CIRCULAR No. 6
OF THE
RECONSTRUCTION
FINANCE CORPORATION

INFORMATION REGARDING SUBSCRIPTIONS FOR
PREFERRED STOCK, OR LOANS UPON PREFERRED
STOCK BY THE RECONSTRUCTION FINANCE
CORPORATION AS AUTHORIZED IN THE
ACT OF CONGRESS, APPROVED
MARCH 9, 1933

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INFORMATION REGARDING SUBSCRIPTIONS FOR PREFERRED STOCK, OR LOANS UPON PREFERRED STOCK BY THE RECONSTRUCTION FINANCE CORPORATION AS AUTHORIZED IN THE ACT OF CONGRESS, APPROVED MARCH 9, 1933

The act of Congress approved March 9, 1933 (Public No. 1, 73d Cong.), authorizes national banks to issue nonassessable preferred stock. The act thus gives an opportunity to communities in which national banks are or may be located to assist in the organization or reorganization of such institutions by the purchase of stock which does not carry the usual double liability. The act also authorizes the Reconstruction Finance Corporation to purchase such nonassessable preferred stock or make loans thereupon, and thereby assist in particular instances where it may not be possible to raise locally all of the required capital.

The Reconstruction Finance Corporation may also subscribe for or lend on preferred stock of State banks and trust companies in those States in which such institutions are authorized to issue preferred stock.

This circular is issued to give information concerning:

I. Subscription by the Reconstruction Finance Corporation to preferred stock in a national banking association, or State bank or trust company, and

II. Loans by the Corporation to others upon the security of preferred stock in such institutions.

By virtue of section 304 of the act, the Corporation is authorized to subscribe for preferred stock in any national banking association, or any State bank or trust company if the Corporation is requested to do so by the Secretary of the Treasury with the approval of the President. Upon similar request and approval, the Corporation is authorized to make loans secured by such stock as collateral. The Corporation is further authorized, with the approval of the Secretary of the Treasury and under such rules and regulations as he may prescribe, to sell in the open market, or otherwise, the whole or any part of such preferred stock acquired by the Corporation pursuant to the provisions of said section.

I. Procedure to be followed in making application to the Corporation for the Corporation's direct subscription to preferred stock of the applicant

1. Application may be made for subscription to the preferred stock of an open bank which is to continue doing business, a closed bank which contemplates reorganization, or a bank to be newly formed.
2. The applicant institution issuing the stock must be authorized by law to issue preferred stock. National banking associations are authorized to issue preferred stock by section 301 of the act. The ability of State banks and trust companies to offer preferred stock for subscription will of course depend upon the laws of the respective States under which they are incorporated. The laws of most States at the present time do not permit the issuance of preferred stock by State banks and trust companies.

3. Application should be made by the applicant bank or trust company directly to the loan agency of the corporation serving the territory in which the applicant is located. The application should include and be accompanied by the following information and documents:
   
   (a) Copy of the charter and any proposed amendment thereto, under which the preferred stock offered for subscription is to be issued.

   (b) If applicant is other than a national bank, copy of the statutes from which the applicant derives its authority to issue preferred stock.

   (c) Copy of a resolution already adopted or proposed to be adopted by the board of directors of the applicant authorizing the sale of such stock.

   (d) Copy of the latest report of examination of the applicant.

   (e) Statement of the applicant’s condition as at the close of business on the date the application is forwarded.

   (f) Schedules in adequate detail showing assets pledged to secure borrowed money, public funds, or other liabilities.

   (g) Statement of any plan of reorganization which the applicant proposes to put into operation.

   (h) Information relating to the approval by the supervisory authority of the proposed plan and the conditions under which such supervisory authority is willing to permit the applicant to resume normal business.

4. The applicant must show that its earning capacity will be sufficient at least to enable it to pay dividends on the preferred stock at the rate of six per centum (6%) per annum after meeting all other expenses and making proper provisions for elimination of losses and/or doubtful assets, and required contributions to surplus and reserve.

5. The terms of the preferred stock offered must give the Corporation substantially the same protection of and provision for retirement of its investment or security interest in the preferred stock as the terms of the suggested Articles of Association for national banking associations issuing preferred stock attached hereto. (R.F.C. Form PS 1, March 20, 1933.) Note particularly that, to be acceptable, any preferred stock must, while any part of it is outstanding, be protected by:

   (a) Substantial voting rights in all matters concerning the issuing institutions.

   (b) Limitations on common stock dividends.

   (c) Compulsory regular application of a substantial part of net profits of the issuing institution to the retirement of preferred stock.
(d) Understandings from time to time between the bank and this Corporation with respect to general policies.

(e) An agreement to furnish the Corporation from time to time such reports of the bank's operations and policies as the Corporation may require.

When the applicant is governed by State law as to the issuance of preferred stock, and when under the law such preferred stock is assessable, the Corporation will not subscribe for such stock (although it may consider making loans upon the collateral thereof).

6. It is anticipated that the Corporation will be asked to participate in preferred stock issues in the following general situations:

(a) Where the capital is partially impaired.

(b) Where the capital is entirely eliminated by losses.

(c) Where the deposits are impaired after total elimination of the capital structure.

Before the Corporation will subscribe for or lend upon the preferred stock of any bank, it shall be determined that the sound value of the assets is at least equal to the deposit liabilities and other liabilities in the bank or to be assumed by the reorganized bank. In addition, there should be provided a reasonable margin of protection for the preferred stock to be taken by the Corporation, represented by common stock, or by a class of preferred stock subordinated to that to be taken by the Corporation, or otherwise.

In case (a) above, it should be determined whether the remaining capital structure is sufficient to furnish such reasonable margin of protection.

In case (b) above, the margin of protection for the preferred stock held by the Corporation may be provided as follows:

1. Purchase of common stock or subordinated preferred stock, by the stockholders, depositors, and others, and/or

2. The voluntary reduction or subordination by depositors and other creditors of a part of their claims against the bank.

In case (c) above, the impairment must be taken care of by a reduction on a pro rata basis of the deposits and/or other creditor claims affected, so that the total of deposits and other creditor claims of the institution will not exceed the sound value of its assets, after which the procedure will be the same as in case (b) above.

Any scaling of liabilities or use of the funds belonging to depositors or other creditors, whether in connection with a reorganization or otherwise, if not actually consented to by the depositors or other creditors affected, must be undertaken in strict conformity with statutory authority. Note that section 207 of the act relates only to national banks.

II. Procedure for making application for a loan secured by stock as collateral

1. The Corporation may make loans to individuals, firms, or corporations desiring to purchase the preferred stock of a bank, but temporarily in need of funds to finance the investment. In making such loans the Corporation will
be governed by the usual factors determining a sound credit risk. The pre-
ferred stock will be accepted as collateral and in addition the financial respon-
sibility of the borrowers will be given careful consideration. Where necessary,
other collateral may be pledged as a margin in addition to the preferred stock.
The Corporation must receive satisfactory voting rights on preferred stock
pledged as collateral.

2. The application for such a loan on preferred stock as collateral should
include all information and documents which would be required in and with
an application for direct subscription to such stock by the Corporation, and
in addition:

(a) A statement of the proposed terms of the loan,
(b) A statement of the applicant's financial condition,
(c) A statement of any collateral offered for the loan in addition to
the preferred stock.

III. Form of application

Application forms shortly will be provided and will be obtainable at the
loan agencies of the Corporation. Meanwhile applications may be made in
writing to the loan agencies in any form that will briefly, but adequately,
supply the information herein requested.

IV. Statutory provisions

A copy of the act of Congress approved March 9, 1933, is enclosed herewith.