



THE COMPTROLLER OF THE CURRENCY
WASHINGTON

November 16, 1939

Honorable Marriner S. Eccles,
Chairman, Board of Governors,
Federal Reserve System,
Washington, D.C.

My dear Mr. Eccles:

Pursuant to your request, there is
transmitted to you herewith a copy of our letter
of July 31, 1939 to the Bank of America.

Very sincerely yours,


Preston Delano



TREASURY DEPARTMENT
COMPTROLLER OF THE CURRENCY

WASHINGTON

ADDRESS REPLY TO
"COMPTROLLER OF THE CURRENCY"

July 31, 1939

Board of Directors,
Bank of America N.T. & S.A.,
San Francisco, California.

Gentlemen:

The current report of examination of your bank, completed July 21, 1939, a copy of which has been sent to you, shows a continuation of the unsatisfactory asset condition which has been the subject of previous communications to you and of discussions with the managing officers of your institution. We shall review in this letter some of the more important phases of the bank's problems, and point out the corrections which must be made if the Bank of America N.T. & S.A. is to be operated soundly and the interests of depositors protected.

The present examination shows that, after deducting estimated losses of \$13,517,598.69, liability on account of service charges of \$619,760.29, and one-half of Classification III, which aggregates \$14,535,225.14, from the total capital structure as shown by your books, there remains \$93,207,348.57 of adjusted capital structure, or approximately \$9,000,000 less than was shown in the prior report.

Previous letters from this office have outlined the wholly unsatisfactory capital and asset condition of your bank. This two-fold weakness is manifestly attributable to such unsafe and unsound policies as (a) refusal of management and directorate to recognize asset problems in general, (b) refusal to recognize the dangers inherent in the excessive concentration in real estate, (c) use of earnings for the payment of dividends rather than for the

*Copy of this furnished Gov. M. W. Lee direct
by Comptroller about Nov. 16th.*

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creation of adequate reserves and the correction of the asset condition and the under-capitalization, (d) persistent unsound and illegal dealings with Transamerica Corporation and allied interests to the detriment of the bank and in other than conventional and accepted methods employed in dealings with other clients of the bank, and (e) refusal to make and keep the bank independent of, rather than subservient to, the interests and expansion policies of Transamerica Corporation.

The concentration of fixed assets, consisting of banking houses, furniture and fixtures and other real estate, exceeds the capital and surplus of the bank, and in fact exceeds the adjusted capital structure mentioned above. On Page 14, insert 1 of the report of examination, there is a schedule showing the total carrying value of fixed assets, which includes the contracts of California Lands, Inc., and Capital Company, since in effect the only collateral pledged as security for these contracts is the real estate covered by them. The amount properly representing banking houses and furniture and fixtures totals \$48,234,851.52, and the amount invested in other real estate is shown to be \$45,766,704.89. The combined total of these accounts is \$94,001,556.41. In addition, there are 346 loans amounting to \$6,032,175.00 which are under foreclosure, and additional loans aggregating \$7,621,226.49 which are believed by the examiner to be potential foreclosures. This brings the total investment in actual and potential fixed assets to \$107,654,957.90, which sum is greatly in excess of the adjusted capital structure. It is to be noted that \$27,387,220.00 book value of other real estate, comprising approximately 1,000 parcels, has been carried beyond five years.

The contracts of California Lands, Inc., and Capital Company, mentioned in the preceding paragraph, aggregate \$33,834,723.80. Notwithstanding your assurance that no more real estate would be transferred to these companies, the examiner reports that you have made a direct advance to the Capital Company in the amount of \$1,100,000, which was used for the construction of a building for a large department store in Los Angeles, and that you have added that sum to the

unpaid balance of the real estate contracts. Such action on your part not only constitutes an unsafe and unsound banking practice but, in the opinion of this office, is a violation of section 24 of the Federal Reserve Act, as amended. Immediate steps must be taken to remove this obligation from the assets of the bank for cash.

The real estate illegally acquired on August 5, 1938 in the amount of \$89,456 (shown in the report as \$85,405) in a transaction designated as the Hellman deal, must be removed from the assets of the bank for cash. You will recall that when these properties were reacquired, a credit of like amount was entered on "Guaranteed Loans."

As you have been previously advised, the illegal real estate loan of Western Furniture Exchange, Inc., in the amount of \$520,000 should be removed from the assets of the bank for cash. That loan was taken from Transamerica Corporation in exchange for 11,320 shares of National City Bank stock carried in the bonds and securities account under "Option to Purchase." The property securing the loan is subject to prior encumbrance of \$1,000,000 in favor of the Metropolitan Life Insurance Company. This loan, with a maturity of approximately fifteen years, represents an illegal investment under section 24 of the Federal Reserve Act, as amended.

Your particular attention is directed to the concentrations of credit to Transamerica Corporation and its affiliates in amount of \$76,684,859.96; to A. O. Stewart in amount of \$7,623,239.31, and extensions under German Credits of \$5,009,239.82, which aggregate \$89,317,339.09, or almost the entire capital and surplus of your bank. The large extension of credit to Transamerica Corporation (which includes the contracts of California Lands, Inc., and Capital Company) is entirely out of proportion to your capital structure and presents one of the most serious problems confronting you. Although this matter has been repeatedly brought to your attention both in reports of

examination and correspondence from this office, you have appeared little disposed to reduce these borrowings through earnings or to have the corporation reduce them by the sale of assets. From the character of the major portion of the collateral pledged as security to this concentration it is apparent that such action will be necessary to bring this line within conservative limitations, and you are directed to take the necessary action to bring this about. Failure to do so constitutes an unsafe and unsound banking practice.

The A. O. Stewart line of \$7,623,239.31 has also been subject to criticism over a long period of time and \$3,618,000 has been classified II in this report. One of the loans in this large line amounting to \$1,946,126.94 is adequately secured by United States Treasury bonds but the other collateral consists chiefly of defaulted bonds and stocks with no ready market or of corporations in liquidation. Prompt steps must be taken looking toward the curtailment of this line, or the pledging of satisfactory collateral back of the line.

Notwithstanding the large and dangerous concentration in real estate, the large and unwarranted obligations of Transamerica and affiliates, and in spite of the fact that the dividend policy has been criticised continuously since resumption of dividend payments in 1933, you have steadily increased that dividend rate until it has reached the annual total of 19.2%. As an illustration of your unsound policies it is noted that during the year 1938 the bank's earnings, after deducting the losses which you charged off, and exclusive of profits realized on the sale of bonds and securities, were \$5,389,975.00, and during that year \$9,600,000.00 was paid out in dividends. Numerous large transactions have been had with Transamerica and affiliates designed to avoid taking known losses and thus to give color of validity to the distribution of earnings by means of dividends to Transamerica and other shareholders. A net profit of \$6,570,000.00 was realized from the sale of securities from September 1, 1938 to March 31, 1939, which was credited to undivided profits. It is the position of

this office that until losses have been written off and adequate reserves established, none of such profits should be distributed to shareholders through dividend payments.

The report indicates that your bank carries its own Fidelity Insurance for the first \$100,000.00 and that premiums which ordinarily would be paid to an insurance company are deposited with Transamerica General Corporation. The amount of such deposit is \$2,272,659.55 and actually represents reserve funds of the bank that are not shown on the books. You are requested immediately to return this deposit to the bank in cash and to set up the proper account on your books. Failure to do so constitutes an unsafe and unsound banking practice.

Violations of law and regulations as shown by the report of examination (page 2) include the non-observance of the provisions of Section 5201, U.S.R.S., by granting loans based on the security of shares of the bank's own stock; of Section 5136, U.S.R.S., by the purchase by the bank for its own account of investment securities which do not conform to the law and regulations; of Section 5137, U.S.R.S., by virtue of certain real estate transactions as cited in the report of examination; and of Section 24 of the Federal Reserve Act in the making and purchasing of certain real estate loans. In addition to the foregoing your attention is again called to the fact that the obligations of Transamerica Corporation and its subsidiaries, in which the Corporation owns or controls a majority interest, amounting to \$23,045,819.58 exceeds the 10% loaning limit of the bank under the provisions of Section 5200, U.S.R.S., and is in violation of the provisions of Section 23A of the Federal Reserve Act which limits loans to holding company affiliates.

It is the Comptroller's duty to insist upon the correction of practices or conditions which violate established sound banking principles. Therefore, it is deemed fair and appropriate to advise you that it is the purpose of this office carefully to scrutinize;

1. All transactions and practices which have resulted or which may result in weakening the capital structure whether by way of unjustified dividends, or the improvident use of the credit facilities of the bank by contributions to, or the forgiveness of obligations of, allied or special interests.
2. The substance and not merely the form of all methods employed in the various and complicated transactions engaged in by your institution.

Furthermore, this office must insist that the bank conserve its earnings and establish an adequate sound capital position, that it refrain from unjustifiable favoritism to allied interests, that it correct the weaknesses and remove the bases of criticisms, that it take appropriate steps to eliminate the undue concentration in real estate including any portion thereof which may have been camouflaged through the use of allied corporations, and that appropriate policies and practices be established and followed to insure a constant sound condition for the bank.

If it has not been done prior to the receipt of this letter, the amount classified as loss by the examiner should be charged off promptly, and certainly not later than the day following the next meeting of your Board. You are advised that until these losses have been written off and adequate reserves established, any further declaration or payment of dividends to shareholders will constitute an unsafe and unsound banking practice.

Each director and officer of the bank is hereby warned, pursuant to the provisions of Section 30 of the Banking Act of 1933, 48 Stat. 193 (U.S.C. title 12, section 77), to discontinue each and all of the unsafe or unsound practices referred to in this letter or which have been disclosed by the reports of examination, and to make provision for the elimination and discontinuance of the violations of law referred to in this letter or in the reports of examination.

Very truly yours,



Comptroller of the Currency