

A meeting of the Board of Governors of the Federal Reserve System was held in Washington on Wednesday, February 7, 1940, at 11:45 a.m.

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

Mr. Morrill, Secretary
Mr. Clayton, Assistant to the Chairman
Mr. Paulger, Chief of the Division of Examinations
Mr. Cagle, Assistant Chief of the Division of Examinations
Mr. Dreibelbis, Assistant General Counsel

Mr. Clerk, First Vice President of the Federal Reserve Bank of San Francisco

This was an executive session at which there was a discussion of a draft of "Comments and Suggestions concerning 'Comptroller's Requirements with respect to Bank of America N. T. & S. A.' which were discussed at the Treasury on February 2, 1940". It was stated by Messrs. Eccles and McKee that they proposed to submit this memorandum at the conference which Under Secretary Bell had invited them to attend this afternoon at 2:30 p.m. at the Treasury, with representatives of the Treasury and the Comptroller's Office and the suggestions and criticisms of the other members of the Board were invited.

The draft was read, paragraph by paragraph, in the light of the draft of the Comptroller's proposed requirements, of which each member had previously been furnished a copy. With some minor changes

2/7/40

-2-

in phraseology, the draft was accepted by the members of the Board in the form hereinafter set forth, with the understanding that Messrs. Eccles and McKee, together with Messrs. Dreibelbis and Morrill, would attend the conference and would submit this memorandum at that time:

"1. Capital. A requirement that the capital must be increased immediately by not less than \$35,000,000 would not appear to be unreasonable. Since it is believed that such capital can be obtained only through the purchase of preferred stock by the Reconstruction Finance Corporation and since the capital of the bank can be reduced only with the consent and upon such terms and conditions as the Comptroller of the Currency may prescribe in the amendments to the articles of association of the bank providing for such increase in capital, we would eliminate from the program any reference to a subsequent increase in common stock upon the retirement of preferred stock, which would be in effect an attempt to determine in advance what should be the capital requirements with respect to this bank over a substantial period of time.

"2. Dividends. We would prefer to attack this problem more directly by imposing requirements which would cause the Bank to rectify its condition and practices, thus leaving to the existing limitation of law the payment of dividends out of any earnings not used in meeting the imposed requirements. Consistently with this approach, one requirement might be that bond profits must be placed in a special reserve account to take care of losses and depreciation in the bond account, and the excess, if any, to be retained as long as any preferred stock is outstanding or until the Comptroller of the Currency is satisfied that it is no longer necessary to maintain such reserves to meet such losses or depreciation and consents to its use for other purposes.

"3. Accounting practices. There is, of course, no objection to the first sentence. As to the other two sentences it is believed that their intent will be covered by other suggestions.

"4. Losses. A large part of the losses set up by the examiners in the last report of examination is represented in banking houses and other real estate which are also a large part of the amount classified in column III.

2/7/40

-3-

"Concerning the Bank's banking premises, we would suggest giving consideration to requiring that additional reserves be set up to the extent necessary so that the carrying values of banking premises, as shown on the Bank's books and in the investments in Merchants National Realty Corporation, shall not include any 'write-ups' (i.e., any increases in book value not due to actual increase in cost due to acquisition of properties or to improvements of a permanent nature) and that the carrying value shall not include any depreciation which should have been taken in accordance with established banking practices during the period that the Bank has been operating under its present charter.

"Concerning the Bank's other real estate we would suggest giving consideration to requiring that additional reserves shall be set up to the extent of 25 per cent of the existing carrying values of all 'other real estate' of the Bank, whether carried on its books as such or as banking premises or transferred to and now held by California Lands, Inc., Capital Company, and Merchants National Realty Corporation; that no real estate acquired by the Bank shall be transferred to California Lands, Inc., Capital Company or Merchants National Realty Corporation, or to any other party under similar arrangements, and that no real estate shall be disposed of except for cash or under bona fide sales contracts with purchasers under conditions justifying the expectation that such sales will be final. As soon as possible after the acquisition of any additional real estate it shall be placed on the Bank's books as 'other real estate' and shall be appraised by competent appraisers, and thereafter shall not be carried at an amount exceeding such appraised value or the book value, whichever is the lower.

"5. Illegally held bank stock. We suggest that further consideration be given to the question whether, in view of the terms of the option agreement, sale of the stock at this time would be advantageous to the Bank. In this connection, it might be well to consider imposing a requirement that if and to the extent that Transamerica Corporation shall fail to repurchase the National City stock from the Bank, in accordance with the existing option agreement between Transamerica and the Bank, the Bank shall make adequate provision for the removal of such stock without prejudice to any rights that it might

2/7/40

-4-

"have against Transamerica Corporation under the option contract.

"6. Large lines. We agree that the progress that has been made in the past year in liquidating indebtedness of Transamerica and its subsidiary corporations should be continued, that the aggregate amount of these lines should be brought within the statutory limitations, and that such indebtedness should be adequately and properly secured in accordance with sound banking practices and applicable legal requirements. We believe also that the concentration of credit in the Bank, depending upon the shares of other closely related banking institutions should be discontinued; that the credit facilities of the Bank should not be used for the expansion of Transamerica; and that, with respect to existing loans representing credit used for that purpose, there should be a program for reduction and retirement. To this end we suggest that there be a definite understanding with the Bank as to what associated and affiliated companies are covered by the restriction and that the aggregate of such loans be brought within the legal limit of the Bank's lending power by July 15, 1942; that the stock of any bank in which Transamerica is substantially interested securing such loans be eliminated by July 15, 1945; and, that no similar pledges be accepted. We believe also that consideration should be given to the discontinuance of further extensions of credit by the Bank for the purpose of purchasing or carrying Transamerica stock and to a provision that no collateral value shall be assigned to such stock when pledged to secure other loans.

"Concerning the A. O. Stewart Line we suggest that the Bank be required to continue its orderly liquidation in accordance with the agreement referred to in the report of examination of August 31, 1939, as having been made by the Bank and A. O. Stewart and which contemplated the liquidation of \$1,000,000 of such indebtedness before the end of 1940 in addition to any liquidation from the sale of United States Treasury bonds and other Government obligations.

"7. Real estate concentration. We have already made certain suggestions with respect to other real estate in our comments and suggestions under '4. Losses.' Non-conforming real estate loans and real estate acquired or carried in violation of section 5137 of the Revised Statutes should receive necessary attention. We have had in mind in making our suggestion as to reserves for real estate the desirability of avoiding statements which might be

2/7/40

-5-

"interpreted as placing upon the Government responsibility for forced, immediate liquidation which might undermine market values.

"8. Self-insurance reserve. We believe that such steps should be taken as may be necessary to determine the legality of the transaction between the Bank and Transamerica General Corporation relating to insurance against certain losses of the Bank. In the event that it be found that such transaction was invalid the balance of the funds in the hands of Transamerica General Corporation, after deducting therefrom all losses paid by it, should be restored to the Bank."

Following this the Chairman referred to the fact that Mr. L. M. Giannini had been in town the last few days and had been trying to make an appointment with either Mr. McKee or himself and that neither Mr. McKee nor he had talked to Mr. Giannini but that Mr. Giannini had talked to Mr. Clayton and that Mr. Clayton had told Mr. Giannini that other very pressing matters, including the fact that a conference of examiners was being held, made it impossible for either Mr. Eccles or Mr. McKee to set a time for a conference. Mr. Clayton had reported that he had mentioned to Mr. Giannini in a telephone conversation that there had been some conferences with the Treasury but Mr. Clayton had not indicated the character of the conferences.

It had also been reported that Mr. O. K. Cushing had called upon the Comptroller of the Currency and had had a conference with him and Mr. Whitney Seymour, Special Counsel for the Comptroller, as to which, however, the Chairman had been advised by Mr. Delano that no mention had been made of a possible program, the discussion being confined entirely to the legal aspects of the hearing on the order to

2/7/40

-6-

show cause. It was, however, understood that Mr. Cushing had desired to have an appointment made for an interview with Chairman Eccles or Mr. McKee and no commitment had been made as to such an appointment.

Both Chairman Eccles and Mr. McKee reiterated the view that it would be preferable for the Comptroller, the Federal Deposit Insurance Corporation, and the Board, to present a common front upon a proposed program but that if the Comptroller did not choose to participate there was reason to believe that the Federal Deposit Insurance Corporation would join with the Board and that, in any event, the Board would have to be in position to confer with the representatives of the Bank of America, as they were of opinion that we could not properly refuse to meet them at some convenient time and that we should be prepared to discuss the condition of the bank frankly with its representatives in the light of what the Board would consider to be corrective measures that should be taken. There was no dissent by the other members of the Board from this view of the situation.

Thereupon the meeting adjourned.

Robert Morrie
Secretary.

Approved:

W. A. Eccles
Chairman.