NYTimes OCT 9 1974

FRANKLIN FOUND INSOLVENT BY U.S. AND TAKEN OVER

European Group in Control After Biggest Bank Failure —Depositors Protected

By JOHN H. ALLAN

The Franklin National Bank was declared insolvent yesterday in the largest bank failure in American banking history.

The institution was immediately taken over by the European-American Bank and Trust Company, a New York. State-chartered entity owned by six of the largest banks in Europe.

All depositors of the Franklin will become depositors of the European-American. All offices will be open during regular banking hours today and there will be no interruption of banking services to the public.

Under the take-over agreement worked out with regulatory authorities, no depositor will suffer any losses.

Pride of Long Island

For the Franklin National Bank, once the pride of Long Island with some $4.5-billion in assets that made it the 20th largest bank in the country, the action yesterday ended a five-month effort to remain alive and independent.

The Franklin National Bank's fundamental problem, Government officials said yesterday, was bad management. This fault was exacerbated this spring when the bank incurred large foreign-exchange trading losses that eventually were estimated at nearly $46-million.

Yesterday's take-over, rumored for weeks, was effected swiftly during the afternoon after the bank closed at its normal 3 P.M. hour. The action was announced by Frank Wille, chairman of the Federal Deposit Insurance Corporation, at a news conference at the Federal Reserve Bank of New York.

To effect the takeover, the office of the Controller of the Currency went into Federal Court for the Eastern District of New York and had the bank declared insolvent.

Then the F.D.I.C. moved im-

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mediately to accept bids from four banks to permit an orderly transfer of assets and liabilities from the beleaguered bank to a strong banking institution.

Basically, European-American agreed to take over slightly more than $1.7-billion, mostly comprising Franklin deposits, plus $1.58-billion of loans and securities. For this package it paid a combined premium of $125-million.

The F.D.I.C. took over loans to Franklin from the Federal Reserve Bank of New York — borrowings that had reached more than $1.7-billion, the reserve bank disclosed yesterday. The figure was perhaps $300-million larger than banking sources outside Franklin had expected.

The deposit insurance agency will also take over about $2-billion of less-desirable Franklin loans and securities and repay the $1.7-billion to the Federal Reserve Bank over a three-year period.

Avoiding Delay

This agreement, Mr. Wille stated, avoids any need for payments to Franklin's 620,000 depositors by the F.D.I.C. and it avoids financial loss or delay to approximately 6,000 Franklin depositors whose accounts exceed the $20,000 deposit insurance limit.

Besides European-American, the other bidders were the Chemical Bank, the Manufacturers Hanover Trust Company and the First National City Bank. Mr. Wille said Citibank's offer was submitted as "a bid of last resort" in case other banks failed to bid.

European-American Bank has been advertising for more than a week in major Long Island newspapers and on radio as a bank the residents would soon hear more about. Mr. Wille denied "categorically," however, that European-American knew before yesterday that it was the winning bank.

One Bid 'Close'

The F.D.I.C. chairman described one bid as "close" to European-American's, but he declined to divulge any of the other bids.

The F.D.I.C. also agreed to guarantee the European-American Bank against any unknown losses it may suffer as a result of past actions of Franklin. In addition, the agency lent the winning bank $100-million and may lend it another $50-million, all to be used to be used as captial.

The take-over, described by the F.D.I.C. as a "merger and assumption transaction" and not simply a merger, was done under the agency's authority to reduce risk of loss to the F.D.I.C., which is responsible for insuring deposits in virtually all American banks.

In pursuing this route, the Controller of the Currency, the F.D.I.C. and the Federal Reserve had to reject the Franklin's plan for remaining independent.

Problems Surface

Earnings of the Franklin National Bank have declined in every year since 1970, when the bank reported a profit of $19.62-million. But its current problems first came to light early in May.

At that time, the Federal Reserve Board denied the bank's application to acquire the Talcott National Corporation, a major factoring and business financing concern, on the ground that the acquisition would divert resources from the bank's recently begun program to improve its management.

In mid-May, the Bank's directors voted to omit a quarterly divident payment, and shortly after that the bank disclosed a large loss in foreign-exchange trading. Since then this loss has been set at nearly $46-million, and the bank reported a total loss of $83-million for the first six months of 1974.

Deposits Shrink

The news caused depositors to move swiftly to withdraw their money. Total deposits, which were reported at $3.72-billion at end of the 1972 in the bank's annual report, sank from $2.99-billion early in May to $1.37-billion last week.

Shortly after disclosure of Franklin's foreign-exchange losses, the Controller of the Currency declared several times that the bank was solvent.

During the summer, the Franklin borrowed heavily from the Federal Reserve Bank of New York to replace funds withdrawn by depositors. According to Franklin officers, this borrowing totaled $1.4-billion for most of the period.

Fed Under Fire

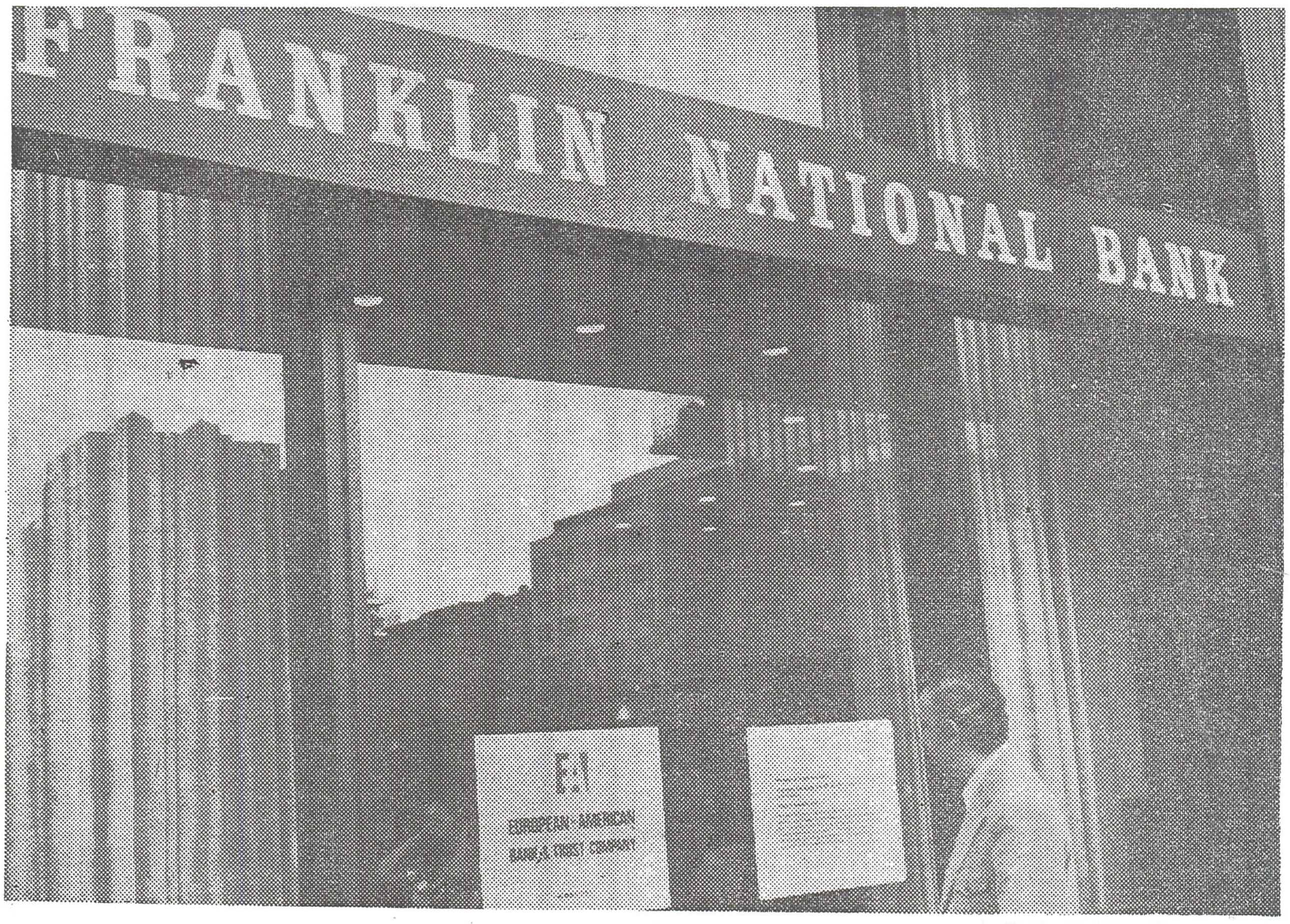
Although the outflow of deposits slowed after late July, it never ceased entirely, and the bank's effort to remain alive and independent never seemed to have much chance, especially in Washington, where the Federal Reserve reportedly was coming under criticism for making such a large loan to an ailing bank.

On June 20, Harold V. Gleason, the former savings bank public relations official who had risen to chairman and chief executive officer of Franklin, resigned and was replaced by Mr. Barr, a former chairman of the F.D.I.C. and Secretary of the Treasury for a short while during the last days of the Johnson Administration.

In mid-September, Mr. Barr presented a plan for the Franklin to remain independent as a caled-down regional bank serving Long Island, the area in which had grown from a one-office operation to the nation's 20th-largest bank.

Mr. Barr's plan called for extensive aid from theF.D.I.C. in the form of purchase of assets, guarantees and loans. Last Thursday, Frank Wille, F.D.I.C. chairman and former Superintendent of Banks for New York State, rejected the Barr plan, although he left open the door by the slimmest crack.

Mr. Barr went to Washington last Friday morning to begin revisions in a last-ditch effort to preserve the institution and apparently those efforts were continuing yesterday afternoon, even as Federal officials were moving into the bank.



The New York Times/Meyer Liebowitz

The Franklin National Bank branch office at 800 Third Avenue after 4 P.M. yesterday. The signs in the window announced that Franklin had become the European-American Bank and Trust Company.