STOCK EXCHANGE PRACTICES

WEDNESDAY, JANUARY 3, 1934

United States Senate,
Subcommittee of the Committee on
Banking and Currency,
Washington, D.C.

The subcommittee met at 10 a.m., pursuant to adjournment on Friday, December 22, 1933, in Room No. 301 of the Senate Office Building, Senator Duncan U. Fletcher, presiding.

Present: Senators Fletcher (chairman), Barkley, Townsend, Couzens, and Goldsborough (substitute for Norbeck).

Present also: Ferdinand Pecora, counsel to the committee, Julius Silver and David Saperstein, associate counsel to the committee; and Frank J. Meehan, chief statistician to the committee.

The Chairman. The subcommittee will come to order, please. Mr. Pecora, have you your witnesses present?

Mr. Pecora. Yes, sir. I think we will recall Mr. Patterson, who has already been sworn.

TESTIMONY OF BERT K. PATTERSON—Resumed

Mr. Pecora. Mr. Patterson, when you became Vice President of the Guardian Detroit Union Group, Inc., what, particularly, were the duties that were assigned to you, or which you undertook to perform?

Mr. Patterson. The first duties were to make examinations of banks which Mr. Lord had tentatively made arrangements with to exchange shares for.

Mr. Pecora. That is, the various banks that that Group contemplated acquiring——

Mr. Patterson. That is right.

Mr. Pecora. Through purchase or acquisition of their stock?

Mr. Patterson. Yes, sir.

Mr. Pecora. Well, did that remain as your principal duty during the entire period of your service as executive vice president of the Group?

Mr. Patterson. Yes, sir.

Mr. Pecora. That is, it was your special function——

Mr. Patterson. It was.

Mr. Pecora. To look after the condition of the various bank units of the Group.

Mr. Patterson. With the exception of a part of 1932, Mr. Pecora, when the work was divided. When Mr. Wilkin was brought from Flint to Detroit and made an officer of the Group Co., whereupon certain banks were allocated to him, that is, certain banks were allocated to my supervision and certain banks to Mr. Wilkin for his supervision.

Mr. PECORA. Did you, for the purpose of observing the condition of the various banking units of the Group, from time to time make examinations of those unit banks or cause them to be made?

Mr. PATTERSON. Yes, caused them to be made mostly. At the beginning I personally made an examination of the Union National Bank & Trust Co. of Jackson for the purpose of acquisition, and later I personally made an examination of the Federal Commercial & Savings Bank of Port Huron, and also of the First National Bank of Port Huron. When the arrangements with the Union Commerce Corporation was far enough along I also made a personal examination of the Union Trust Co. of Detroit. After that I do not believe I personally made any examinations. That was all done with the help of Mr. Bryan and Mr. Penningroth.

Mr. PECORA. And Mr. Hopkins?

Mr. PATTERSON. No. Mr. Hopkins did not make any examinations of banks forming the Group.

Mr. PECORA. Now, the three gentlemen last named had been bank examiners in the office of the Comptroller of the Currency for quite a number of years before they became connected with the Group, hadn't they?

Mr. PATTERSON. That is right.

Mr. PECORA. And you also had had many years of service as a national bank examiner immediately prior to your becoming connected with the Group.

Mr. PATTERSON. Yes, sir.

Mr. PECORA. Well, when those examinations of unit banks were made by others than yourself while you were vice president of the Group, were the results of their examinations submitted to you for your action?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. Was that true of all the banking units of the Group?

Mr. PATTERSON. I believe it was.

Mr. PECORA. Did you also in connection with your supervision of those examinations of the various unit banks have access to copies of reports on those banks made by the public authorities from time to time, both State and Federal?

Mr. PATTERSON. As to the national banks, yes. The commissioner of banking in Michigan has not followed the practice of supplying State banks with reports of examinations other than merely a letter of criticism.

Mr. PECORA. You were the vice president of the Group when on December 31, 1931, the Guardian National Bank merged with the National Bank of Commerce?

Mr. PATTERSON. Yes, I was.

Mr. PECORA. And became the Guardian National Bank of Commerce?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. Had you made or caused to be made any examination of the National Bank of Commerce prior to that consolidation for the purpose of ascertaining the condition of that bank?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. And did you make any special report to the Group?
Mr. PATTERSON. Yes, sir.
Mr. PECORA. Have you a copy of it?
Mr. PATTERSON. No, I have not.
Mr. PECORA. Do you recall the substance of the conclusions that you stated in your report with regard to the condition of the National Bank of Commerce and the desirability or advisability of the Guardian National Bank merging or consolidating with it?
Mr. PATTERSON. It wasn't my report, Mr. Pecora, and I don't recall much about it now.
Mr. PECORA. Well, can't you tell the committee from your personal recollection whether or not you recommended the consolidation?
Mr. PATTERSON. Yes; I believe I did.
Mr. PECORA. And did you recommend it because your examination revealed to you a healthy condition of the National Bank of Commerce at the time?
Mr. PATTERSON. Well, there were many very excellent economies to be effected by the consolidation. I do not recall whether the condition of the bank was healthy or not, and could not say until I could see the figures, Mr. Pecora.
Mr. PECORA. Well, that was one of the more important consolidations of unit banks effected by the Group, was it not?
Mr. PATTERSON. Yes.
Mr. PECORA. Can't you recall whether or not your judgment, as a result of your examination of the National Bank of Commerce prior to consolidation, was that it was in a good, healthy, wholesome condition or otherwise?
Mr. PATTERSON. I will answer that question in this way: If there were any undesirable assets of quantity there, there was sufficient capital to eliminate them and still leave the consolidated bank with ample capital to protect the deposits. I do not recall the figures so as to accurately answer your question now.
Mr. PECORA. One of the reasons I am asking you these questions, Mr. Patterson, is because my recollection is to the effect that Mr. Lord stated in the course of his testimony before this subcommittee, among other things, that certain conditions of the Guardian National Bank of Commerce were really inherited by his original institution as a result of this consolidation with the National Bank of Commerce.
Mr. PATTERSON. That is probably apparent now. That is to say, at the time of consolidation, or at the time of the examination made by the Group examiners prior to consolidation, conditions were such that assets afterwards taken over proved to be good—or, rather, proved to be poor as the depression continued and collateral values slipped off.
Mr. PECORA. Do you recall having found in the National Bank of Commerce, prior to consolidation with the Guardian National Bank, that the former bank, the first-named bank, had carried a large amount of the Group stock as collateral for loans?
Mr. PATTERSON. No; I do not recall it now, sir.
Mr. PECORA. Do you recall what the situation was in that particular respect with the Group banking units generally?
Mr. PATTERSON. Yes; I do.
Mr. PECORA. What was it?

Mr. PATTERSON. There was a great amount of collateral of the Group stock held as security for loans.

Mr. PECORA. And to whom or to what classes of persons had those loans so secured been made by the various unit banks? Were they made to officers or directors of the Group or of the unit banks themselves in large part?

Mr. PATTERSON. No; not in large part.

Mr. PECORA. Well, to a substantial extent?

Mr. PATTERSON. No; I wouldn't even say that. Not knowing exactly what the split would be between loans to officers of banks and to other individuals, I could not say that. But may I say this, that as time went on the amount of the Group stock held was the result of the exchange of Group stock for bank stock.

Mr. PECORA. Well, I am speaking now of the policy of making loans secured by Group stock, regardless of how the Group stock found its way into the hands of borrowers.

Mr. PATTERSON. I do not believe there was any pronounced policy to deliberately make loans and take Group stock as collateral. It was only taken when it was necessary to get any or all kinds of security to protect a poor loan, or as it became poor.

Mr. PECORA. Do you recall that various national bank examiners from time to time severely criticized the large amount or blocks of Group stock which various unit banks held as collateral for loans?

Mr. PATTERSON. Yes, sir; I do.

Mr. PECORA. Do you recall that those criticisms were constantly recurring?

Mr. PATTERSON. Yes, I do.

Mr. PECORA. What, if anything, was done by the Group officials to remedy that situation?

Mr. PATTERSON. Anything and everything.

Mr. PECORA. Well, what? That answer is too general.

Mr. PATTERSON. Well, we were having a war out in our country, and we were trying to collect loans from people who were nearly broke. And I think that the record of liquidation in the banks of the Group, particularly at Flint, at Grand Rapids, and at Saginaw, if you could review them you would agree with me that they had done all that anybody humanly could do.

Mr. PECORA. Well, will you tell us what, specifically, was done to meet the criticisms of national-bank examiners which were based, in part, upon the holding of so many shares of Group stock as collateral for loans?

Mr. PATTERSON. Why, the officers endeavored to convert the loans into cash wherever they could.

Mr. PECORA. Did they succeed?

Mr. PATTERSON. I think they did, pretty well.

Mr. PECORA. Or did those loans secured by Group stock increase in amount from the time national-bank examiners first began to criticize them.

Mr. PATTERSON. Well, I do not believe I could specifically answer that question, Mr. Pecora, unless I could have the figures to go on. I would not want to trust my memory. I should say that there were none purchased.

Mr. PECORA. Would you say that they were reduced to meet the criticisms of national-bank examiners?

Mr. PATTERSON. Possibly not substantially reduced.

Mr. PECORA. Would you say they were reduced at all?

Mr. PATTERSON. Yes; I would.

Mr. PECORA. Now, let me call your attention to the following item of criticism embodied in the report of the examination of the National Bank of Commerce, which report was made in April of 1929 by William Taylor, then bank examiner and now chief national-bank examiner in Chicago. I am quoting from the report:

> Loans aggregating $2,029,015 secured entirely or in part by 2,583 shares of stock—

Referring to stock of the Union Commerce Investment Co.—

> are subject to criticism on two occasions: First, the concentration is regarded as excessive; and, second, for the reason that the investment company owns practically all the stock in the subject bank, and the pledged stock as collateral for loans amounts to a circumvention of the law.

Did you become familiar with the situation referred to in that criticism?

Mr. PATTERSON. In April of 1929?

Mr. PECORA. Yes.

Mr. PATTERSON. No. And I was not——

Mr. PECORA (interposing). I know that you were not connected with the Group at that time; but I mean when you specifically made an examination of the National Bank of Commerce for the purpose of determining or enabling the Group to determine the advisability of consolidating that bank with the Guardian National Bank.

Mr. PATTERSON. Yes.

Mr. PECORA. Did you then familiarize yourself——

Mr. PATTERSON (interposing). Yes.

Mr. PECORA (continuing). With those criticisms?

Mr. PATTERSON. No; not with the criticisms.

Mr. PECORA. Well, with the condition?

Mr. PATTERSON. Yes; I knew what they had.

Mr. PECORA. Now, the Union Commerce Investment Co. was the investment affiliate or securities affiliate of the National Bank of Commerce, wasn't it?

Mr. PATTERSON. I believe it was; but I cannot tell you very much about the Union Commerce Investment Co.

Mr. PECORA. Why not?

Mr. PATTERSON. Because I do not know much about it.

Mr. PECORA. Well, it was one of the units owned by the Group, wasn't it?

Mr. PATTERSON. No. It was a corporation which Mr. Blair and his associates formed for the purpose of acquiring banks, and the Guardian Detroit Group afterwards acquired the Union Commerce Corporation.

Mr. PECORA. This Union Commerce Investment Co. was a holding company, wasn't it?

Mr. PATTERSON. I cannot tell you much about it, Mr. Pecora.

The CHAIRMAN. What became of it? Did it disappear entirely; that is, I mean the corporation, or what became of it?

Mr. PATTERSON. The Union Commerce Corporation was merged with the Guardian Detroit Group, and afterwards liquidated by them.

Mr. PECORA. Mr. Patterson, it so happens that you were chief national bank examiner for the seventh district in April of 1929, when the National Bank of Commerce was examined by Mr. William Taylor.

Mr. PATTERSON. Yes, sir.

Mr. PECORA. And you signed the report, didn't you?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. Now, the criticism that I read to you is embodied in the report which you yourself signed.

Mr. PATTERSON. Those reports are signed, Mr. Pecora, by all chief bank examiners as a matter of routine.

Mr. PECORA. Only as a matter of routine?

Mr. PATTERSON. Pretty largely that; yes, sir.

Mr. PECORA. Doesn't the chief national bank examiner when he reviews reports made by examiners working under his direction do something more than merely affix his signature to the examiner's report as a matter of form?

Mr. PATTERSON. Oh, yes, sir, depending upon the situation. But chief national bank examiners are in no different category than any other examiner, and each examiner prepares his own report, and it is his.

Mr. PECORA. It is his report, but it is submitted first to the chief national bank examiner for the district, and then is transmitted to the Comptroller of the Currency, isn't it?

Mr. PATTERSON. I will put it this way: The report is prepared by the field examiner for the Comptroller of the Currency, and the report is typed in the chief examiner's office, and he signs it and forwards it to the Comptroller of the Currency.

Mr. PECORA. Well, does the chief examiner sign it without familiarizing himself with its contents? Is that the custom?

Mr. PATTERSON. Oh, no. Reports are scanned. It is assumed always, unless it is a very difficult case, that the examiner has handled all the criticisms on the ground.

Mr. PECORA. Well, the purpose of the examiner itemizing subjects of criticism is to concentrate attention, isn't it?

Mr. PATTERSON. That is right.

Mr. PECORA. Not only on the part of the Comptroller of the Currency but on the part of the immediate superior of the field examiner, namely, the chief bank examiner for the district.

Mr. PATTERSON. That is correct.

Mr. PECORA. Well, now, didn't you notice that your field examiners in the early part of 1929 were calling attention to the vice embodied in the situation where a bank carried a substantial line of loans secured by stock of a holding company which, in turn, owned the bank through stock ownership?

Mr. PATTERSON. No, sir. That was not noticed. That is to say, it was not brought up as a major item at that time.

Mr. PECORA. Well, now, let us see about that——

Mr. PATTERSON (continuing). It was one form of concentration of credit it is true, which was probably entitled to criticism, but not particularly noticeable merely because it was holding company stock acting as security for a large aggregate of loans.

Mr. PECORA. Just let us see what the field examiner said, for this is the field examiner's language embodied in the report which you signed. Under the caption "Loans Secured by Stock in Union Commerce Investment Company", he says:

> Loans aggregating $2,029,015 secured entirely or in part by 2,583 shares of stock of this company, are subject to criticism on two occasions: First, the concentration is regarded as excessive; and, secondly, for the reason that the investment company owns practically all the stock in the subject bank, and the pledged stock as collateral for loans amounts to a circumvention of the law.

Now, that was not an ordinary criticism, was it?

Mr. PATTERSON. Why, yes, I would think it was.

Mr. PECORA. Do you think where a field examiner reports a condition which he regards as practically amounting to a violation or circumvention of the law, is something that does not require any special consideration by the chief bank examiner?

Mr. PATTERSON. Well, that was his opinion, as to circumvention of the law.

Mr. PECORA. And you adopted that opinion when you signed the report, didn't you?

Mr. PATTERSON. No; I did not.

Mr. PECORA. Why did you sign the report if you disagreed with any part of it?

Mr. PATTERSON. I did not disagree with any part of it. I signed it as a matter of office routine.

Mr. PECORA. Well, I asked you before if that was the spirit in which chief national bank examiners performed their duties when they signed reports made to them by their field examiners. Do they merely sign the reports without any consideration of their contents?

Mr. PATTERSON. No, sir; they do not.

Mr. PECORA. Do they sign them, in other words, as a matter of routine as you have just stated?

Mr. PATTERSON. They sign them pretty largely as a matter of routine, and they make note of any serious criticisms, and it is always assumed that the examiner has endeavored to correct the criticisms while on the job.

Mr. PECORA. Well, now, when you signed your field examiner's report in this instance, did you observe this criticism that he made with respect to a practice that he found in the bank and which he specifically reported amounted to a circumvention of the law?

Mr. PATTERSON. That report is almost a matter of fair phraseology, and I do not recall it.

Mr. PECORA. I am now reminding you of it by reading to you the precise language, and am asking you for a statement of policy which was adopted by you as the chief national bank examiner in the district at the time.

Mr. PATTERSON. The policy in regard to all concentration of loans was to recommend to the Comptroller of the Currency that the banks be written and their attention called to them, and I imagine the Comptroller did it in this case.

Mr. PECORA. Now, the criticism that I have read to you from this report, Mr. Patterson, appears on that page of the report which is captioned "List of Items Requiring Attention and not any Corrections Made or Promised During Examination."

Wouldn't any items of criticism, appearing under that caption, require especially the attention of the chief national bank examiner of the district?

Mr. PATTERSON. No. Those criticisms are written for the attention of the Comptroller of the Currency.

Mr. PECORA. Well, does the chief national bank examiner pass them on without any consideration of his own?

Mr. PATTERSON. It is only in unusual cases where the chief examiner, in transmitting another examiner's report to the Comptroller of the Currency, will write a letter about it. Reports are merely signed and forwarded in that way to the Comptroller's office.

Mr. PECORA. Are you trying to tell us by that answer that the chief national bank examiner signs reports prepared by his field examiners purely as a matter of routine?

Mr. PATTERSON. Not always. Wherever——

Mr. PECORA (interposing). Is that the general rule, or did you follow that rule generally?

Mr. PATTERSON. I followed that general rule; yes, sir.

Mr. PECORA. And do you know whether that was followed in the same fashion by other chief national bank examiners in other districts?

Mr. PATTERSON. No; I cannot say as to that.

Mr. PECORA. The next examination of the National Bank of Commerce appears to have been made in October 1929. By that time you had ceased to be the Chief National Bank Examiner for the 7th District and had become vice president of the Guardian Detroit Union Group, had you not?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. From the report which was made of the examination of the National Bank of Commerce in October 1929 let me read the following item of criticism to you, on the page captioned "List of Items Requiring Attention" and "note any corrections made or promised during examination," the following item appears "Loans secured by Union Commerce Company stock: 10,665 shares secures loans totaling $2,294,910.81. Such loans have technically been made in violation of law, since all but 391 shares of stock of subject bank is owned by this company"

Doesn't that indicate to you, Mr. Patterson, that the condition complained of by the examiner whose report you signed as the Chief National Bank Examiner for the District in April 1929, instead of having been abated by the bank's officials, had become more aggravated by October 1929?

Mr. PATTERSON. In that period; yes, sir. The loans had increased and the collateral had increased. I would like to make this observation, however, that undoubtedly a review of the market price of that collateral will show that a great many of the loans were adequately secured. The examiner is merely calling attention to a concentration of credit.

Mr. PECORA. The examiner did something more than that, didn't he?

Mr. PATTERSON. What was it?

Mr. PECORA. Called attention to the continued violation or contravention of the law?

Mr. PATTERSON. Yes, he did.

Mr. PECORA. That is a matter of serious consideration, is it not?

Mr. PATTERSON. It was his opinion as to whether or not it was a contravention of law.

Mr. PECORA. Did your opinion differ from the field examiner's opinion on that when you signed the April 1929 report?

Mr. PATTERSON. I believe it did, sir.

Mr. PECORA Then why did you sign the report?

Mr. PATTERSON. I say I signed the report merely transmitting it to the Comptroller.

Mr. PECORA. And you signed it knowing or feeling that the field examiner had made a criticism of a very serious character in which he virtually charged a violation of the law, while you disagreed with that conclusion of the field examiner?

Mr. PATTERSON. There are many reports the chief examiner signed of many other field examiners where violations of law are more pronounced than that.

Mr. PECORA. Let us confine ourselves to the instance that we are speaking of. Won't you please do that, Mr. Patterson?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. You want the committee to understand that when you signed the field examiner's report of the examination of the National Bank of Commerce of Detroit in April 1929, which report called attention to what the field examiner stated to be a circumvention of the law, of the National Banking Act in other words, did you sign that report as the Chief National Bank Examiner for the district while you disagreed with that conclusion or criticism of the field examiner?

Mr. PATTERSON. I signed the report but did not indicate any such disapproval. I tell you now that I probably did disagree with the examiner then.

Mr. PECORA. Then why did you permit that criticism to stand if you thought it was an unjust or unfair one?

Mr. PATTERSON. It was the examiner's own criticism and not mine.

Mr. PECORA. But you made it your own when you signed the report, did you not?

Mr. PATTERSON. Oh, no; I beg to differ. The report was signed as a matter of transmitting it to the Comptroller.

Mr. PECORA. Would not a forwarding letter merely serve to transmit the report without your having signed it as the Chief Examiner?

Mr. PATTERSON. That is not the way it is done, sir.

Mr. PECORA. Then do you still want us to understand that the Chief National Bank Examiner signs the reports of examinations made by his field examiners without regard to their contents and merely for the purpose of forwarding them to the Comptroller of the Currency?

Mr. PATTERSON. It is largely that. As a matter of fact, the chief examiner is merely, in signing the report, the examiner's attorney-in-fact.

Mr. PECORA. Did you ever disagree while you were chief examiner in any district with the conclusions of your field examiners embodied in their reports?

Mr. PATTERSON. Many times.

Mr. PECORA. Well, did you indicate that disagreement?

Mr. PATTERSON. Not always; no, sir.

Mr. PECORA. Where you did, how did you indicate it?

Mr. PATTERSON. By letter.

Mr. PECORA. By letter to whom?

Mr. PATTERSON. To the Comptroller.

Mr. PECORA. Do you recall whether in this instance you gave expression to your disagreement with that conclusion of the field examiner in any letter you sent to the Comptroller of the Currency?

Mr. PATTERSON. I don't recall. I don't believe I did.

Mr. PECORA. Do you mean that you were willing to pass on to the Comptroller of the Currency over your signature as a chief national bank examiner for the district a report which in words stated that certain things were being done by the bank in contravention of the law without calling the Comptroller's attention to the fact that you disagreed with that conclusion of the field examiner?

Mr. PATTERSON. Yes; I apparently did that in that case.

Mr. PECORA. Do you think that that is the way in which a chief national bank examiner should attend to his duties?

Mr. PATTERSON. Well, the chief national bank examiner has many duties, and sometimes he cannot cover everything.

Senator COUZENS. While you are on that point, Mr. Patterson, will you please tell the committee what the duties of the chief national bank examiner are, and particularly in view of the fact that you say you signed all these reports as a matter of form?

Mr. PATTERSON. His duties are to maintain the office of the chief examiner, which includes the supervision of clerks who reconcile bank accounts, correspondent accounts, the typing and preparation of the field examiners' reports, to see that the various examinations at the banks are kept up and men routed, provide that they are properly systemized.

Senator COUZENS. Does not include visiting any of the banks that are examined at all?

Mr. PATTERSON. Sometimes.

Senator COUZENS. Isn't it a fact that some of the chief bank examiners do go around and call on the banks which their assistants examine and discuss these matters with the directors?

Mr. PATTERSON. Yes, sir.

Senator COUZENS. Describe your duties in that connection.

Mr. PATTERSON. In some of the larger and more difficult examinations I participated in the discussions with the field examiners, or if it was not possible for me to attend the discussions at that time later on I called the bank. It was merely a matter of call.

Senator COUZENS. Now, in connection with the query that has just been made by Mr. Pecora, did you discuss with any of these banks who were criticized as carrying their own stocks or circumventing the law or making technical violations, any of those questions?

Mr. PATTERSON. No, sir.

Senator COUZENS. Then apparently you must have thought that these technical violations and circumventions of law were an ordinary occasion and that there was no particular object of your discussing them with the banks who were charged with them?

Mr. PATTERSON. I left that to the Comptroller to determine whether or not it was a circumvention of law, inasmuch as I believed it was merely the examiner's opinion.

Senator BARKLEY. Were these reports of the examiner made to you or to the Comptroller and just passed through you?

Mr. PATTERSON. To the Comptroller.

Senator BARKLEY. They were not made to you at all?

Mr. PATTERSON. The field examiner's pencil copy of reports are forwarded to the chief examiner's office for typing and finished. Many times the examiner cannot be present when the report is finished and we sign his name for him. Each chief examiner signs for him.

Senator BARKLEY. You sign his name and then sign your own?

Mr. PATTERSON. That is right.

The CHAIRMAN. What is the precise language preceding your own signature?

Mr. PATTERSON. I don't remember, Senator, what it is.

Mr. PECORA. I was just looking at that, Senator.

The CHAIRMAN. It was a question of whether you merely say "I herewith transmit the report of the field examiner", or whether you sign some sort of certificate as to its correctness or soundness.

Mr. PATTERSON. The examiner supplies us with a small form or certificate authorizing the chief examiner to sign for him.

The CHAIRMAN. I mean following that comes the signature of the chief examiner, either that he is hereby transmitting the report of the field examiner or that the report he has examined and approved.

Mr. PATTERSON. Yes.

The CHAIRMAN. Now, which happens? What does happen?

Mr. PATTERSON. I would say it was merely a transmittal.

Senator BARKLEY. Where the report of the examiner shows a situation which is so serious that it ought not to wait for the ordinary routine of a transmittal to Washington and a report from the Comptroller, does the chief examiner assume any authority to take any action and make any examination to correct it?

Mr. PATTERSON. When the examination has been finished, Senator, and the situation is very serious, the examiner will ask the chief examiner to immediately participate with him in formulating some plan and correct whatever is found to be wrong. Many times directors are called into the chief examiner's office for discussion as to means to effect that correction. If the situation is large and immediate, the chief examiner will get in touch with the Comptroller's office for advice.

The CHAIRMAN. What provision of the law do you have in mind as being contrevened? Do you recall that? What law is that?

Mr. PATTERSON. I would say that it was the statute preventing the making of loans secured by its own bank stock.

The CHAIRMAN. There is a statute against that?

Mr. PATTERSON. Yes, sir.

The CHAIRMAN. Well, that was done here, was it not?

Mr. PATTERSON. It was holding company stock, Senator.

Mr. PECORA. But the holding company owned all but some three hundred-odd shares of the capital stock of the subject bank, did it not?

Mr. PATTERSON. That is correct.

Mr. PECORA. And that circumstance was specially called attention to by the field examiner?

Mr. PATTERSON. That was one of his criticisms that was specially mentioned; yes, sir.

Mr. PECORA. So that in effect he was reporting that the bank had made a substantial number of loans, the amount of loans aggregating over $2,000,000, which were secured by the stock of the holding company, which in turn owned practically all of the capital stock of the bank?

Mr. PATTERSON. Yes. It is quite probable that this examiner was proceeding on the same theory that many others have. The large amount of shares here was undoubtedly due to the exchange of bank shares, wherein the holders got a great many shares more of holding company stock than they formerly held of bank stock.

Mr. PECORA. What has that got to do with the matter of correcting what is reported to be a circumvention of the law with regard to the making of loans?

Mr. PATTERSON. It hasn't anything to do. I was merely offering an explanation of the large number of shares which were reported.

The CHAIRMAN. Were any of these loans made to the directors of the bank?

Mr. PATTERSON. I don't recall whether they were or not.

Mr. PECORA. Mr. Chairman, I have before me a photostatic reproduction of the entire report that was made of the National Bank of Commerce as of April 25, 1929. That report is signed in the following manner: The signature of William Taylor—or rather the name "William Taylor"—is typewritten on a line over the printed word "Examiner." Directly underneath is the typewritten word "by"; then the handwritten signature of "B. K. Patterson, Chief Examiner." So that the only handwritten signature is that of the chief examiner.

Mr. PATTERSON. That is right.

Mr. PECORA. And you say that in this case you affixed your signature to Mr. Taylor's report virtually as a matter of form or routine?

Mr. PATTERSON. I think you should see the form or certificate which each examiner, including Mr. Taylor, signed in transmitting this pencil copy authorizing me to sign the finished copy for him. I don't recall just what that is, Mr. Pecora.

Mr. PECORA. We will find it for you. Now, by October 1929, you had, as already testified, become the vice president of The Group. Was it then called to your attention that the condition complained of by Examiner Taylor in April 1929, had not been allayed, but that rather had been aggravated?

Mr. PATTERSON. Yes; I knew that there had been an increase in shares and some increase in loans based upon those shares.

Mr. PECORA. What, if anything, did you do about it?

Mr. PATTERSON. In October 1929?

Mr. PECORA. Yes.

Mr. PATTERSON. Nothing.

Mr. PECORA. An examination of the National Bank of Commerce and Union Trust Co. was made as of September 15, 1930, by the National Bank Examiners and again attention was called to this evil of the bank making loans secured by the stock of the holding company, which in turn owned practically all of the shares of the bank. Are you familiar with the situation that was disclosed by that report?

Mr. PATTERSON. I don't recall it now.

Mr. PECORA. Do you recall whether by that time anything at all had been done by the group to alleviate the condition complained of with respect to the unit banks making, and particularly the National Bank of Commerce making, a large amount of loans secured by the stock of the holding company?

Mr. PATTERSON. I recall that there was a pretty well-defined policy to try to reduce as much as possible.

Mr. PECORA. Do you recall that in the pursuit of that policy the outcome was an increase in the amount of collateral consisting of stock of the group held by the bank?

Mr. PATTERSON. No, I don't recall it now.

Senator COUZENS. Mr. Patterson, while Mr. Pecora is looking that up will you tell us what jurisdiction you have over your subordinates?

Mr. PATTERSON. While with the group?

Senator COUZENS. No, while you were chief bank examiner of the seventh district.

Mr. PATTERSON. Well, they were all directly the employees of the Comptroller of the Currency, and chief examiners are also employees of the Comptroller of the Currency. Each of the field examiners is assigned to specific subdistricts within each Federal Reserve district.

Senator COUZENS. By whom?

Mr. PATTERSON. By the Comptroller of the Currency. And he establishes convenient headquarters in order to examine the banks as economically as possible. He proceeds to do that without any particular orders from the chief examiner, inasmuch as he knows what banks are due for examinations.

In addition to that the chief examiner is provided with three or more examiners who are not assigned to any particular district, for work at large. These examiners are specifically assigned by the chief examiner to special cases or to large examinations in the larger districts.

Senator COUZENS. Have you any jurisdiction to remove or reprimand or facilitate the efficiency of the examiners?

Mr. PATTERSON. That should come directly from the Comptroller, although in many instances the chief examiner makes recommendations to the Comptroller.

Senator COUZENS. But you do not check up on the examiners to see whether they are doing efficient work or not or whether their reports are reliable, do you?

Mr. PATTERSON. Not particularly, no, sir, unless it is a flagrant case.

Senator COUZENS. Well, who is responsible for looking after the examiners to see that they do properly the work and their reports are satisfactory and the examinations are satisfactory? Whose responsibility is that?

Mr. PATTERSON. Well, directly the Comptroller, I would say, but of course the chief examiner is held responsible, too.

Senator COUZENS. You have no authority to remove anybody or to change them or to reprimand them for the kind of examinations that they make?

Mr. PATTERSON. No, sir.

Senator BARKLEY. You do have authority to recommend removals and you do have authority to transfer men in your district from one place to another, don't you?

Mr. PATTERSON. Only by recommendation, Senator.

Senator BARKLEY. You mean you cannot take a man out of one territory within your district and put him in another?

Mr. PATTERSON. No, sir.

Senator BARKLEY. Don't you direct where he should go to examine a bank?

Mr. PATTERSON. Only within his own district.

Senator BARKLEY. That is what I mean.

Mr. PATTERSON. Yes.

Senator BARKLEY. And you do recommend in other cases?

Mr. PATTERSON. If he were to be transferred to another district that would have to be recommended to the Comptroller and he would arrange it.

Senator BARKLEY. But you would make the recommendation for transfer?

Mr. PATTERSON. Yes, sir.

Senator BARKLEY. And you do make the recommendations for dismissals where you do not think that the examiner is complying with your idea of his performance of his duties?

Mr. PATTERSON. Yes, sir.

Senator BARKLEY. And in order to make such a recommendation you have to know something about his work, don't you?

Mr. PATTERSON. Yes, sir.

Senator BARKLEY. And you know that from examining him?

Mr. PATTERSON. Yes, sir.

Senator BARKLEY. So that you do have a good deal of authority over him?

Mr. PATTERSON. Well, sometimes; sometimes not.

Senator COUZENS. I still do not understand. If you signed those reports in behalf of Mr. Taylor, then you did it just as a matter of form and without any knowledge of your own as to whether Mr. Taylor had conducted an efficient and competent examination?

Mr. PATTERSON. Why, Senator, many of these reports are signed by the chief clerk in the chief examiner's office when the chief examiner is away from the office.

Senator COUZENS. So those examiners are free-lances and there is no one around anywhere apparently to check up on the examiners to see whether they are doing competent and efficient work—is that not a fact?

Mr. PATTERSON. No; I would not say that.

Senator COUZENS. Just what is the check? I am trying to find out what check there is to find out whether the national-bank examiner does a proper and efficient job. Whose responsibility is it and who passes on it?

Mr. PATTERSON. It is likely reflected in the kind of reports he makes and the amount of correction of criticizable things he discovers.

Senator COUZENS. Well, in signing this report for Mr. Taylor you did not agree apparently with the statement that he made that these were technical violations and a contravention of the law; you did not agree, but you let it go by without any comment. Who is supposed to comment on that, the Comptroller's office?

Mr. PATTEROSN. Yes, sir.

Mr. PECORA. Does not the Comptroller's office look to the chief national-bank examiner for a review of the field report?

Mr. PATTERSON. Not in all cases, no, sir.

Mr. PECORA. Well, in what cases does the Comptroller of the Currency rely upon the chief national-bank examiner for a review of the field reports?

Mr. PATTERSON. Only in those cases where it is a very serious affair.

Mr. PECORA. And who is supposed originally to determine whether there is a very serious affair, as you call it?

Mr. PATTERSON. The examiner.

Mr. PECORA. And after him the chief examiner?

Mr. PATTERSON. Yes; he will frequently call upon the chief examiner for his advice.

Mr. PECORA. From the way you have described the manner in which you acted in transmitting after signing the reports of the field examiners under your supervision one might be led to believe that the chief national-bank examiner in each district is nothing more than a rubber stamp for the field examiners. That is not a sound conception of the chief examiner's function, is it?

Mr. PATTERSON. Well, that may be the way you have construed it. I believe in actual practice you would find differently.

Mr. PECORA. What would you find in actual practice that would make him anything more than a rubber stamp for the field examiner?

Mr. PATTERSON. You are referring to the report only?

Mr. PECORA. I am referring to the performance of duty by a chief national-bank examiner.

Mr. PATTERSON. Certainly not.

Mr. PECORA. If the chief examiner signs his name on the field examiner's reports as matter of routine, why is he anything more than a mere rubber stamp for the field examiner?

Mr. PATTERSON. Well, I would not say that he is a rubber stamp.

Mr. PECORA. Why not?

Senator COUZENS. As a matter of pride—that is all you say it for, not as a matter of fact?

Mr. PATTERSON. No; I think that if you could understand some of the duties of the chief examiner you would think that he was anything but a rubber stamp.

Senator COUZENS. That is what we are trying to find out.

Mr. PECORA. Yes. Tell us what the duties are.

Mr. PATTERSON. Well, I have just told you that while reports are signed by the chief examiner for the examiner upon his authorization to sign them, in difficult cases the chief examiner will immediately get into it himself and find out what is the matter and try to assist the examiner in the correction of serious affairs.

Senator COUZENS. Then you did not construe this as a difficult case?

Mr. PATTERSON. No, sir; apparently not.

Mr. PECORA. Why did you disagree with the conclusion of Examiner Taylor when he reported that these loans made by the banks secured by the stock of the holding company, which in turn owned practically all of the stock of the bank, were in circumvention of the National Banking Act prohibiting the making of loans secured by the bank's own stock?

Mr. PATTERSON. A holding company holding bank stock was a rather new thing in April of 1929, at least in the seventh district, and it was not clear to me that any position had been taken on it by the Comptroller's office as to whether or not it did amount to a circumvention. I don't recall now that the Comptroller's office ever took a position on that point.

Mr. PECORA. You were thoroughly familiar with the provision of the Banking Act prohibiting a national bank from making loans secured on its capital stock, were you not?

Mr. PATTERSON. Yes, sir; except in those cases where they take the collateral for debts previously contracted.

Mr. PECORA. In the instance of the examination of the National Bank of Commerce made in April 1929 it was reported to you that loans had been made by the bank in contravention of that provision of the National Banking Act that I have just called your attention to. Why did you disagree with Examiner Taylor's conclusion in that respect?

Mr. PATTERSON. I have just stated that I did not believe it had been clearly outlined by the Comptroller's office that a circumvention had occurred, inasmuch as holding companies who held bank stocks were so new in the seventh district that it never had been decided.

Mr. PECORA. Was that any reason you took a position contrary to that advanced by the field examiner?

Mr. PATTERSON. That was the reason why I did.

Mr. PECORA. Well, weren't you called upon as the chief examiner for the district to reach some determination yourself on that? The mere fact that the question was a novel one to you was no reason why you should sidestep it, was it?

Mr. PATTERSON. No.

Mr. PECORA. As you now reflect on the situation, is it still your opinion that the making of those loans secured by the stock of the holding company which owned the stock of the bank was not in substance a contravention of the law?

Mr. PATTERSON. No, sir; I don't believe it is.

Senator COUZENS. Will you explain why, because from a practical standpoint it seems to me that it is loaning money on the bank stock? I would like to have your angle of it.

Mr. PATTERSON. It is a direct loan on a corporation stock and not bank stock, as defined in the statute.

Mr. PECORA. You were looking here to form rather than substance when you reached that conclusion, were you not?

Mr. PATTERSON. That is right.

Senator ADAMS. Mr. Patterson, if the holding company had only held stock of this one bank could you have drawn that distinction then?

Mr. PATTERSON. No, sir. I beg your pardon—I did not understand your question, Senator.

Senator ADAMS. My question was this: You were drawing a distinction between loaning on a bank's stock itself and loaning on the stock of a corporation which held the bank stock.

Mr. PATTERSON. Yes, sir.

Senator ADAMS. I was asking you if the holding company had limited its ownership to the stock of the particular bank that was making the loan——

Mr. PATTERSON. Yes.

Senator ADAMS. Would you then have looked through the form to the substance of it?

Mr. PATTERSON. No; I don't believe I would change my opinion even then.

Senator ADAMS. You would have still thought that was all right?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. Do you revere form more than you do substance?

Mr. PATTERSON. Well, no; I would not say so.

Mr. PECORA. Don't you think in effect that is what you were doing here?

Mr. PATTERSON. Well, as a matter of fact, I didn't do anything there, Mr. Pecora.

Mr. PECORA. Then you were a rubber stamp in this particular instance?

Mr. PATTERSON. No.

Mr. PECORA. You say you did not do anything, but you signed the report. Does the signing of the report represent an idle act? In other words, is your signature simply a rubber stamp signature?

Mr. PATTERSON. So far as the report is concerned it is merely a signature under the authorization of the examiner to transmit the report to the Treasury.

Mr. PECORA. Was it in substance a rubber stamp signature then?

Mr. PATTERSON. Oh, if you wish to call it that; yes, sir.

Mr. PECORA. All right.

Senator ADAMS. What became of the original pencil copy, which I assume was signed?

Mr. PATTERSON. That is filed in the chief examiner's office.

Senator ADAMS. You retain that?

Mr. PATTERSON. Yes, sir.

Senator ADAMS. That comes as a signed copy?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. In the examination of the National Bank of Commerce, made in the fall of 1930, the following criticism appears:

> Loans secured by Guardian Detroit Union Group stock, 48,431 shares of this stock held as collateral.
>
> New loans with this stock as collateral unfavorably regarded. Numerous loans based thereon at present lacking collateral coverage.

Did you, as vice president of the Group, whose special function it was to attend to or supervise examinations of the various banks, the unit banks of the Group, do anything about meeting this criticism?

Mr. PATTERSON. I do not recall that particular instance, except that I was almost in daily contact with officers of that bank in regard to many matters. I did not get the date of that report, Mr. Pecora.

Mr. PECORA. September 15, 1930.

Mr. PATTERSON. By that time the market price of the collateral had gone off seriously, which accounts for the examiner's statement that the collateral is short, I believe you said, or words to that effect.

Mr. PECORA. He said, "Numerous loans based thereon at present lacking collateral coverage."

Mr. PATTERSON. That is right.

Mr. PECORA. He also called attention to the fact that over 48,000 shares of the Group stock was held as collateral for loans by the National Bank of Commerce.

Mr. PATTERSON. Yes, sir.

Mr. PECORA. So that the amount of such stock had increased over the amount reported during the preceding year?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. Which leads to the conclusion that the condition called attention to in the preceding year had not been allayed but had been permitted to become aggravated?

Mr. PATTERSON. Largely because of the fact that they had to acquire any and all collateral possible in order to protect the loans. I will say now, without knowing the circumstances, that no new loan was made.

Mr. PECORA. Don't you know that the number of loans increased substantially, which were secured by the group stock, by September 1930?

Mr. PATTERSON. No, sir; I do not recall.

Mr. PECORA. The next examination of the bank—that is, the National Bank of Commerce—appears to have been made as of March 2, 1931, and the field examiner happened to be Mr. R. L. Hopkins in that instance, who finally became an officer of the group or one of its unit banks. Do you recall that?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. Do you recall the condition reported by Examiner Hopkins as the result of his examination of March 1931, with respect particularly to the amount of group stock held as collateral by the National Bank of Commerce?

Mr. PATTERSON. No, sir; I do not recall that.

Mr. PECORA. Do you recall that the report indicated that the condition had continued to become aggravated instead of relieved?

Mr. PATTERSON. I do not even recall having seen that particular report.

Mr. PECORA. Were these reports kept from you?

Mr. PATTERSON. No, sir; they were kept by officers of the bank.

Mr. PECORA. But you, as the vice president of the group, were specially charged with the function, as I understood your testimony earlier this morning, of supervising these reports made by your bank examiners.

Mr. PATTERSON. No; not supervising the reports.

Mr. PECORA. To act upon the conditions indicated by the reports?

Mr. PATTERSON. We endeavored to make our own examinations; and my testimony was with respect to Messrs. Bryan and Penningroth, and not with respect to the national bank examiners' reports after I had gone with the Group.

Mr. PECORA. Let me read to you the following criticism made by Examiner Hopkins in March 1931:

> The bank has necessarily had to be lenient in their attitude in dealing with loans secured by the stock of their parent corporation, and undoubtedly a policy of reducing the aggregate of such loans will be carried out as soon as practicable.

Do you recall that?

Mr. PATTERSON. No; I do not.

Mr. PECORA. Do you recall the condition that prompted the bank to be lenient in its attitude toward loans secured by the stock of the Group or, as Mr. Hopkins calls it, the "parent corporation"?

Mr. PATTERSON. No; I do not think I do recall that.

Mr. PECORA. Were those criticisms being lightly passed over or ignored by the Group officers?

Mr. PATTERSON. Certainly not.

Mr. PECORA. What was being done about this particular item of criticism between 1929 and the spring of 1931?

Mr. PATTERSON. Everything that it was humanly possible for officers of the bank to do, to reduce loans which were already undercollateral because of the shrinkage in security values, and particularly in that stock, the holding company's stock.

Mr. PECORA. What, specifically, was done?

Mr. PATTERSON. The collection of the loans or the acquisition of additional collateral to strengthen the loans.

Mr. PECORA. Was any measurable success made at all in that respect?

Mr. PATTERSON. I think so.

Mr. PECORA. Let me read further to you what Mr. Hopkins had to say in his report of the March 1931 examination, under the caption of "List of Items Requiring Attention":

Loans secured by the capital stock of the Guardian Detroit Union Group. The management should seriously consider the possibility of an unwarranted concentration being brought about through an apparent liberal policy in extending loans predicated on shares of an affiliated or parent concern. Many of the loans classified as slow in this report are secured by this stock and now show a deficit due to the reduction in market value. Being unable to forecast the future trend of the market price of this stock no other course is felt warranted. Should the stock increase in market value to an average over the past 18 months many of these loans will automatically be removed from the classified section. The bank has necessarily had to be lenient in their attitude in dealing with loans secured by the stock of their parent corporation, and undoubtedly a policy of reducing the aggregate of such loans will be carried out as soon as practicable.

Mr. PATTERSON. I do not recall those remarks; I do not think I ever heard them before.

Mr. PECORA. You were an executive officer of the group and a former chief national bank examiner who, you said, were specially charged with the function, as such vice president of the group, to look into the condition from time to time of the various unit banks of the system. Now, you are telling us that the report of the national bank examiner on the National Bank of Commerce, one of the unit banks, made in March 1931, was not brought to your attention by anybody?

Mr. PATTERSON. I do not think it was.

Mr. PECORA. How do you account for that?

Mr. PATTERSON. I do not know.

Mr. PECORA. Do you think there was any studious attempt to keep this information from you?

Mr. PATTERSON. No; I do not believe so.

Mr. PECORA. But you are unable to account for the fact that this report was not brought to your attention?

Mr. PATTERSON. I would like to ask, Mr. Pecora, whether you are reading from the confidential section of that report or the open section of the report, in those remarks?

Mr. PECORA. This is the open section of the report.

Mr. PATTERSON. I do not recall ever having seen it, sir.

Mr. PECORA. Can you give any reason why you did not see it? Do you know why it was withheld from you or that you were not permitted to see it, by anybody?

Mr. PATTERSON. No, sir.

Mr. PECORA. You knew an examination had been made, did you not?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. Did you call for the report?

Mr. PATTERSON. No; I did not.

Mr. PECORA. Why didn't you do that?

Mr. PATTERSON. We were going on our own reports pretty largely.

Mr. PECORA. When you say that, do you mean that you were ignoring the reports made by the national bank examiners and relying upon the examinations made by your own men?

Mr. PATTERSON. No; not ignoring them at all.

Mr. PECORA. Apparently, when you had not even seen the report or had it brought to your notice, if you were not ignoring it somebody was seeing to it that you did not learn of it.

Mr. PATTERSON. I do not know who it was.

Mr. PECORA. Why did you not call for the report of an examination that you knew had been made?

Mr. PATTERSON. As I say, we were relying on our own reports of examinations.

Mr. PECORA. More than you were on the reports of the national bank examiners?

Mr PATTERSON Well, yes

Mr. PECORA. Do you think that is a fair guide, Mr. Patterson, for a bank officer to be guided more by an examination made by some one employed by the bank rather than an examination made under the independent auspices of the Comptroller of the Currency?

Mr. PATTERSON. Well, frankly, Mr. Pecora, I had a little more faith in our own men in making our own examinations.

Senator ADAMS. Were you a director of the bank?

Mr. PATTERSON. No, sir; I was not.

Senator ADAMS. You do know that the bank directors are forced to send word to the Comptroller's office that they have personally given consideration to these reports?

Mr. PATTERSON. Yes, sir; I know that.

Mr. PECORA. Mr. Patterson, let me repeat part of the language of this criticism:

> The management should seriously consider the possibility of an unwarranted concentration being brought about through the apparent liberal policy of extending loans predicated on the shares of an affiliated or parent concern.

In view of that language, how is it that the management, or at least that part of the management that you took part in, did not even consider this report or learn of it?

Mr. PATTERSON. I was not a part of the management of the bank.

Mr. PECORA. Would you think that referred only to the management of the bank?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. The stock of the bank was owned by the group. Did not that place the responsibility for the management of the bank directly upon the group's officers and board?

Mr. PATTERSON. Not entirely; no. The management of each bank was left up to its own officers and its own directors.

Mr. PECORA. Without any supervision by the group?

Mr. PATTERSON. Oh, yes.

Mr. PECORA. Why was not that supervision given to it in this instance?

Senator COUZENS. When you said, "Oh, yes", what did you mean?

Mr. PATTERSON. I have lost it now, Senator Couzens.

Senator COUZENS. The reporter will read the question and the answer, please.

(The question and answer referred to were read by the reporter as above recorded.)

Mr. PATTERSON. I was mistaken. I would like to change it and say no.

Senator COUZENS. Then it was under some supervision of the group?

Mr. PATTERSON. Yes.

Senator COUZENS. It appeared before in the evidence that they were dictating the dividend policies of the banks, so I thought you must have been in error when you made your answer, "Oh, yes."

Mr. PATTERSON. When I say that the banks were supervised by the group, I mean we made examinations of them and we were in daily contact with whatever problems they had. The management of the National Bank of Commerce was very well regarded, and I am sure that they put full confidence in a criticism of Mr. Hopkins or other examiners and they did all they could to protect bad loans as security values were fluctuating.

Senator COUZENS. Who employed Mr. Hopkins in the group?

Mr. PATTERSON. The employment of Mr. Hopkins came about in this way, Senator. Mr. Mott, of Flint, had talked to Mr. Covington and myself about the affairs there, and he asked us if we could make a suggestion for some one to take Mr. Wilkin's place. Mr. Covington and I conferred and we thought that Mr. Hopkins would make a desirable bank officer in Flint, and suggested his name to Mr. Mott. Later on Mr. Mott and Mr. Hopkins were brought together.

Senator COUZENS. So you recommended, or at least joined in the recommendation of Mr. Hopkins to Mr. Mott?

Mr. PATTERSON. Yes, sir.

Senator COUZENS. I assume you know that Mr. Hopkins had been reporting to the Comptroller of the Currency that they should be lenient with your Group, do you not?

Mr. PATTERSON. No; I did not know that.

Mr. PECORA. You said that you depended more on your own examinations of these unit banks than on the examiners, the national bank examiners. Was a report of the examining committee of this bank, that is, of the National Bank of Commerce, made in May 1931?

Mr. PATTERSON. I do not know.

Mr. PECORA. Well, perhaps this will serve to refresh your recollection, if I read to you the following extract from a report made by the examining committee of the National Bank of Commerce in May 1931?

Senator COUZENS. Will you please state at that point who the examiners were, Mr. Pecora?

Mr. PECORA. The members of the examining committee were as follows: Edwin H. Nelson, John R. Russel, George H. Klein, Francis C. McMath, and Hal H. Smith.

I will read the entire report, Mr. Patterson to see if it refreshes your recollection [reading]:

The committee has reviewed in detail every loan which has been marked "slow, doubtful, or loss" by either the national bank examiner or by the bank's officers, and has discussed as to each of said loans the responsibility of the maker, the security to the loan, and the prospects of payment. The total estimate of loss ($3,097,944.73 on 268 loans) represents a combined judgment of the committee and the bank's officers as to such loss. It has not yet been able to review in detail the bonds, securities, and mortgages owned by the bank. It has accepted the statement of the national bank examiner as to the bank's cash, the correctness of its accounts and the physical presence of the bank's securities in its vaults.

The large amount of the estimated loss on the loans calls for some explanation and comment by the committee. It is the opinion that the major cause of these larger losses and the greater number of loans which have been so estimated has been the poor credit information assembled by the credit department in the past and the lack of proper organization of the loaning responsibility in the officers of the bank. These two major causes have, however, as the committee believes, now been corrected. The credit department has been reorganized and remanned and the loaning responsibility and authority of the officers has been radically and materially strengthened. All poor credits cannot be eliminated, but the committee has reason to believe that the fundamental defects have been removed.

The committee, however, feels called upon to make the following suggestions and recommendations as to future policies for which it asks the approval of the board:

1. Not sufficient attention has been paid in the past to the character of the respective borrowers and their income capacity. Too much emphasis has been placed on the collateral alone. A large number of loans have been made on what was sufficient collateral at the time of the inception of the loan, but where the maker was of doubtful earning capacity and not good character as a credit risk. This should be corrected in the future. The fundamental of every loan should be the character of the borrower and the excess of collateral should not justify a loan to any one of doubtful honesty or without any material earning capacity.

2. The committee finds in the list of bad loans many loans that obviously have no other purpose than speculation in the stock market. The makers of these loans had only limited earnings and no prospects of the payment of the loan otherwise than the rise in stock prices. They are made to clerks, stenographers, bank officers and bank clerks, salesmen, and others whose income was not sufficient to warrant any substantial credit. These loans should be definitely discouraged in the future.

3. The committee finds also in the list of bad loans, loans to officers of this bank and officers in other banks which were clearly made to assist or further stock-market operations. This class of loans has been a source of loss to the bank, and the encouragement of these loans has ruined many worthy bank officials. In the future no loaning officer of this bank should be permitted to have a margin account or should become indebted to this bank or any of its correspondents to purchase stocks. If knowledge of loans of this character made by any officer of this bank comes to the attention of the officials of this bank the officer should be required to close out such loans at the earliest practicable moment. Applications by, officers of other banks for this class of loans should be reported to executives of that bank before any action is taken. These rules should be rigidly enforced.

4. One of the major causes of loss has been loans to real-estate operators and companies engaged in real-estate operations and stock equities in real estate. In almost every instance the real estate has been subject to prior indebtedness, and the loan, therefore, no matter what form it takes, is certainly no better than a second mortgage. This class of loans should be definitely eliminated. Loans on real estate or any equity therein should not be accepted except in particular instances, and on approval of responsible committees of the bank.

5. We find on the list of loans a substantial number of individuals who have been recommended by directors of the bank for such loans, loans to friends of directors whose only claim for the accommodation is that of acquaintanceship, loans to associates of directors in business, and loans to concerns in which the directors are interested or in which they were officers. Obviously the cases in which a director should recommend any loan to the bank without his endorsement should be rare. Where there is any doubt as to the credit or the matter of a loan is as described above, the endorsement of the directors should be asked. This rule should be applied to the loans now in the bank and any loans made in the future.

6. The committee finds in the list of bad loans a great many so-called "policy" loans. Judges of courts, referees in bankruptcy, and other political officers have been extended substantial credit. Many of these loans are doubtful. All these loans should be stopped, and the so-called "policy" loans should be eliminated. Doubtful loans made where the action is in reality the hope of securing a deposit should be eliminated. Every loan should, in the future, meet the single test of the maker's ability to pay, independent of all the foregoing considerations.

7. We have, in the course of the examination, found that the makers of some slow and doubtful loans have complained that they made the loan in order to buy certain securities recommended by an officer of the bank or securities in which this bank or some affiliated institution was directly or indirectly interested. Loans made for this purpose should be rigidly scrutinized and a definite policy should obtain, except in cases where there is some good reason for the exception, of declining loans for the purpose of financing the purchase of any securities in which this bank or its affiliates are directly or indirectly interested.

8. Instances were brought to the attention of the committee where certain officers of the bank have recommended the purchase of stock or securities. A definite rule should be established that this should not be done, and the officer breaking this rule should be promptly disciplined.

9. The bank has been from time to time requested to purchase bonds or other securities on a repurchase agreement. This is not sound banking practice and should be discouraged even with the members of the Guardian Detroit Union Group.

10. The committee feels that the discount committee of the bank has not been given the opportunity to pass on a sufficient number of the loans in the past, and has not given sufficient attention to the application of the borrowers. It is obvious that the committee could not pass upon all minor loans, but if it were frequently convened it could see that the loaning policy of the bank as fixed by the board was maintained. We recommend that the committee be asked to meet frequently and that every loan and its renewal be submitted.

11. The credit files do not contain all the information that the officers desire. The committee recommends that the officers should be instructed to ask for a certified balance sheet and detailed statements of all unsecured loans of corporations of $10,000 or over.

12. The large deposit accounts which the bank has on which demands may be made at any time for substantial payments require, in the opinion of the committee, that particular attention be given to the investment of funds in commercial paper and in loans that are eligible for rediscount with the Federal Reserve bank or in securities in which there can be an immediate realization. This policy is, in the opinion of the committee, more important than the increase of our miscellaneous deposits or the distribution of our loans and discount facilities over a wide range of borrowers.

13. The amount of investments of the bank in bonds and securities is so great that the committee believes that the responsibility of keeping a daily check on the situation of these bonds and securities, if not now delegated, should be delegated to some one officer designated by the president. A special committee should be created for the purpose of reviewing these investments at least once a month. The purchase of bonds should continue to be handled by the president. The constantly changing situation on municipal securities and the fluctuations in the value of other bonds require, in our opinion, much more constant and detailed consideration of this class of the bank's assets than has been given it in the past.

14. The bylaws of the bank at the present time require that the examining committee count the cash and verify the accounts of the bank. This is too great a responsibility for the committee. It is obvious that it should do neither. The bylaws should be amended to relieve it of this responsibility. It should still be required, however, to examine the loans and investments in detail and still be permitted to report its recommendations as to the general policies of the bank. The committtee will, if it be continued, examine the mortgages and the bonds of the bank and make a further report thereon.

A schedule of the criticized loans is attached. It is likely that a salvage will be made from these loans, but the committee urges that full support be given to the particular officers who now have the direct responsibility for those collections, and that every officer make every effort to realize as much as possible on these debts. The progress on this work should be reported monthly to the board.

Respectfully submitted.

That is the end of the report, with the exception of the schedule of the criticized loans.

The CHAIRMAN. It is something like locking the stable door after the horse has been stolen.

The committee will now take a recess until half past 2.

(Whereupon, at 11:45 a.m., a recess was taken until 2:30 p.m., the same day, Jan. 3, 1934.)

AFTER RECESS

The subcommittee resumed at 2:30 p.m. on the expiration of the recess.

The CHAIRMAN. The subcommittee will resume.

TESTIMONY OF BERT K. PATTERSON—Resumed

Mr. PECORA. Mr. Patterson——

Mr. PATTERSON (interposing). Mr. Pecora, might I make a few remarks with regard to the testimony of this morning?

Mr. PECORA. Yes.

Mr. PATTERSON. In connection with certain criticisms of bank examiners, in the matter of examination of the National Bank of Commerce of Detroit during 1929 and 1930, where there was raised the question as to the legality of a national bank lending against collateral of a holding company: During the noon recess one of my associates called my attention to a letter, which I had never seen before, written by the Comptroller of the Currency to another national bank examiner in January of 1929, and with your permission I should like to read the letter. One of my reasons for asking this permission is that it will show, I think, that examiners reported directly to the Comptroller of the Currency, and had the privilege of writing the Comptroller in regard to examinations, or on any other subject; and, secondly, it will be somewhat of a confirmation of my idea at the time and which I testified to this morning.

The CHAIRMAN. Have you the original letter or is that a copy?

Mr. PATTERSON. This is a copy.

The CHAIRMAN. Do you know whether it is a correct copy?

Mr. PATTERSON. Yes, sir; I believe it is a correct copy.

The CHAIRMAN. All right.

Mr. PATTERSON. It is in confirmation I think, too, of what my idea was relative to the legality of the stock as collateral in a national bank. This letter is dated January 10, 1929, and is addressed to Earl W. Moon, national bank examiner, 164 West Jackson Boulevard, Chicago, Ill.:

DEAR SIR: Your letter of January 4 is received requesting an answer to your letter of December 19.

You state that the officers, directors, and stockholders interested in the Union Trust Company, Griswold First State Bank, and the National Bank of Commerce, all of Detroit, Mich., have organized a corporation known as the Union Commerce Investment Company, but that this corporation is in reality a holding company for the stock of these three institutions; that the assets of the Union Commerce Investment Company consist of the total capital stock of the three institutions except for directors' qualifying shares, and request to be advised whether the National Bank of Commerce may lawfully and without criticism hold stock of the Union Commerce Investment Company as collateral to loans.

The stock of the corporation referred to is not capital stock of the bank within the meaning of section 5201 of the United States Revised Statutes, even though a part of its assets consist of stock of the bank. In the matter of accepting stock of the company as collateral to a loan, it is one for the determination of the management of the bank, although this office does not look with favor on loans secured by stock of a company so closely allied to the bank and having little or no assets other than the stock of banks, national and state.

Your letter of December 19 was inadvertently placed in the files before being answered.

Respectfully,

JOHN S. PROCTOR, *Deputy Comptroller.*

Mr. PECORA. Have you another copy of that letter?

Mr. PATTERSON. I only have this one.

Mr. PECORA. Will you let me have it?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. I want to have the text of it before me.

Mr. PATTERSON. Here it is.

Mr. PECORA. Is there any other statement that you want to make before I resume your examination?

Mr. PATTERSON. I believe not.

Mr. PECORA. Now, when did this letter which you have just read into the record, first come to your attention, Mr. Patterson?

Mr. PATTERSON. This noon.

Mr. PECORA. And through what channels was it brought to your notice this noon?

Mr. PATTERSON. Mr. Frank Blair called my attention to it.

Mr. PECORA. Who is Mr. Frank Blair?

Mr. PATTERSON. Mr. Frank Blair used to be the president of the Union Trust Co., and later on of the Union Guardian Trust Co., and is now connected with the Union Joint Stock Land Bank of Detroit.

Mr. PECORA. I notice that this letter, or the copy thereof which you handed to me, is addressed by the Deputy Comptroller to the national-bank examiner in Chicago.

Mr. PATTERSON. Yes, sir.

Mr. PECORA. Do you know how it happens to find its way in the possession of anyone not connected with the Comptroller of the Currency?

Mr. PATTERSON. No, sir; I do not.

Mr. PECORA. Did you know Mr. Earl W. Moon, National Bank Examiner, to whom this letter was addressed?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. Did he serve under you at any time?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. Do you advance this letter now, or the information or ruling, whatever you may prefer to call it, therein contained, as a justification for your having disagreed with the conclusion or judgment of Mr. Taylor, national bank examiner, or field examiner, under you, who examined the National Bank of Commerce in 1929, and from whose report I read to you this morning?

Mr. PATTERSON. Well, I offer it here because I do not think the question was very clear to the subcommittee this morning, in view of the examiner's criticism. And it is the first thing I have seen bearing on the subject.

Mr. PECORA. You will recall that what Mr. Taylor said in his field report was not that the lending of money on collateral consisting of stock of the holding company, which in turn owned the stock of the bank, was not a violation of the banking law, but rather was a circumvention of it.

Mr. PATTERSON. Yes.

Mr. PECORA. You understand that there is a clear distinction between a violation and a circumvention of any legal provision, don't you?

Mr. PATTERSON. Yes.

Mr. PECORA. Well, apparently the Deputy Comptroller in this very letter that you now advance as a measure of justification for your judgment, felt that in some fashion or other it was an unwise policy for a national bank to make loans on security consisting of the stock of a holding company which in turn owned all the stock of the bank, or substantially all of it. Don't you observe that statement in Mr. Proctor's letter?

Mr. PATTERSON. Yes; I know it is there.

Mr. PECORA. He says:

"'In the matter of accepting stock of the company as collateral to a loan, that is one for the determination of the management of the bank, although this office does not look with favor on loans secured by stock of a company so closely allied to the bank and having little or no assets other than the stock of banks, national and state."

Mr. PATTERSON. Yes, sir.

Mr. PECORA. Do you disregard that statement by Mr. Proctor?

Mr. PATTERSON. No; I do not. But as I say——

Mr. PECORA (interposing). Do you think it is sound?

Mr. PATTERSON. I think it is.

Mr. PECORA. Did you think it was sound back in 1929 when you disagreed with the judgment or conclusion expressed by Mr. Taylor, your subordinate field examiner?

Mr. PATTERSON. Well, Mr. Pecora, I think that, as I stated this morning, as to the legality of the thing, that was something for the Comptroller to pass upon.

Mr. PECORA. You also stated this morning that you did not agree with Mr. Taylor's statement.

Mr. PATTERSON. That is true.

Mr. PECORA. That those loans so secured were a circumvention of the law as distinguished from a violation of it.

Mr. PATTERSON. Oh. Well, I misunderstood you, then. I thought you meant that it was a violation of law.

Mr. PECORA. No. I read the exact language contained in Mr. Taylor's report, which was signed by you as Chief Examiner.

Mr. PATTERSON. Well, I think I would still believe that it was not a circumvention of the law.

Mr. PECORA. Wasn't it in effect the making of loans on security that rested on the bank's stock?

Mr. PATTERSON. That is right.

Mr. PECORA. Isn't that a circumvention of that provision of the law which directly prohibits the making of such a loan, directly secured by the bank's stock?

Mr. PATTERSON. Well, I think that is a legal matter, and I do not believe I could answer it.

Mr. PECORA. Apart from its legality, apart from its legalistic aspect and as a matter of substance don't you think it is just as much a violation of the spirit of the law?

Mr. PATTERSON. No; I do not think so.

Mr. PECORA. Do you think it is in accord with both the spirit and the letter of the law?

Mr. PATTERSON. I do.

Mr. PECORA. What do you think was the purpose of the enactment which prohibited national banks from making loans secured by their own stock?

Mr. PATTERSON. I do not believe I could answer that question either.

Mr. PECORA. Why not?

Mr. PATTERSON. Well, it was, perhaps, for the purpose of preventing the lending of the bank's own capital.

Mr. PECORA. That is sound public policy, isn't it?

Mr. PATTERSON. Yes, sir

Mr. PECORA. Now, where a bank's own capital is owned by another corporation, not organized under the banking laws but practically whose sole asset is the bank's capital, don't you think a loan made by such a bank secured by the stock of the holding company, is in effect a loan secured by the stock of the bank?

Mr. PATTERSON. No; I do not.

Mr. PECORA. What are the differences?

Mr. PATTERSON. I think you are lending against entirely different collateral.

Mr. PECORA. Well, of course it is different collateral in form, but the value of the collateral upon which the loan is made is dependent upon the value of the bank's stock, which is the sole asset of the company whose security in the shape of stock is taken as collateral. Isn't that a fact?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. You still see a difference between the two?

Mr. PATTERSON. As to form, I think there is a difference.

Mr. PECORA. Oh, there is no doubt that there is a difference as to form, but why do you ignore the substance?

Mr. PATTERSON. Well, I suppose you would have to recognize that, too.

Mr. PECORA. Well, do you recognize it?

Mr. PATTERSON. Yes.

Mr. PECORA. And recognizing the substance do you still say that there is fundamentally a difference between the two acts?

Mr. PETERSON. I think if you followed it right on through you would trace it on to a violation.

Mr. PECORA. Do what?

Mr. PATTERSON. That you would probably trace it on to a violation.

Mr. PECORA. Did you follow it through while you were the executive vice president of the group?

Mr. PATTERSON. We accumulated that stock largely as the result of other loans, and we did all we could, all that was humanly possible, during the shrinkage in values, to get the loans out of the bank. We were fighting a war in Detroit, and every loan officer was doing all he possibly could to get that collateral out, not only in Detroit but all over Michigan.

Mr. PECORA. You were fighting a war in Detroit, were you?

Mr. PATTERSON. That is right.

Mr. PECORA. Fighting a war against whom?

Mr. PATTERSON. Against the depression, and the shrinkage of values.

Mr. PECORA. And in order to enable you to fight that war successfully the bank was doing the things that its own examining committee complained of in this report of May 1931, including the making of so-called "policy loans" to the politicians; isn't that so?

Mr. PATTERSON. No.

Mr. PECORA. Was that a part of your campaign to fight the war against depression?

Mr. PATTERSON. No.

Mr. PECORA. And for the conservation of the depositors' interests?

Mr. PATTERSON. The loans that you read this morning were old loans, and they were not made during the time we were "fighting the war" as I term it.

Mr. PECORA. Well, if they were old loans why hadn't they been liquidated at the time that the bank came under the control of the Group?

Mr. PATTERSON. The loans at that time that came under the control of the group, as I remember the situation, were probably good loans as to their security.

Mr. PECORA. Well, isn't that at variance with what the examining committee reported in May of 1931?

Mr. PATTERSON. That was considerably after the time when collateral values had slipped off.

Mr. PECORA. Did you see a copy of this examining committee's report that I read into the record this morning?

Mr. PATTERSON. I think I did.

Mr. PECORA. Did you do anything about it?

Mr. PATTERSON. That was left to the management of the bank.

Mr. PECORA. What was done, if anything, by the management of the bank, do you know?

Mr. PATTERSON. As I say, I think they did all they possibly could.

Mr. PECORA. Do you know what they did?

Mr. PATTERSON. No, sir.

Mr. PECORA. Did the group do anything about it?

Mr. PATTERSON. No, sir.

Mr. PECORA. Why not?

Mr. PATTERSON. Except to institute a policy in regard to any new loans based upon group stock.

Mr. PECORA. Now, you said that the group sought to remedy the situation represented by its unit banks holding large blocks of stock of the group as collateral for loans, by seeking to have those loans reduced by payment. Let me call your attention in that regard to the following item of criticism:

Loans secured by Guardian Detroit Union Group stock: 48,431 shares of this stock held as collateral.

New loans with this stock as collateral unfavorably regarded. Numerous loans based thereon at present lacking collateral coverage.

Now, that was based upon an examination as of September 15, 1930. The next examination of that bank was made as of March 2, 1931, and it indicates that at that time there were 57,531 shares of Group stock held by the bank as collateral for loans, as against 48,431 shares of that stock held in September of 1930. So apparently the group had not succeeded in effectuating what you said was the policy it embarked upon with regard to clearing those loans secured by group stock; isn't that so?

Mr. PATTERSON. It is my opinion, without knowing what the records are between those dates, that any increase in collateral in group stock to any loans, was due to the acquisition of additional collateral of that type to protect poor loans. I do not believe there were any made, or none that I know of at least, any new loans based entirely upon group stock, or largely upon group stock, after the policy had been instituted some time in 1930 as I recall it. They were trying to get any and all collateral they possibly could together, and if that consisted only of group stock the officers took it.

Mr. PECORA. Now let me read to you from the report made by Mr. Hopkins, field examiner, and who afterwards became connected with the Group, based upon his examination of the bank as of March 2, 1931:

> Your examiner is of the opinion that the loans secured by the stock of the Guardian Detroit Union Group constitute an unwarranted concentration. The bank is handicapped in liquidating its debts from the sale of this stock for the reason that the most of its shareholders acquired the stock at a period when it was selling on the market anywhere from $100 to $300. At the beginning of the examination the market value of the stock was $50, and at the time the examination closed the market value had dropped to $40 due to the closing of the American State Bank.
>
> Your examiner has no opinion as to the recovery of the stock, but it is surmised that a long period will be required before the bank is in position to eliminate many of these losses.

Were you familiar with that criticism made by Mr. Hopkins?

Mr. PATTERSON. I do not believe I ever read it, but it sounds familiar.

Mr. PECORA. You have said this afternoon, referring to those loans that were secured in large part by the stock of the Group or holding company that owned the bank's stock, that you thought the most of those loans were old loans and had been made before the Guardian Detroit Union Group had acquired control of the bank. Am I correct in that statement of your testimony?

Mr. PATTERSON. You are substantially correct, I believe.

Mr. PECORA. Then those loans must have been made at the time when you were the chief national bank examiner in that district, isn't that so?

Mr. PATTERSON. That is probably so, and probably before then.

Mr. PECORA. Was that fact brought to your attention?

Mr. PATTERSON. No, sir; it was not.

Mr. PECORA. Well, wasn't it actually brought to your attention by Mr. Taylor, among other persons, in his report of the bank of April 1929?

Mr. PATTERSON. Not particularly that phase of it; no, sir.

The CHAIRMAN. When did the Commerce and those other unit banks begin to call in their loans and refuse loans?

Mr. PATTERSON. During the latter part of 1930, I believe, Senator Fletcher, and continuing through 1931, all banks were liquidating as fast as they could.

The CHAIRMAN. In the latter part of 1930?

Mr. PATTERSON. Yes, sir.

The CHAIRMAN. I thought that was begun pretty soon after October of 1929.

Mr. PATTERSON. Well, I do not believe many of them began as soon as that.

Mr. PECORA. While I am waiting for some data let me ask you this, Mr. Patterson: You heard the testimony week before last submitted to this subcommittee while Mr. Lord was on the stand, with regard to the policy of the group not to have its unit banks show any bills payable on statements made in compliance to the call of the Comptroller of the Currency from time to time for such statements, didn't you?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. You are familiar with that testimony?

Mr. PATTERSON. Yes.

Mr. PECORA. What do you know about that policy?

Mr. PATTERSON. I know that we were trying to make as good a showing in all the banks as we could, at all times. Where there were excess funds in the Guardian Bank and other units of the group were in need of funds, the Guardian Bank made deposits in those unit banks.

Mr. PECORA. To enable them, primarily, or rather temporarily, to take care of bills payable items?

Mr. PATTERSON. Or any other items.

Mr. PECORA. To enable them to take care of bills-payable items specifically, I ask?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. Did you approve of that policy?

Mr. PATTERSON. That was the policy that had been in current use by many banks for years.

Mr. PECORA. Did you approve of that policy, Mr. Patterson, is what I asked you.

Mr. PATTERSON. I was going to add, inasmuch as the Guardian Bank was in funds to lift those bills payable, I approved it; yes, sir.

Mr. PECORA. In other words, you approved of a policy which had for its object a window-dressing purpose, didn't you?

Mr. PATTERSON. Well, that is the term commonly used.

Mr. PECORA. That is the vernacular.

Mr. PATTERSON. Yes, sir.

Mr. PECORA. But it is a very apt characterization of the situation, isn't it?

Mr. PATTERSON. Yes, sir; that was quite widespread in its use. Many banks have done that sort of thing.

Mr. PECORA. Did you approve of it in principle?

Mr. PATTERSON. No; I cannot say that I did, Mr. Pecora.

Mr. PECORA. Did you disapprove of it in principle by any affirmative action that you took?

Mr. PATTERSON. No. As a matter of fact, however, I think that in view of the circumstances, wherever it was used, in certain units of the Group, that at the time it was done it was probably the very best thing to do. The war that we were fighting in Michigan had worn the morale of the people to a very low point, where they were very much concerned about banks in general.

Mr. PECORA. And you thought that morale could better be sustained by misrepresentation.

Mr. PATTERSON. I did not consider it misrepresentation.

Mr. PECORA. Well, was it anything other than misrepresentation in substance if not in form?

Mr. PATTERSON. In principle I did not approve of the practice wherever it could be avoided. However, the circumstances, I repeat, justified it in my mind.

Mr. PECORA. Do you recall any instances where a large depositor of any one of these unit banks was asked to help out in a temporary situation by the making of a large deposit which was permitted to remain on deposit for only a few days or a very short period of time?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. How frequently was that done, Mr. Patterson?

Mr. PATTERSON. I personally know of two instances.

Mr. PECORA. And who was the depositor who was asked to make such temporary deposits?

Mr. PATTERSON. General Motors Corporation.

Mr. PECORA. Anyone else?

Mr. PATTERSON. Not that I know of personally.

Mr. PECORA. Do you know of any instance where a large depositor of any one of the unit banks also maintained a very large deposit account in a Chicago bank and near the end of the year, of a certain year, in response to a request from the Group or its officials drew out a large sum from its Chicago bank by check, deposited it in the Detroit bank and then drew it out of the Detroit bank by check, and the two checks crossed in the mails?

Mr. PATTERSON. No.

Mr. PECORA. Do you know of any such instance?

Mr. PATTERSON. I don't believe I do.

The CHAIRMAN. How long has that practice been going on among banks, the practice of banks eliminating temporarily in this way bills payable?

Mr. PATTERSON. Why, I don't know, Senator, for how many years, but in certain distressed areas of the country where bank failures have been the rule it has been a common practice probably for 10 years, perhaps.

The CHAIRMAN. As bank examiner did you have occasion to inquire into that sort of practice or disapprove of it in any way?

Mr. PATTERSON. Yes, sir; we did.

The CHAIRMAN. Generally you would not as an examiner condone or favor a practice like that?

Mr. PATTERSON. It would depend upon the circumstances, Senator, just as it did in our Group during 1930, '31, and '32. I do not want to speak for all national bank examiners, but I think a constructive examiner will take into consideration the existing circumstances.

The CHAIRMAN. Did you ever know of any just such circumstance arising before?

Mr. PATTERSON. Yes. Where a bank is an important one and more or less in a distressed condition, efforts upon the part of national bank examiners are to try to save the bank from disaster, and in the course of that if they are successful in getting large deposits in the bank in order to make a better showing in a statement which will not arouse the public, many of them practiced it.

The CHAIRMAN. The effect of it was to represent to the public that the bank's financial condition was better than it really was, was it not?

Mr. PATTERSON. The general idea was to protect the larger public interest and prevent failure, prevent a run.

Senator COUZENS. When you were on the witness stand week before last, Mr. Patterson, I think you were asked the question whether you purchased any stock which you had contracted to purchase when you entered the employ of the Guardian Group. Is that correct?

Mr. PATTERSON. Yes. I contracted to purchase 300 shares of stock. The contract is dated October 1, 1929, and calls for the purchase of 300 shares at $275 a share.

Senator COUZENS. Did you purchase that?

Mr. PATTERSON. I did not pay for it.

Senator COUZENS. You did purchase it, though?

Mr. PATTERSON. The contract was signed, yes, sir.

Senator COUZENS. Well, did you follow out the contract?

Mr. PATTERSON. I paid about $11,000 in interest on that contract, nothing on the principal.

Senator COUZENS. Did you borrow any money to do that with?

Mr. PATTERSON. No, sir.

Senator COUZENS. Are you a bank examiner now out of the seventh district?

Mr. PATTERSON. I am employed by the Federal Reserve Bank of Chicago.

Senator COUZENS. And what are your activities with the Federal Reserve Bank of Chicago?

Mr. PATTERSON. I have been principally engaged in the handling of applications by State banks for membership in the Federal Reserve system.

Senator COUZENS. Are you in debt to any of the banks?

Mr. PATTERSON. No, sir.

Senator COUZENS. You are not in debt to any of them?

Mr. PATTERSON. No, sir.

Senator COUZENS. So you did not borrow any to pay that $11,000 interest on your contract?

Mr. PATTERSON. No, sir; I did not.

Senator COUZENS. Is the contract canceled now?

Mr. PATTERSON. No; it is not.

Senator COUZENS. Is it still an obligation you have?

Mr. PATTERSON. The receiver of the Guardian Holding Co. holds it as an asset. I presume it is still in force.

Senator COUZENS. You do not feel that you are going to be able to carry out the contract?

Mr. PATTERSON. I don't think so.

Mr. PECORA. Let me read to you the following general remarks made by Examiner Hopkins while he was national bank examiner of the condition of the National Bank of Commerce as of October 6, 1931:

> Large balances: Including public funds, the records show that $43,500,000 is carried in 54 accounts. The largest of these is the Ford Motor Co., which has a balance of $25,420,000, others ranging from $7,000,000 down.

This fact might appear to constitute a dangerous situation. However, the management maintains that all of them are extremely close to the bank and that in event of a run on the bank by its depositors these particular depositors would in no manner afford any trouble. If this be true, the extreme quick liability of the bank's assets would be sufficient to pay off all of the other depositors.

"Liquidity" is probably what was meant. The word in the report is "liability".

The fact remains, however, that the Ford Motor Co. account is rather erratic at times, and frequently the bank finds it difficult to borrow funds for a few days' duration. The management has agreed to strengthen the liquid position.

Under the caption of "Earnings":

The earnings have not been all they might have been desired, because of the low interest return on so large a portion of the assets. Every economy possible is being maintained in order to show greater earnings. The large amount of interest paid on deposits is having its effect on the net earnings.

And under the caption of "Guardian Detroit Union Group" appears this:

All of the stock of this bank except the directors' qualifying shares is owned by the Guardian Detroit Union Group. A list of the affiliations is shown on page 11A. Considerable weakness is known to exist in several of the affiliated banks. The Group has apparently failed in contributing policies which tend to clean up these affiliated banks, and charge-offs are made reluctantly. Apparently the Group management has been unable to inject policies which were originally planned into the various units, and the local management operates almost in the same manner as they did prior to their acquisition.

The stock of the Group has continuously declined from a high point of $310 to $20 since 1929. At the time of this examination the stock was priced at the market of $23. The market is rather inactive, and efforts to stabilize it at higher prices have been unsuccessful. A large portion of the losses resulting to this bank has come from the policy of riding along on those loans which were secured by this stock, and for the reason that foreclosing out of such loans would create a feeling of hostility among those customers who had paid excessive prices in the beginning. Undoubtedly, all of the units hold substantial amounts of this stock in their collateral files.

In view of these facts, the stock has lost its liquidity, since any suggestion of forced sales would run the market to very low figures. This situation should be closely watched.

Mr. Covington, the vice president of this bank, stated to me that he would undertake to create a pool from the directorate of the group banks with sufficient contributed funds to furnish relief to this bank and at the same time maintain the market on the stock.

The CHAIRMAN. What bank is that?

Mr. PECORA. This is the National Bank of Commerce, one of the unit banks which was at the end of this year, 1931, consolidated with the Guardian National Bank.

Senator COUZENS. Was what Mr. Covington promised carried out, Mr. Patterson?

Mr. PATTERSON. I believe so, yes.

Mr. PECORA. Under the caption of "Losses" the following appears in this report of Mr. Hopkins while he was the national bank examiner:

The losses shown in the report by no means represent the actual losses set up at the time of the discussion, and other estimated losses of approximately $1,000,000 could have been set up. The examiner accepts the responsibility for this action, inasmuch as the bank has so recently reduced its surplus fund to the sum of 2½ million dollars and met the recommendations of the examiner in the matter of charge-offs at the time of the previous examination. To further reduce the surplus fund at this time would undoubtedly create undesirable comment in this city and might prove disastrous.

The bank is unquestionably solvent. The condition found here is not altogether desirable, and a strong letter should be addressed to the board of directors touching on the matters contained herein. If not inconsistent with the policies of your office, the matter of holding shares of the Guardian Detroit Union Group as collateral to loans should be brought to their attention.

Are you familiar with those remarks in this report?

Mr. PECORA. Was this matter ever brought to the attention of the board so far as you know? I am referring to the matter of holding shares of the Guardian Detroit Union Group as collateral to loans.

Mr. PATTERSON. I think Mr. Hopkins may have called it to the attention of the executive committee of the bank.

Mr. PECORA. Do you know what action was taken on it?

Mr. PATTERSON. No, sir; I do not.

Senator COUZENS. What is Mr. Hopkins doing now?

Mr. PATTERSON. Mr. Hopkins is employed by the Federal Deposit Insurance Corporation.

Senator COUZENS. Where?

Mr. PATTERSON. At Lansing.

Senator COUZENS. Michigan?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. Now, following the consolidation of the National Bank of Commerce with the Guardian National Bank, Mr. Lord, who had been president of the Guardian National Bank prior to the consolidation, continued as president of the consolidated institution, did he not?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. Are you familiar with the report made on the examination of the bank by the national examiner as of May 16, 1932?

Mr. PATTERSON. I don't believe I ever saw that report, Mr. Pecora. That was the examination by Examiner Walker?

Mr. PECORA. By Examiner Walker, yes.

Mr. PATTERSON. I never saw that.

Mr. PECORA. Do you know why you did not see it? Do you know any reason why you did not see it?

Mr. PATTERSON. I think the officers merely kept it.

Mr. PECORA. What were you doing about exercising the main function that I understood from your testimony this morning had been delegated to you as executive bank president of the Group of attending to the examination of these banks and keeping the Group posted as to their condition from time to time?

Mr. PATTERSON. Mr. Lord was president of the bank, and I presume he saw the report, and Mr. Covington also, and I did not think it was necessary for any Group officer to go any further than that.

Mr. PECORA. Were they kept from you for any reason?

Mr. PATTERSON. No; I don't believe they were kept from me for any particular purpose.

Mr. PECORA. Let me read the following statements under the caption of "General remarks" from the report of the bank, the Guardian National Bank of Commerce, as of May 16, 1932, under the caption of "Losses":

The losses listed at this time are only a nominal amount in comparison with the actually existing losses irrespective of further substantial doubtful items. In extended meeting with the bank's executive committee, at which meeting Chief Examiner Leyburn and your examiner was present, it was agreed that losses of roughly $1,200,000 were to be charged off at this time. The committee felt that to charge off an amount in excess of this figure when conditions are in their present demoralized condition would only add fuel to the flames and would do more harm than good by impairing the surplus fund in any way.

And under the caption of "management" let me read these remarks in the report:

The management of the bank has rested in the hands of President Lord, who is not the strong, dominant type that the bank is so much in need of today. He is believed to be more or less heavily involved and probably insolvent, though he is not borrowing of the bank and does not furnish a statement. In this condition himself, he is hardly qualified to pass intelligently upon credits, for your examiner has noticed that when a loaning officer is himself in bad financial condition he does not view credits in the same light that he would were he in good financial condition himself. His attitude is more one of riding along to see what is going to happen next, rather than to face the facts and to figure out corrective measures immediately.

Under the caption of overhead charges I will read to you as follows from the report:

Salaries have been reduced 10 percent, which is not enough in proportion to earnings, but there are many officers and employees who are owing substantial amounts to the bank who cannot meet their interest payments unless the bank pays them enough to do so. In other words, then, the bank is actually paying the interest for the employee, for in numerous instances other capable men could be employed at materially less money than is being paid now, and the bank would be receiving just as much value for materially less money.

Were you familiar with that condition at that time?

Mr. PATTERSON. Yes. I never heard the report before.

Mr. PECORA. That was the condition, was it not?

Mr. PATTERSON. Approximately that; yes, sir.

Mr. PECORA. The bank could not let go these officers who owed it money for fear that the bank would thereby not be able to collect even the interest on the loans?

Mr. PATTERSON. Well, the remarks of the examiner in my opinion are a little too general. I do not think that would apply to every officer in the bank.

Mr. PECORA. He does not say that it applies to every officer. He said "There are many officers and employees." That is correct, isn't it?

Mr. PATTERSON. Well, yes; I would say that it is.

Mr. PECORA. Now let me read this portion of the report under the caption of "Real Estate Mortgages Under Foreclosure:"

Detroit has probably been as hard hit as any large industrial city in the United States, for prosperity of this town is of course contingent upon the automobile industry. Forty percent of the bank's capital is now invested in the other real estate account, and with mortgages going into foreclosure every day, the next examination will doubtless reflect a very material increase in this undesirable account.

Are you familiar with the fact that as much as 40 percent of the bank's capital was invested in real estate mortgages?

Mr. PATTERSON. I do not remember just what the figures are. It occurs to me at the moment that the examiner is somewhat overdrawing the picture there, Mr. Pecora. The capital of the bank was $10,000,000, as I recall. Forty percent of that would be approximately $4,000,000, and it does not seem to me that $4,000,000 of the real estate mortgages were in foreclosure. Now I may be wrong, but I just don't recall that amount.

Mr. PECORA. Well, as a matter of fact, according to the report of the condition of the bank as of May 16, 1932, the bank actually had loaned $4,085,015.71 on "other real estate." That is other real estate than that owned by the bank.

Mr. PATTERSON. Well, I had forgotten.

Mr. PECORA. Now let me read the following statement from this report of condition or examination as of May 16, 1932, under the caption of "Guardian Detroit Union stock held as collateral":

> A list of the loans which this bank is carrying on this stock is incorporated in this report, and it is not surprising that there are many of these loans which are short on collateral by large amounts, when we stop to reflect that the stock sold for over $350 a share and is now quoted nominally at $5.50, though no material amount of the stock could be liquidated at even this figure.

You know that at that time the bank actually carried 149,574 shares of the Group stock as collateral for loans?

Mr. PATTERSON. Yes; that sounds about right.

Mr. PECORA. Which represented an increase of nearly 100,000 shares over the number of shares carried as collateral on loans as of March 2, 1931?

Mr. PATTERSON. I imagine, however, that increase is due to the consolidation of the banks that occurred on December 31, 1931.

Mr. PECORA. Was that increase also due to the fact that the bank continued to loan on that kind of collateral?

Mr. PATTERSON. I would say not.

Mr. PECORA. Are you sure of that?

Mr. PATTERSON. I am quite sure of it; yes, sir.

Mr. PECORA. Had the practice prevailed in the Guardian National Bank prior to the consolidation with the Guardian Detroit Bank of making loans secured by the stock of the Group or holding company?

Mr. PATTERSON. With very few exceptions, and certainly not after approximately the middle of 1930

Mr. PECORA. Under the caption of "Large balances" let me read to you as follows from this report as of May 16, 1932:

> Over 30 percent of the bank's deposits are in 11 accounts, as shown in the confidential section of this report. While some of these deposits might prove a source of strength, that is, the Ford balances might remain and even be built up somewhat in case of an emergency, there are other balances which probably would not prove to be as friendly. There are so many angles to this situation, and most of which are weaknesses, that this institution could find itself in even more serious difficulties if some one of its affiliated banks or itself should be subjected to a heavy run. On the other hand, the names of Edsel Ford, Charles S. Mott, and some others, lend material strength to the picture.

Are you familiar with the situation reflected in that portion of the report?

Mr. PATTERSON. You are referring to the amount of deposits in a few accounts? Yes, sir; I am.

Mr. PECORA. I am referring to what I have read from the report.

Mr. PATTERSON. It is the first time I have heard the report, but I am familiar with the condition that he is talking about.

Mr. PECORA. Now let me read from this report the following statement made by the examiner as an answer to the form question reading:

> What person or persons, if any, in your opinion, dominate the policies of the bank, and to what extent?

The answer is as follows:

There seems to be friction existing between President Lord and Executive Vice President Covington.

Were you familiar with that situation?

Mr. PATTERSON. I don't believe there was any friction between the two men, Mr. Pecora.

Mr. PECORA. In answer to this form question:

If control is owned by individual or affiliated interests, give particulars as to how maintained and the amount of stock owned or controlled.

The answer of the examiner is:

All shares except directors' qualifying shares stand in the name of Guardian Detroit Union Group.

That was true; wasn't it?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. Now let me read the examiner's answer to this question:

Are the directors men of independent judgment and familiar with the affairs, or are they dependent upon active officers or directors and leave the management to them?

The answer is as follows:

Men of independent judgment who as a rule, judging from the attendance record, leave the bank's operations largely in the hands of the active officers.

Do you think that is a fair statement?

Mr. PATTERSON. Yes; I do.

Mr. PECORA. In answer to the question in the printed form of the report reading:

Do you consider the bank absolutely solvent, both in having collectable assets sufficient to pay depositors and other creditors and its ability to meet maturing and the usual demands in the ordinary course?

The answer to that is, "See remarks", and these are the remarks embodied in the report:

Aside from the many serious criticisms listed on page 11, the most serious of all is the fact that not only is there practically no justified earnings which the parent corporation can acquire in the form of dividends from its various affiliated banks, but the Detroit Union Group has liabilities of about $14,500,000, which together with the expense of operation of around $130,000 a year, makes it encumbent upon the company to derive revenue of around $850 000 to meet interest charges and expenses. In other words, in the ordinary unit bank the double liability feature is a source of some strength as a rule, whereas here we have not only no strength from the principal stockholder, the Guardian Detroit Union Group, but in addition the parent company must derive, as stated above, some $850,000 a year to keep its own head above water.

From this angle it will be readily seen that the situation is a serious one, and I would not care to hazard a guess as to the future of this bank and the others in the group, few if any of which could keep their doors open if this bank found it impossible to carry on.

Senator COUZENS. What date was that?

Mr. PECORA. This is as of May 16, 1932.

Senator COUZENS. Is that the copy of the report sent to the Comptroller?

Mr. PECORA. Yes, sir. This is a report made by Mr. Harry W Walker, field examiner, which is signed by the chief examiner.

Would you say that those remarks were based upon the existing facts?

Mr. PATTERSON. I think the examiner has drawn a picture just about as I see it.

Mr. PECORA. In other words, he was fairly accurate?

Mr. PATTERSON. I think he was.

Mr. PECORA. Do you know when the Guardian National Bank of Commerce declared its first dividened in the year 1932?

Mr. PATTERSON. No, Mr. Pecora; I do not recall.

Mr. PECORA. Do you recall that the National Bank of Commerce declared a dividend amounting to $200,000 for the first quarter of the year 1932?

Mr. PATTERSON. Yes; I think I do.

Mr. PECORA. Do you know the circumstances under which that dividend was declared?

Mr. PATTERSON. Well, it was for the purpose of paying a dividend on the Group stock, together with dividends received from other units of the Group.

Mr. PECORA. Was it done in order to help the group out?

Mr. PATTERSON. I do not think so. You mean, to pay interest?

Mr. PECORA. In order to help the group out by putting it in possession of funds with which to meet its own obligations?

Mr. PATTERSON. No. My recollection is that it was paid to group stockholders as a dividend. Those funds which you spoke of, $200,000, together with other funds from the other units of the group, were used to pay a dividend.

Mr. PECORA. Do you recall the last dividend that was declared and paid by the group on its stock?

Mr. PATTERSON. I think it was the first quarter of 1932.

Mr. PECORA. It then paid a dividend amounting to $386,022 for that first quarter of the year 1932?

Mr. PATTERSON. That is about 25 cents a share.

Mr. PECORA. Yes; exactly 25 cents a share. Of that dividend of $386,000-odd, $200,000 was obtained from a dividend of that amount paid by the Guardian National Bank of Commerce, was it not?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. Do you know the circumstances under which the Guardian National Bank of Commerce declared that dividend for the first quarter of 1932?

Mr. PATTERSON. I do not know what you mean by "circumstances." Their profit account probably was sufficient for them to declare that amount into the group company.

Mr. PECORA. Why do you say that the profit account was probably sufficient?

Mr. PATTERSON. Well, I do not know what the figures are now.

Mr. PECORA. Have you any consciousness or recollection of the fact that the condition of the bank in its earnings did not justify the payment of such a dividend by the bank?

Mr. PATTERSON. No, I do not. My recollection is that they did have sufficient earnings to pay that dividend.

Mr. PECORA. Do you know whether or not the dividend was actually paid out of current earnings or was it paid in part out of earnings and in part out of surplus funds?

Mr. PATTERSON. I cannot remember the figures now.

Mr. PECORA. You know that the national bank examiner in his report of the condition of the Guardian National Bank of Commerce on May 16, 1932, stated that the dividend which was declared for the first quarter of 1932 was illegal?

Mr. PATTERSON. No; I did not know that he stated that.

Mr. PECORA. And that the reason it was illegal was because there was not a quorum of the board of directors in attendance?

Mr. PATTERSON. No; I did not know that, Mr. Pecora.

Mr. PECORA. Did you know that in his report of condition as of May 16, 1932, the national bank examiner stated that the condition of the assets of the bank did not warrant the declaration of any dividend at the end of the current dividend period, which would be for the second quarter?

Mr. PATTERSON. No; I did not know that it was in the report.

Mr. PECORA. Apparently the bank did not declare a dividend for the second quarter of 1932. Do you recall that fact?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. Did it declare a dividend at any subsequent time during the year 1932?

Mr. PATTERSON. I have not the dividend record here; I could not say.

Mr. PECORA. Well, according to the dividend record which I have, the bank declared a dividend for the final quarter amounting to $150,000. Do you know whether the payment or the declaration of that dividend was justified by the earnings and by all the other circumstances of the bank?

Mr. PATTERSON. I would say that it was justified at the time. It seems to me that there were earnings sufficient then to declare that amount.

Mr. PECORA. Were you a member of the board of this bank?

Mr. PATTERSON. No, sir.

Mr. PECORA. But as the executive vice president of the group whose special function it was to inquire from time to time into the condition of the bank units of the group, did you not know the condition of the bank?

Mr. PATTERSON. Approximately; not intimately.

Mr. PECORA. According to the report of the National Bank Examiner, who in this instance was Mr. W. A. Reagan, on the condition of the Guardian National Bank of Commerce as of November 9, 1932, he then reported slow loans aggregating $5,388,682.52, doubtful loans $18,692,876.22, and loss of $546,942.07. Does that accord with your recollection of the condition of the bank?

Mr. PATTERSON. I do not remember ever seeing Mr. Reagan's report. I believe that that report was not delivered to the bank until some time after the 1st of January, although I am a little bit hazy on that point, and by that time we were working very hard at other matters.

Mr. PECORA. Did you know that the doubtful loans alone, independently of the slow loans, that were reported by the National Bank Examiner as of November 9, 1932, actually exceeded the entire capital funds of the bank at that time, which aggregated $17,945,433.93?

Mr. PATTERSON. Yes; apparently they did.

Senator COUZENS. Did you know it at that time?

Mr. PATTERSON. No, sir.

Mr. PECORA. Do you think that under those circumstances any dividend should have been declared for the final quarter of the year 1932?

Mr. PATTERSON. In view of the necessity to take care of some of the indebtedness of the Group Corporation, I would say, yes.

Mr. PECORA. Of the Group Corporation?

Mr. PATTERSON. Yes.

Mr. PECORA. Then the interests of depositors were being sacrificed to take care of the interests of the stockholders of the group?

Mr. PATTERSON. No.

Mr. PECORA. Is not that so?

Mr. PATTERSON. No.

Mr. PECORA. Does not that necessarily follow from the answer you have given?

Mr. PATTERSON. No; I believe not.

Mr. PECORA. Have you not said in words here or in substance, just now, that you justify the declaration of the dividend because of the necessity for taking care of the group?

Mr. PATTERSON. The declaration of a dividend by the Guardian National Bank of Commerce would come out of the profit account of that bank, and the assets were to take care of the depositors' interests, and they have, pretty largely, so far.

Mr. PECORA. Are not the depositors' interests supposed to be protected also by the capital funds of the bank?

Mr. PATTERSON. That is true; but $150,000 would not——

Mr. PECORA. Would not pay them in full, of course. We know that.

Mr. PATTERSON. Would not jeopardize the depositors' interests.

Mr. PECORA. It would to that extent, would it not?

Mr. PATTERSON. Yes.

Mr. PECORA. It would jeopardize them to the amount of dollars and cents involved in the dividend.

Mr. PATTERSON. That is right.

Mr. PECORA. Do you think, under those circumstances, that the officers did their full duty to the depositors in declaring that dividend, with the bank in that condition?

Mr. PATTERSON. Viewing it strictly as a bank operation, you are right.

Mr. PECORA. Do you know why the dividend was declared by the bank?

Mr. PATTERSON. Only, as I said before, it was used to pay some of the current indebtedness of the Group Corporation.

Mr. PECORA. What interest did the depositors of the bank have in taking care of the Group Corporation?

Mr. PATTERSON. Well, the Group Corporation was the stockholder of bank stock, and, I believe, had a right to declare earnings out of that bank.

Mr. PECORA. Even though the earnings of the bank itself, considering the bank as a separate entity, were not sufficient to make the declaration of a dividend advisable?

Mr. PATTERSON. I do not believe there was any legal objection to declaring dividends, even though the profit account is used or some of the surplus.

Mr. Pecora. I am not talking about a legal objection; I am talking about the practical consideration of principles of sound banking.

Mr. Patterson. As a practical consideration it was wrong.

Mr. Pecora. It was wrong?

Mr. Patterson. Yes, sir.

Mr. Pecora. Do you know at whose instance this wrong thing was done?

Mr. Patterson. No, sir; I do not.

Mr. Pecora. Can't you guess?

Mr. Patterson. I suppose it was the directors of the bank who declared the dividend.

Mr. Pecora. Do you think the directors of the bank did it upon their own initiative, or do you think they acted in response to a suggestion, if you please, from the group?

Mr. Patterson. I don't know, sir.

Mr. Pecora. Do you know anybody that would know that?

Mr. Patterson. I presume Mr. Lord could tell you.

Mr. Pecora. Mr. Lord told us, when he was on the stand that suggestions only were made to the unit banks by the group on the subject of declaration of dividends. You heard that testimony, did you not, week before last?

Mr. Patterson. Yes, sir.

Mr. Pecora. Didn't it appear to you that those suggestions were regarded as commands?

Mr. Patterson. Oh, no, sir; not at all.

Mr. Pecora. They were not regarded as commands by those officers of the bank who, when they first received the suggestion, reported back that the earnings of their bank did not justify the declaration of the dividend suggested by the group?

Mr. Patterson. No, sir; and I can positively state that so far as any apparent domination is concerned, that did not exist in my experience with the Guardian Group.

Mr. Pecora. And you say that, despite the documentary as well as oral evidence that was introduced week before last before this committee?

Mr. Patterson. I am speaking in a perfectly practical manner, now, about day-to-day operations; and any suggestion——

Mr. Pecora. I am not talking about day-to-day operations; I am talking about operations based upon general policy.

Mr. Patterson. I do not believe there was any domination by the group officers of any of the units.

Mr. Pecora. Was it customary when you were chief national bank examiner for you to notify a bank that it was to be examined and the date when the examination would commence?

Mr. Patterson. No, sir.

Mr. Pecora. As a matter of fact, do you know whether or not any of the officers, either of the group or of the unit banks of the group, received at any time any information concerning the time of the examination of any one of those banks or that an examination was to be made by the national bank examiners?

Mr. Patterson. Yes; I know of one instance.

Mr. Pecora. When was that instance?

Mr. Patterson. I believe it was Examiner Walker's examination of the Guardian Bank in May of 1932, when he and one of his assistants came to me and made preliminary arrangements to conduct an examination. The bank was quite a large one, Mr. Pecora——

Mr. Pecora. Which bank are you referring to?

Mr. Patterson. The Guardian National Bank of Commerce, of Detroit, Mich. The bank had 28 branches, and part of its operations were conducted in what we call the Union Guardian Trust Building, and a part of its operations were conducted in the Penobscot Building. It was his first examination of the bank, and he came to see me to learn what the physical layout of the institution was, to determine where the branches were located, where the loans and discounts were handled, and with regard to the large office in the Boulevard District, in the General Motors Building.

Mr. Pecora. Is that the only instance that you recall?

Mr. Patterson. I do not remember any other. I believe we participated with the national bank examiners—I am referring now to the examiners of the Group corporation—I believe we participated with the national bank examiners in an examination of the Grand Rapids National Bank at one time.

Mr. Pecora. Under what circumstances was that done?

Mr. Patterson. After the national bank examiners had taken charge of the bank for examination we were notified and sent men over there to participate with them rather than to discommode the bank with two examinations.

Mr. Pecora. Do you recall receiving a letter dated December 17, 1931, from Mr. Leyburn, then chief national bank examiner, a photostatic copy of which I now show you?

Mr. Patterson. Yes; I recall this letter.

Mr. Pecora. That was another instance, was it not, where you received notice in advance that an examination was going to be made of the bank on a certain date?

Mr. Patterson. Yes, apparently; although it does not state that an examination is to be made.

Mr. Pecora. What does it state? Suppose you read the letter, yourself, into the record while you have it before you.

Mr. Patterson. It is addressed to me. [Reading:]

> Hopkins will be in Detroit Saturday morning with Norsen and McLean to line the work up and start it off. He will have to be away Monday and then he will return and he will have some more help.

Mr. Pecora. What did you think these examiners were coming there for?

Mr. Patterson. I would think now it was for the purpose of some examination; but I do not just recall what this particular instance was.

Mr. Pecora. Will you look at this document which I now show you and which purports to be a photostatic reproduction of an intra-Group memorandum addressed by you to Messrs. Lord, Kanzler, Covington, and Walsh, under date of December 18, 1931, and tell me if you recognize it to be a correct copy of such a memorandum prepared and sent by you to the gentlemen to whom it is addressed?

Mr. Patterson. Yes; I recall it.

Mr. Pecora. I want to offer that memorandum in evidence.

The Chairman. Let it be admitted.

(Photostatic copy of memorandum dated Dec. 18, 1931, addressed by Mr. Patterson to Messrs. Lord, Kanzler, Covington, and

Walsh, was received in evidence, marked "Committee Exhibit No. 57, Jan. 3, 1934.")

Mr. PECORA. The memorandum in question that has just been received in evidence as Committee Exhibit No. 57 is on the letterhead of the Guardian Detroit Union Group, Inc., an Intra-Group memorandum to Messrs. Lord, Kanzler, Covington, and Walsh from B. K. Patterson, dated December 18, 1931, and reading as follows [reading]:

> You are advised that the chief national bank examiner informs me, under date of December 17, that National Bank Examiner Hopkins and two assistants will be in Detroit Saturday a.m., December 19, for the purpose of beginning the work of the examination of the Guardian Detroit Bank. Mr. Hopkins cannot be here on Monday, December 21, but will leave his assistants here to continue the work of examination, and Mr. Hopkins is to return on Tuesday to finish the job.

What were you going to say about it?

Mr. PATTERSON. I was going to say this, that arrangements had been made for a consolidation of the National Bank of Commerce and the Guardian Detroit Bank, the latter being a State bank, and we had made arrangements with the Comptroller's office and had requested, in fact, that an examination of the Guardian Detroit Bank be made, and I had contacted Mr. Leyburn to ascertain when the examiner and his crew of men would be over to the State bank, the Guardian Detroit Bank, for that purpose. We had ordered the examination ourselves incident to the consolidation of the two banks.

The CHAIRMAN. Which bank was it that you said had 28 branches?

Mr. PATTERSON. The National Bank of Commerce.

The CHAIRMAN. They were all in Detroit?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. Did you know with reference to the dividend that was declared for the last quarter of 1932 by the Guardian National Bank of Commerce that in his report on the bank as of November 9, 1932, the national bank examiner said, in answer to the question, "State reason, if any, why bank should not declare a dividend at the end of current dividend period", as follows:

> Statutory bad debts, doubtful assets and bond depreciation prohibit.

Did you know that?

Mr. PATTERSON. No, sir; I have never seen that report, Mr. Pecora.

Mr. PECORA. Let me read to you from the report of the National Bank Examiner as of November 9, 1932, on the condition of the Guardian National Bank of Commerce, as follows: [reading]:

> At the present time a cooperative spirit toward the Department is evident throughout this bank and their credit department and loan information is far above the average. Also asset values are frankly discussed with the Department's representatives. This same spirit is not reflected in the Group by President Lord. It is believed that Vice President Covington of the bank should be given full credit for the attitude in the bank, the improved condition of its loans, and its very material improvement in its liquidity which is now 40.5 or better on an average. However, in considering its liquidity full consideration should be given to the vulnerable position of the bank as reflected in the attached list. The real-estate situation in the bank is serious, and at the present time it is very difficult to determine values of any Detroit property. It is felt that eventually substantial losses will develop in some of these assets. The concentration in collateral of Guardian Detroit Union Group and Detroit Bankers Co. stocks is outrageous, and little if any value is given to either of these stocks by the examiner. Some time ago the Detroit banks took over the American State Bank to avert closing, and proportionately guaranteed the First National Bank, the absorbing

bank, against loss. This bank's share is 18 percent. The reserve fund upon the books of the bank has unquestionably lost $1,600,000, and an arbitrary default classification of an additional $1,500,000 is estimated at this examination, although even this figure is believed to be a generous classification.

Much depends in this institution on how much confidence the public will continue to place in the connection of Edsel Ford and C. S. Mott with this bank and whether they will continue to assist. This will depend upon the trend of business at the present time.

Under the caption of "General Remarks" let me read the following from this report as of November 9, 1932 [reading]:

The condition of this bank is very unsatisfactory, and the stock ownership by the Guardian Detroit Union Group adds nothing to strengthen the picture. The Group has heavy debts of its own, approximately $14,000,000, and it is necessary for them to find ways and means to liquidate some of their own debts and have no funds nor assets with which to assist the member banks. The Group assets consist almost entirely of bank stocks which are not productive of dividends. It was frankly stated that the Group were very much interested in national legislation in hopes that state-wide branch banking will be legalized and in that way rearrange their capital structure in such a way as to provide substantially for elimination of losses in their member banks. Just how far its capital structure will go toward the accomplishment of this end is a problem, but it should only be permitted to be done under the direct supervision of the Department. The losses of this bank as estimated at this examination are nominal as compared with the very questionable assets that it was desired to eliminate, and it was felt that in view of impending legislation it would be the most desirable thing from the Department's viewpoint to postpone such classification until some future time when the possibility of using a portion of the Group's capital structure can be determined.

Under the circumstances reflected by this report, do you think the declaration of a dividend for the final quarter of 1932 by this bank was advisable or justifiable?

Mr. PATTERSON. No, sir.

Mr. PECORA. In the light of the condition of the bank as disclosed by these reports of the national bank examiners throughout the year 1931 and the year 1932, do you agree with the opinion expressed here by Mr. Lord before this committee week before last, that this bank should not have been closed when it was closed, in February 1933?

Mr. PATTERSON. Yes, sir; I do.

Mr. PECORA. You do?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. Do you disagree with the report of the national bank examiners that I have read to you this afternoon?

Mr. PATTERSON. I think that their classifications were pretty drastic at that time, throughout 1931 and 1932.

The CHAIRMAN. What do you mean by "classifications"?

Mr. PATTERSON. I mean the classification of its assets, as to slow and doubtful, or loss. I think that that is borne out pretty much by what has happened since the bank has been in the hands of a receiver, and what is very likely to happen in the final liquidation of the bank.

The CHAIRMAN. In other words, you think the bank was solvent when it was closed?

Mr. PATTERSON. I think it was; yes, sir.

Mr. PECORA. And that despite the fact that doubtful loans, the item of doubtful loans alone, as of November 9, 1932, exceeded in amount the entire capital funds of the bank?

Mr. PATTERSON. That classification was made at the very lowest point in all price history, almost, of this country; and in addition to that I still say that the classifications were quite drastic. I think that bank could have been saved.

Mr. PECORA. What report had your own examiners made to you for the year 1932 concerning this bank?

Mr. PATTERSON. We had not been able to get into the bank in the year 1932 with our own examiners.

Mr. PECORA. Why not?

Mr. PATTERSON. Because in the spring of that year, in March, it became necessary to economize more and more in the Group Corporation, and all the examiners attached to the Group Corporation were assigned to other duties, and practically no examination work was done during that year by the Group Corporation.

Mr. PECORA. This bank was one of the most important units in the group, was it not?

Mr. PATTERSON. That is true.

Mr. PECORA. Why were you not able to obtain a report from your own examiners of the condition of the bank for the entire year 1932?

Mr. PATTERSON. I just said, Mr. Pecora, that in the interests of economy we had detached all the examiners from the Group Corporation and assigned them to other duties, and all examination work on the part of the group was discontinued approximately the 1st of March 1932.

Mr. PECORA. Then how were you informed as to the condition of the bank in 1932?

Mr. PATTERSON. Only by contact with the officers of the bank.

Mr. PECORA. That contact, or that information, did not consist of any information you got from any of the national bank reports for that year, because you have acknowledged this afternoon that you are learning of the contents of these reports for the first time this afternoon.

Mr. PATTERSON. Yes.

Mr. PECORA. It did not consist, either, of any information you got from examinations made by your own men, did it?

Mr. PATTERSON. No, sir.

The CHAIRMAN. In other words, you had not made any classifications of your own?

Mr. PATTERSON. No, sir.

The CHAIRMAN. You were not in a position to criticize?

Mr. PATTERSON. We had not made any examinations during 1932.

Mr. PECORA. Was not that the time when, in view of existing conditions, it seemed most imperative to you that such examinations be made?

Mr. PATTERSON. Yes, sir.

Mr. PECORA. And in the interests of economy those examinations were not made?

Mr. PATTERSON. Apparently.

Mr. PECORA. Well, actually?

Mr. PATTERSON. Actually; yes, sir.

Mr. PECORA. Mr. Chairman, that completes this phase of the examination.

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But, Mr. Chairman, I think this letter, which was read, in part at least, into the record by Mr. Patterson, should be marked as an exhibit.

The CHAIRMAN. Let it be appropriately marked.

(Thereupon the letter dated Jan. 10, 1929, from Mr. Proctor to National Bank Examiner Moon, was marked "Committee Exhibit No. 58," and will be found at the end of the day's proceedings.)

The CHAIRMAN. The committee stands adjourned until 10 o'clock tomorrow morning.

Mr. PECORA. Witnesses now in attendance will be here at that time.

(Whereupon, at 4:30 p.m. Wednesday, Jan. 3, 1934, an adjournment was taken until tomorrow, Thursday, Jan. 4, 1934, at 10:30 a.m.)

COMMITTEE EXHIBIT NO. 58 JANUARY 3, 1934

TREASURY DEPARTMENT,
January 10, 1929.

MR. EARL W. MOON,
National Bank Examiner,
164 West Jackson Blv'd., Room 1203, Chicago, Illinois.

DEAR SIR: Your letter of January 4, is received, requesting an answer to your letter of December 19.

You state that the officers, directors, and stockholders interested in the Union Trust Company, the Griswold-First State Bank, and the National Bank of Commerce, all of Detroit, Michigan, have organized a corporation known as the Union Commerce Investment Company; that this corporation is in reality a holding company for the stock of these three institutions; that the assets of the Union Commerce Investment Company consist of the total capital stock of these three institutions except the directors' qualifying shares, and request to be advised whether the National Bank of Commerce may lawfully, and without criticism, hold stock of the Union Commerce Investment Company as collateral to loans.

The stock of the corporation referred to is not capital stock of the bank within the meaning of Section 5201, U. S. R. S., even though a part of its assets consist of stock of the bank. The matter of accepting stock of the company as collateral to a loan is one for the determination of the management of the bank, although this office does not look with favor on loans secured by stock of a company so closely allied to the bank and having little or no assets other than stock in banks, national and state.

Your letter of December 19 was inadvertently placed in the files before being answered.

Respectfully,

JOHN S. PROCTOR,
Deputy Comptroller.