

June 1, 1950

Board of Governors

Messrs. Millard and Vest

Proposed certification by
Comptroller of the Currency with a view
to removal of national bank directors.

STRICTLY CONFIDENTIAL

In accordance with the instructions of the Board at the meeting on May 19, representatives of the Board's staff met with staff representatives of the Comptroller of the Currency and the FDIC to discuss further the proposed certification by the Comptroller to the Board with a view to the removal of the directors of the Continental National Bank and Trust Company, Salt Lake City, Utah, under section 30 of the Banking Act of 1933. Mr. Slade, Vice President of the Federal Reserve Bank of San Francisco, attended the meeting. Mr. Jennings and Mr. Anderson represented the Comptroller's Office, and Mr. Shearer and Mr. Aycock represented the FDIC.

We pointed out that action by the Board in a case of this kind would be reviewable by the courts; that the failure of the bank to increase its capital, being negative in character and a matter for stockholders' action, would hardly be a proper basis for a section 30 proceeding; that the overexpansion of loans in relation to capital is a relative matter and is actually tied in with the amount of the bank's capital; that despite the substandard quality of many of the bank's loans, the losses of the bank have not been abnormal and the total amount of paper classified doubtful and loss in the most recent examination report is relatively small; that the most recent examination report contains some statements of the examiner indicating some little improvement and other somewhat complimentary language on his part; that even if the proceeding were successful, there would seem to be nothing to prevent the stockholders from electing other directors to carry out the policies desired. Mr. Slade also stated his views, which in general were in accord with those of the Board's representatives.

The matter was thoroughly discussed. The Comptroller's representatives took the position that the bank was one of the worst, if not the worst, national bank in the United States from the standpoint of ratio of capital to risk assets and that something should be done to correct the situation. They felt that a section 30 proceeding for the removal of directors offered the only practicable solution and that this was much preferable to a proceeding by the FDIC to terminate the bank's insurance, for the latter would necessarily force the bank to liquidate as a national bank. They argued that the question whether the bank was engaged in unsafe or unsound banking practices was a matter of expert opinion and that if the Board, after hearing and on the basis of the certification by the Comptroller, found that it was so engaged, the courts probably would not overrule the Board. Even if the Board should lose the case, they felt that the supervisory authorities would then be in a good position to go to Congress and ask for appropriate amendatory legislation.

The FDIC representatives felt that the situation was definitely a bad one and that something should be done about it. They did not commit themselves definitely, however, on whether or not the Board would have a good case in undertaking to remove the directors of the bank because of its failure to increase its capital or because of its persistent liberal loan policy in relation to capital. They said that they had brought a number of proceedings against banks for the termination of insurance in which factors of this kind were alleged, but in all of these cases there had also been other factors which gave other legal grounds for action. None of these proceedings had been considered by the courts. When asked whether the FDIC would proceed against this bank for the termination of insurance in the event the Board did not act in the matter, the FDIC representatives indicated that they had not fully considered the matter and that they were not prepared to give a definite answer to the question at this time. They referred to the fact, however, that Mr. Harl had advised Deputy Comptroller Robertson that, if the section 30 proceeding did not go through, to let him know and he would then consider termination proceedings by the FDIC.

The Continental National Bank and Trust Company is one of a group of nine banks in which the Cosgriffs have substantial ownership or control. Three are national banks, one a State member bank, and of the others four are nonmember insured and one nonmember uninsured. Nearly all of these banks have low capital ratios and some of them are in approximately the same situation in this respect as the Continental National. For this reason the Board's representatives suggested several times the desirability of making a simultaneous examination of all of these banks in order to get as full and complete information as possible with respect to all matters, and particularly with respect to such matters as the possible switching of loans among the institutions, before anything else is done. We also suggested the desirability of sitting down with Mr. Cosgriff and trying to work out some arrangement under which the bank might obtain more capital, as for example by the sale of its building and the use of the proceeds to increase the capital of the bank. Mr. Slade particularly had indicated that such a conference with Mr. Cosgriff might possibly be productive of some good results and would do no harm particularly if representatives of all three agencies participated.

Mr. Jennings of the Comptroller's Office, said that, subject to checking with the Comptroller, he felt that they would be agreeable to a simultaneous examination but would not be agreeable to permitting such an examination to delay the certification by the Comptroller to the Board. He also indicated that he thought they would invite Mr. Cosgriff to come to Washington to discuss the matter before making the certification, but that they would not be willing to have any representative of the Comptroller go to Salt Lake City or to San Francisco to discuss the matter with Mr. Cosgriff.

It is our view that it would be desirable for the Board to authorize us to advise the Comptroller's representatives substantially as follows: In view of the fact that practically all of the Cosgriff banks are in a relatively weak capital position and the unsound practices, if any, probably would apply to all, the Board feels that a simultaneous examination is desirable and would be glad to arrange with the Federal Reserve Bank to participate in such an examination so far as the State member bank is concerned; that since the purpose of the examination would be to develop what information there might be that would have a bearing upon a determination as to whether there should be a section 30 proceeding, any further steps toward such a proceeding should be deferred until the results of such an examination could be considered; that at some appropriate time, probably after such an examination, one representative each from the Comptroller's Office, the FDIC and the Federal Reserve Bank should sit down with Mr. Cosgriff and discuss the matter fully with him, with the hope to obtaining some additional capital or change in loaning policies; and that such a conference would have more chance of being productive if held in San Francisco or Salt Lake City. This would contemplate that we would not voluntarily say to the Comptroller whether or not the Board would proceed with a section 30 proceeding if the Comptroller made the certification, but if pressed, that the Board's representatives would say that the Board hoped that the Comptroller would not make the certification at this time and, if he insists on doing so, the Board's present feeling is that it would not be advisable for it to undertake such a proceeding.

July 7, 1950.

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Proposed certification by the Comptroller of the Currency with a view to removal of directors of the Continental National Bank & Trust Company, Salt Lake City, Utah.

Geo. S. Sloan

CONFIDENTIAL

Assistant Chief National Bank Examiner Jennings called the writer by telephone this morning to state that Mr. Walter Cosgriff, President and (with his family) controlling stockholder of the Continental National Bank and Trust Company of Salt Lake City, had conferred in Washington with the Office of the Comptroller of the Currency on Friday and Monday (presumably June 30 and July 3).

As a result of this conference Mr. Cosgriff tentatively agreed to reduce the total of the loans of the subject bank from \$21,000,000, as shown by the report of examination as of February 28, 1950, to approximately \$17,000,000. Such reduction was to be accomplished within 6 to 9 months and was to be a bona fide reduction made in loans of borderline or distinctly risk character. Capital of the bank was also to be increased \$250,000 through the injection of new funds. The agreement was to be confirmed by Mr. Cosgriff after his return to Salt Lake City and consultation with his associates.

If confirmed, as confidently expected, Mr. Jennings said the Comptroller's Office did not intend to proceed further with its proposal to cite the directors of the bank under Section 30.

Mr. Jennings said that consideration had been given to the fact that the bank had \$4,250,000 in NHA Title 1 loans which were further insured by private coverage to provide total coverage of 40 per cent and, therefore, appeared to represent little, if any, risk. Also, the actual value of the banking house, which appears to exceed carrying value by \$800,000, was noted. If the proposed action is taken, the risk asset ratio of the bank will be about 13 per cent. (It was 8.2 per cent.)

In view of the possibility that all or part of the proposed reduction in loans might be effected through transfer to other banks of the Cosgriff chain, he felt that the proposed simultaneous examination of all banks in the group should be carried out but said that, in the circumstances, the Comptroller would not wish to enter the national banks involved before September. The writer suggested that it might be preferable to defer simultaneous action until the six to nine months period allowed for effecting the reduction in loans had elapsed. Mr. Jennings agreed but said the matter should be determined after confirmation of the tentative agreement had been received from Mr. Cosgriff.

We are to be advised when the agreement has been confirmed and Mr. Jennings suggested that advices to the Federal Reserve Bank of San Francisco be deferred until that time.

July 31, 1950.

Mr. H. F. Slade, Vice President,
Federal Reserve Bank of San Francisco,
San Francisco 20, California.

Dear Mr. Slade:

Your letter of July 28 addressed to Mr. Millard was received this morning. He is not expected to return until August 7.

You are correct in your understanding that Mr. Cosgriff reached an agreement with the Comptroller's Office with regard to the provision of additional capital and other action to be taken and we were advised informally that the Comptroller would not proceed, for the present at least, with his proposal to issue a citation under Section 30. When reported, however, the agreement was tentative and was to have been confirmed by letter after Mr. Cosgriff had talked with his associates. At that time it was agreed that the capital of the Salt Lake bank would be increased \$250,000 through the injection of new funds and total loans of the bank would be reduced about \$4,000,000 within 6 to 9 months. The reduction was to be made in loans of border line or distinctly risk character.

Chief National Bank Examiner Folger advised us today that the letter of confirmation had not been received but he understood that Mr. Cosgriff was still in the East and had not returned to Salt Lake City since his discussion at the Comptroller's Office. You would have heard from us earlier had we not thought it best to await confirmation and give you the exact terms of the agreement as soon as they could be ascertained.

Everyone seems to feel that simultaneous examination of the banks in the chain would be most desirable but, in view of the agreement with the Comptroller, we have suggested that such action might be taken after the time for compliance with the terms of the agreement had expired. This would permit determination of the extent of compliance and whether it had or had not been accomplished through transfer of assets to other banks in the chain. Vance Sailor of the FDIC apparently feels that simultaneous examinations should be made this fall.

At present the whole matter seems to be up in the air. It is good to note that you do not have examination of the Boise bank scheduled for the near future and we will give you definite advices as soon as possible. If your time for entry at Boise should near before you receive further advice from us, please call the matter to our attention.

Very truly yours,

Geo. S. Sloan
Assistant Director,
Division of Examinations.

August 16, 1950.

Mr. Millard
Geo. S. Sloan

Walter E. Cosgriff and other
directors of the Continental National
Bank and Trust Company, Salt Lake City,
Utah.

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On May 19, 1950, Mr. Vest reported to the Board that representatives of the Office of the Comptroller of the Currency had advised the Board's staff that the Comptroller was prepared to make a certification to the Board as a basis for proceedings for the removal of all of the directors of the Continental National Bank and Trust Company, Salt Lake City, Utah, under Section 30 of the Banking Act of 1933. The Board had no previous knowledge of the matter although a warning pursuant to Section 30 had been sent to the board of directors of the bank by the Comptroller on December 1, 1949.

The letter of warning stated that District Chief National Bank Examiner Wright had been requested to discuss with Mr. Cosgriff the unsatisfactory condition of the bank from the standpoint of its excessive loan volume and the heavy amount of its current loan problems in relation to its inadequate capital structure, the various reasons why additional capital was essential and to request that action be taken to raise the needed capital. Mr. Wright had reported his meeting with Mr. Cosgriff on October 25, 1949, and that Mr. Cosgriff stated, among other things, he had no intention of complying with the request that (1) the capital structure of the bank be strengthened through the sale of new stock, and (2) efforts be directed toward a more conservative lending policy.

The following data were submitted to set forth the bank's "steadily worsening capital position due to loan volume growth which has far outstripped capital structure growth from retained earnings":

(Figures in thousands)

Date of Examination	Deposits	Loans	Classified and Special Mentioned Loans	Adjusted Capital Structure	Ratio	
					Capital to Deposits	Capital to Risk Assets
5- 5-44	\$24,582	\$3,694	\$196	\$1,301	1-19	1- 5.93
11-14-44	30,822	5,100	488	1,342	1-23	1- 7.14
6-12-45	29,944	4,523	547	1,388	1-21	1- 6.59
12-28-45	34,709	5,952	543	1,447	1-24	1- 7.88
6-28-46	31,665	8,179	748	1,717	1-18	1- 7.86
12-17-46	35,674	11,729	1,096	1,739	1-20	1- 9.60
6- 9-47	32,190	15,528	940	1,936	1-16	1- 9.81
3- 1-48	35,348	17,334	2,064	1,884	1-19	1-10.16
8- 1-49	40,659	21,978	2,677	1,924	1-21	1-12.04

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The letter also stated:

"These two factors, namely, (1) a heavy general loan volume, and (2) a disproportionate volume of weak loans, in relation to your bank's capital structure are the main basis for our conclusions that additional capital is essential to provide your depositors with a reasonably protective margin of capital structure and that your loaning policies should be made more conservative.

"Subsidiary factors bearing on the conclusions expressed in the above paragraph are as follows:

1. \$5,551,800 of your bank's loans are to individuals and interests outside the State of Utah. While many of these loans undoubtedly are justified extensions of credit, we do consider that you have gone far afield to loan money, thereby increasing your loan supervision problems and the attendant degree of risk in a substantial portion of your loan portfolio.
2. \$1,762,000 of your bank's loans are to relatively small finance companies, are capital in nature, and would appear to be collectible only through transfer to other banks or substantial liquidation of the finance companies concerned. None of these loans appear in the classified or special mentioned loan schedules of the report.
3. Out of approximately \$3,000,000 of livestock loans, \$847,000 constitute potential problems.
4. \$951,000 of your bank's loans are not supported by current and satisfactory credit information.
5. \$1,310,850.12 of your bank's loans (5.96 per cent) were in a past due status at the time of the August 1, 1949, examination. This reflects adversely on the effectiveness of your supervision and on the quality of the loans involved.
6. Your bank's earnings are only fair, and your dividend policies, beginning with the year 1946, have been liberal. From January 1, 1944, to June 30, 1949, you have paid out \$540,000 in dividends and retained \$693,300 of earnings. Considering your bank's great need for additional capital this is not a good record. We are aware that improved earnings may be expected, if substantial loan losses do not accrue, but we do not consider that future retained earnings may be regarded as the answer to your bank's badly undercapitalized position.

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7. 43% of your bank's capital structure is invested in fixed assets. We recognize that your banking house may be worth well in excess of its book value, but the percentage of capital presently invested in fixed assets is high, and the possible excess value in the banking house can not soundly be regarded as an offset to your bank's under-capitalized position. The probable or potential excess value in a banking house is a sound capital value only when it has been realized upon. As you are well aware, when realization of such a value becomes a necessity, the results are usually disappointing.
8. Over a long period of time our examiners have consistently regarded your bank's loaning policies with grave reservations. Commencing with the year 1944, we find no instance in examination reports where our examiners have regarded your loaning policies as measuring up to acceptable standards. The fact that your loan losses have been small is, in our opinion, the result of a constantly expanding economy and not the outgrowth of sound loaning policies. We think far too many of your loans are strictly fair weather credits which would not stand up successfully under a moderate decline in economic conditions."

Another important extract from the letter is:

"...The only alternative to raising additional capital which will be acceptable to us is a very substantial reduction in loan volume coupled with more conservative loan policies."

The letter of warning (copy in Counsel's office) has been quoted at length as it is understood that the character of and basis for the Comptroller's complaint is of particular interest. The specific charge was:

"Specifically we charge that your loaning practices and policies which permitted a total loan volume of \$21,978,181.18 (on August 1, 1949) in relation to an adjusted capital structure of \$1,924,046.07 are unsafe and unsound. We charge that the existence of loan problems in the amount of \$2,677,900, as set forth in the Classified Loan and Other Loans Especially Mentioned schedules of the examination report dated August 1, 1949, is unsafe and unsound in relation to gross capital accounts and reserves of \$2,027,479.15. We request that this first warning to each of you under Section 30 of the Banking Act of 1933 be heeded and the unsafe and unsound practices be corrected by means of raising additional capital, reducing the volume of loans, and the adoption of reasonably conservative loaning policies."

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In subsequent correspondence with the Comptroller, beginning with a letter dated December 6, 1949, President Cosgriff took exception to the charges made and stated that the holders of the majority of the stock of the bank (himself, his wife, mother and sister) would not vote to increase capital under existing conditions. He invited the Comptroller to proceed under Section 30, and stated that he was prepared to defend himself at a hearing before the Board of Governors and would appeal to the courts, if necessary.

The bank was examined February 28, 1950, and the Comptroller proposed to state in his certification to the Board, which was never presented for formal consideration, that the examination disclosed no appreciable change in loan policies, that the matter of additional capital had not been presented to the meeting of shareholders held on January 10, 1950, and that the directors had failed to discontinue (after warning) the unsafe and unsound practices complained of in conducting the business of the bank.

The report of examination as of February 28, 1950, showed the following principal items:

Total assets		\$50,188,700
Deposits		46,315,400
Borrowed money (F. R. Bk.)		1,500,000
Cash and Government securities		25,831,800
Loans and discounts		20,954,000
Banking house, furniture and fixtures		831,100
Capital:		
Common	\$900,000	
Surplus	900,000	
Undivided profits	<u>307,100</u>	2,107,100

Adjusted capital account amounted to 4 per cent of total assets and 8.2 per cent of risk assets. Losses had been charged off during the examination and classified assets were:

	<u>Substandard</u>	<u>Doubtful</u>	<u>Loss</u>
Loans and discounts	\$781,500	\$128,600	\$42,800
Overdrafts	-0-	-0-	28
Suspense	-0-	-0-	167
Totals	<u>\$781,500</u>	<u>\$128,600</u>	<u>\$43,000</u>

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To: Mr. Millard

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Significantly, the examiner stated in the CONFIDENTIAL section of the report that:

"While there has been no expressed change in the loaning policies of this institution examiner senses a tendency towards conservatism."

A meeting of representatives of the Board's staff and Vice President Slade of the Federal Reserve Bank, San Francisco, with representatives of the Comptroller and the FDIC was held June 1, 1950. The Continental National Bank and Trust Company of Salt Lake is one of a group of nine banks in which the Cosgriffs have substantial ownership or control. There are three national banks, one State member bank, four nonmember insured banks and one nonmember uninsured bank. It was suggested that all should be examined simultaneously to determine the situation of the whole group. After discussion the Comptroller's representatives agreed to the suggestion that simultaneous examinations should be made but did not wish to delay Section 30 proceedings. Also, they agreed to invite Mr. Cosgriff to Washington for a further discussion of the matter before certifying the case to the Board.

Mr. Cosgriff did come to Washington about July 1 and, after a discussion at the Comptroller's office, tentatively agreed to increase the capital of the bank by \$250,000 through the injection of new funds and to reduce the loans of the Salt Lake bank by about \$4,000,000 within six to nine months. The reduction in loans was to be a bona fide reduction made in loans of borderline or distinctly risk character. This agreement was to be confirmed by letter after Mr. Cosgriff had consulted with his associates and we were advised that, if the confirmation was received, the Comptroller did not propose to proceed further with the matter of certification to the Board under Section 30.

About two weeks ago we were advised that the agreement had not been confirmed but it was understood that Mr. Cosgriff had not returned to Salt Lake City.

Simultaneous examination of all banks in the group is still contemplated but the time for such examinations has not been determined.

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