

Chairman Eccles:

Following our telephone conversation,  
I have sent the attached memorandum on to  
Messrs. Leonard and Smead.

W.T.

BOARD OF GOVERNORS  
OF THE  
FEDERAL RESERVE SYSTEM

# Office Correspondence

Date March 12, 1947

To Mr. Smead and Mr. Leonard

Subject: Bank Profits

From Woodlief Thomas

The Chairman is much interested in the development of bank profits, particularly in view of their bearing upon the interest-rate problem. If bank profits decline in the next few years, as seems likely, banks will be under more pressure than in the past to shift from short-term securities into longer-term securities and into loans that will give them a higher rate of return.

Preliminary figures obtained as to earnings in 1946 show that, although earnings from current operations were larger than in 1945, net profits after allowance for recoveries, charge-offs, etc., and taxes were smaller in 1946 than in 1945. This would suggest that banks may have set up a large amount of charge-offs of various sorts on their books, some of which are not deductible for tax purposes, or made larger allowances for tax accruals than they will need.

In order to have a correct appraisal of the bank earnings situation, it is desirable to be able to explain these charge-offs. They may be completely justified on the basis of the larger volume of bonds bought at premiums or on the basis of the increase in loans. There is a question, however, as to whether banks should include in their earnings and expense reports submitted to the banking authorities charge-offs and the like which are not allowable for tax purposes.

The following actions are proposed for consideration:

1. Make as thorough an analysis as possible of the reported figures on the earnings reports and publish as much explanation as we can regarding these developments.
2. Have examiners, in connection with their next quarterly report of developments, comment with respect to whatever information they are able to obtain regarding the charge-offs, etc.
3. In cooperation with other supervisory authorities, consider whether banks should be required to prepare their earnings reports on the same basis as their income tax reports. This is a matter that can be put on the agenda for discussion at a contemplated meeting of the supervisory authorities which Under Secretary Wiggins has indicated to the Chairman he will call soon.

M. J.