

A meeting of the Board of Governors of the Federal Reserve System was held in Washington on Thursday, June 29, 1939, at 12:15 p. m.

PRESENT: Mr. Eccles, Chairman
Mr. Ransom, Vice Chairman
Mr. Szymczak
Mr. McKee
Mr. Davis
Mr. Draper

Mr. Morrill, Secretary
Mr. Bethea, Assistant Secretary
Mr. Clayton, Assistant to the Chairman

The action stated with respect to each of the matters herein-after referred to was taken by the Board:

The minutes of the meeting of the Board of Governors of the Federal Reserve System held on June 28, 1939, were approved unanimously.

Letter to Honorable Preston Delano, Comptroller of the Currency, reading as follows:

"There is enclosed herewith a copy of a letter which the Board has received from the Federal Reserve Bank of Kansas City requesting advice as to whether the Union National Bank in Kansas City is violating the provisions of the Board's Regulation F, relating to the collective investment of trust funds, by acting as trustee under a trust indenture executed by such bank and American Trust Funds, Inc. There is also enclosed a copy of the reply which the Board proposes to make to this inquiry. In view of the fact that the operations of a national bank are involved, it will be appreciated if you will advise whether there is any objection, from the standpoint of your office, to the transmission of the proposed reply.

"This matter has been discussed informally with representatives of your office; and, if your office should desire to examine further the enclosures forwarded

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"to the Board with the letter from the Federal Reserve Bank of Kansas City, such enclosures, of course, will be made available."

Approved unanimously.

Letter to Mr. Fletcher, Vice President of the Federal Reserve Bank of Cleveland, reading as follows:

"Reference is made to your letter of June 19, 1939, submitting for the consideration of the Board an application of 'The First-Central Trust Company', Akron, Ohio, for permission to retire its outstanding issue of capital debentures amounting to \$500,000.

"It is noted that you feel that you are without authority in this particular case in view of the instructions contained in the Board's letter of December 15, 1934 (X-9048). Reference, therefore, is made to the Board's letter of May 1, 1937, (X-9882) which extended the authority to approve reductions of capital on behalf of the Board 'to cover all cases where the Board's approval is required under a condition of membership, subject only to the condition that the Federal reserve bank is of the opinion that the proposed reduction is justified as a matter of sound banking policy and that it may be legally accomplished'. In this case, however, the approval of the Board is not required as the debentures in question are held by the State Superintendent of Banks and do not come within the scope of the condition of membership to which the member bank is subject. (See Section 9 of the Federal Reserve Act and footnote numbered 9, Regulation H.) Nevertheless, the Board understands that an expression of its opinion is desired and has given the matter consideration.

"The liquidity, good asset condition and satisfactory management of the institution have been noted, also the fact that the proposed transaction has been approved by the State Superintendent of Banks. In view, however, of the bank's position as the largest bank in the community, the steady increase of its deposits, the extent of its trust activities and the fact that the total of its capital accounts is now less than ten per cent of deposits, the Board feels that the retirement of the full

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"amount of debentures should not be made at this time. Nevertheless, the circumstances are such that the Board will not object to the retirement, as you suggest, of a nominal amount, say \$100,000 or so. It is felt that future retirements, if not replaced by new capital, should be dependent upon the realization of actual earnings definitely earmarked for retention in the capital account rather than upon the anticipation of future earnings."

Approved unanimously.

Letter to Mr. Parker, President of the Federal Reserve Bank of Atlanta, reading as follows:

"This is in reply to your letter of May 29, 1939, regarding the 'American Bank & Trust Company', New Orleans, Louisiana, with particular reference to the question of further retirements of preferred stock. Last April when you and Mr. Clark were in Washington members of the Board's Division of Examinations discussed the situation with you and expressed the opinion that the reduction of the preferred stock from \$1,500,000 to \$750,000, and particularly the latest retirement of \$250,000, had not been justified. You state that shortly following that conversation, the bank desired to retire an additional \$250,000 preferred stock and that President Legier became incensed when advised that, in your opinion, further reduction would be inexpedient because of the large total of assets consisting of investments in the company owning the bank building, real estate holdings, and loans representing potential other real estate. You report that Mr. Legier stated that he had been definitely assured by Mr. Newton at the time the preferred stock was sold that it might be retired at any time, and that the 'repudiation' of Mr. Newton's assurance constituted bad faith.

"We do not know what assurances Mr. Newton gave, but a review of the record would indicate that Mr. Legier must be laboring under a misunderstanding. In a letter to the Board dated January 23, 1934, Mr. Newton advised of his fruitless efforts to induce the bank to strengthen its capital and stated that he would be unable to certify the bank for deposit insurance until steps had been taken to rehabilitate the capital. No action having been taken,

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"the Board wrote Mr. Newton on May 18, 1934, pointing out the unsatisfactory capital position of the bank and asked him to present the condition of the bank as he saw it to the bank's board of directors, inform them that it was the firm opinion of the Board that action should be taken to provide adequate capital, and request that they advise him what action they expected to take to accomplish it. On May 31, 1934, Mr. Newton again advised the Board that he could not recommend the bank for certification for deposit insurance unless additional capital were introduced. In June 1934 the bank's directors decided to apply to the Reconstruction Finance Corporation for the sale of not less than \$1,000,000 preferred capital. Subsequently the requirement of individual certification for deposit insurance was repealed and the sale of \$1,500,000 preferred stock to the Reconstruction Finance Corporation was not completed until April 1, 1935, the bank in the meantime having made application for conversion into a national bank. Incidentally, in a letter dated August 31, 1934, to the Comptroller of the Currency, Mr. Clark, then Assistant Federal Reserve Agent, stated that it was the consensus of opinion of Mr. Legier, officers of the Federal Reserve Bank of Atlanta, and Mr. Robb, Chief National Bank Examiner, that additional capital funds of \$1,500,000 instead of \$1,000,000 would be necessary to counterbalance the investment in the building. In view of these circumstances, it seems highly improbable that Mr. Newton definitely assured Mr. Legier that the preferred stock might be retired at any time, which in effect would nullify the efforts made by Mr. Newton to obtain an increase in the bank's capital.

"The report of examination as of April 4, 1939, recently forwarded, shows adjusted capital funds of \$3,591,000 as compared with deposits of \$39,832,000, a liquid condition, and a negligible amount of assets classified as III or IV. The report shows, however, that the bank has investments in and advances to its wholly owned subsidiary owning title to its banking house amounting to \$2,416,000, and potential other real estate of \$740,000. Although the bank pays substantial rent for the space occupied and in addition pays taxes on the property, the combined total amounting to approximately \$106,000 last year, the building company has operated at a net loss or only negligible profit during recent years, with the result that the bank has been receiving no income on its investment of \$1,684,000 in the stock of the company.

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"In the report of examination the examiner classes \$300,000 of the line to Bell Realty Company and the \$274,000 line of Nard, Inc., as potential other real estate. The principal asset of the Bell Realty Company is property originally purchased by the bank to be used as a bank building site, but later sold to the Bell Realty Company, which at the time was a wholly owned affiliate. The company is reported to have only nominal net worth and some time ago its stock was sold for approximately \$1,000. According to information contained in the current and previous reports of examination, Nard, Inc., was organized with nominal capital of \$5,000 to take over other real estate from the bank. Its capital stock of \$5,000 has been practically wiped out through a surplus deficit of \$4,800.

"In view of all of the circumstances which have been set forth in the current and previous reports of examination regarding the companies, their relationship to the bank, and the purpose of their organization, it seems obvious that the companies are merely devices to avoid showing other real estate and that the obligations should be shown in the call report of condition as assets indirectly representing other real estate in accordance with the instructions on page 16 of the Manual of Instructions for the Preparation of Reports of Condition. In this connection reference is made to the confidential section of the previous report of examination wherein it is stated that both corporations served the bank as holding companies for other real estate, which would seem to be the only excuse, if indeed it be an excuse, for the transaction reported where the bank sold Nard, Inc., certain bonds on August 8, 1937, and repurchased them on the same day at a profit of \$12,600 to Nard, Inc. Early in the year a similar transaction had resulted in a profit of \$8,300 to the corporation.

"The report of examination shows that the Bell Realty Company stock formerly owned by Fischer Company, Inc., which is and has been closely associated with the bank, had been sold by Fischer Company, Inc., prior to the recent examination and the examiner reports that the management professed not to know who now owned the company. It has been noted also that the management continues to disclaim any knowledge as to the ownership and management of the Carondelet Building Company, to which it loaned \$400,000 on a second mortgage subject to a prior lien of

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"\$440,000 on property appraised at \$1,180,800. It is difficult to understand this, as, on the one hand, a lack of definite information regarding the ownership and management of the Carondelet Building Company and the Bell Realty Company is inconsistent with the claims made regarding the ability of the management and, on the other hand, a deliberate attempt to deceive the examiner and withhold from him pertinent credit information would be inconsistent with the complimentary remarks which have been made regarding the honesty and integrity of the management. It is believed that this matter should be cleared up, since, if the management actually does not know the facts in these cases, they should obtain them, or, if the management has deliberately deceived the examiners that fact should be known, made a matter of record, and the full facts as to the assets developed in order to complete the report of examination.

"One rather disturbing feature in the situation is that, through active trading, the bank in effect has been writing up its bond account and has used the profits to retire preferred capital and pay dividends. At the time of the previous examination, as of February 1, 1938, the bank's investment in Government securities consisted, except for a nominal amount, of \$14,375,000 par value $2\frac{1}{2}\%$ Treasury Bonds of 1949-53. In the period between examinations, all those bonds were sold and replaced by other Treasury Bonds. During the period January 1, 1935 to April 4, 1939, net profits of the bank are shown as \$1,336,000. Of this amount, however, \$1,162,000 represents net profits on securities sold. Net profits, exclusive of profits on securities sold, amounted to \$174,000, while dividends during the period amounted to \$259,000. The use of bond profits to pay dividends and retire capital in substantial amounts is inconsistent with the principles set forth in the uniform agreement regarding bank examination announced last summer wherein it was stated that 'until losses have been written off and adequate reserves established, the use of profits from the sale of securities other than those, will not be approved.'

"In the concluding paragraph of your letter of May 29 you ask for an expression of opinion with respect to Mr. Legier's very decided feeling concerning the further

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"retirement of preferred stock. The Board concurs in the opinion expressed by its Division of Examinations and by you that additional retirements of preferred stock are not justified at this time. You report that Mr. Legier is formulating plans for the sale of common stock at a premium in an aggregate amount sufficient to retire the \$750,000 preferred stock now outstanding. It is hoped that this desirable step may be accomplished shortly, and it will be appreciated if you will keep the Board advised as to progress made in this connection."

Approved unanimously.

Letter to Mr. Lichtenstein, Secretary of the Federal Advisory Council, reading as follows:

"Your letter of June 6 in regard to the consideration by the Council of the topic originally submitted by the Board in December, 1937, entitled 'How can the Federal Reserve System increase the value or scope of its services to member banks in practicable or desirable ways' has been brought to the attention of the members of the Board.

"The first response of the Council to this question was the submission of a compilation of replies to inquiries which members of the Council had made. The subjects covered were important to the System. The Council did not, however, give the Board any expression of its own views regarding these matters.

"As the members of the Board are confronted with the necessity of supplying their reasons for conclusions which they reach, they felt that the cooperation of the Council in furnishing the views of its members on these questions would be of value to the Board. It thereupon requested the views of the Council on the subjects covered by the compilation. Since the Council, however, desires to be excused from further consideration of this topic and expansion of its views, the Board has asked me to advise you that it acquiesces in the request which the Council has made."

Approved unanimously.

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Thereupon the meeting adjourned.

Chester Morris
Secretary.

Approved:

W. Steeles
Chairman.