance that Congress itself will liberalize the bank branching law, for such legislation would first have to pass through the House Committee on Banking and Currency, presently headed by Wright Patman, a strong opponent of large commercial bank expansion. N.Y. Times, Sept. 25, 1962, p. 59, col. 2. See Sheehan, *supra* note 31, at 246.