

Member Bank Earnings

net profits after taxes

millions
of dollars

Ratio
to capital
account

| | | |
|--------------------|-----|------|
| 1929 | 557 | 8.8 |
| 1935 | 212 | 4.1 |
| 1940 | 349 | 6.2 |
| 1945 | 788 | 10.9 |
| 1946 ¹² | 860 | 10.8 |
| 1947-est. | 635 | 7.6 |

1070

75

67

1170

547

623

1135

547

588

2) 1.080
540

6^m
2
1

1^x

1.47

1123/47

IMPOSITION OF INTEREST CHARGE ON OUTSTANDING
FEDERAL RESERVE NOTES

The earnings of the Federal Reserve Banks for the year 1946 were such that they were able to transfer to their surplus accounts at the end of the year an aggregate amount of more than \$81,000,000. Unless steps are taken by legislation or otherwise to change the situation now existing, it is reasonable to expect that the earnings of the Reserve Banks will not be greatly different for the year 1947. All of the Reserve Banks now have a surplus in excess of twice the amount of their paid-in capital stock.

Several methods of meeting the problem caused by the increased earnings of the Federal Reserve Banks, resulting in large measure from their holdings of Government obligations, have been suggested. One of these is that the franchise tax to which the Federal Reserve Banks were subject prior to 1933 be restored to the law. This, however, would require legislation. As an alternative to the franchise tax, the Federal Reserve Banks, without the necessity for legislation, might be required to pay to the Government interest on outstanding Federal Reserve notes in an amount commensurate with the amount which might be payable under a franchise tax provision.

Legal Authority. - The fourth paragraph of section 16 of the Federal Reserve Act provides that a Federal Reserve Bank "shall pay such rate of interest as may be established by the Board of Governors of the Federal Reserve System on only that amount of such notes (Federal Reserve notes) which equals the total amount of its outstanding Federal Reserve notes less the amount of gold certificates held by the Federal Reserve agent as collateral security."

It is true that the primary intent of Congress in placing this provision in the law seems to have been to provide a means of controlling the expansion of Federal Reserve notes, but the legislative history indicates that a minor consideration at least was possible revenue to the Government. At any rate, the provision of the law is explicit and appears to give the Board full authority to impose an interest rate on outstanding Federal Reserve notes (less the amount of gold certificates securing them) whenever it considers it advisable to do so. The law does not specifically state to whom the interest shall be paid by the Federal Reserve Banks, but it is reasonable and logical to conclude from the legislative history of the matter that the payment is to go to the Government.

How It Would Work. - Under this authority the Board could establish a rate of interest on Federal Reserve notes not secured by gold so that the amount payable by the Reserve Banks to the Government would be equivalent to the amount which would be payable under a franchise tax requirement. For example, if outstanding Federal Reserve notes not covered by gold certificates for the year 1947 averaged, say, \$15,000,000,000 the Board could fix a rate of interest equal to such a percentage of this amount that the Reserve Banks would pay to the Government 80 to 90 per cent, or any other desired proportion, of their earnings for the period. Under the law it would be permissible for the Board to establish a different rate of interest

for different Federal Reserve Banks, so that it could take into consideration the situation at individual Reserve Banks in arriving at the rate of interest to be paid, although whether this would be desirable is a matter that would require consideration.

The authority for imposing an interest charge on outstanding Federal Reserve notes, which has never been used, has been in the law since the enactment of the Federal Reserve Act. However, it is only in the last few years that use of the provision would have brought any considerable net revenue to the Government. Prior to 1933, when the franchise tax was in effect, the payment of such an interest charge would, of course, have caused a corresponding reduction in the amount paid by them to the United States as a franchise tax. In the years 1933 to 1939 the net earnings of the Federal Reserve Banks (after payment of dividends) were comparatively small, in no year being as much as \$7,000,000. In several years since 1933, outstanding Federal Reserve notes have been exceeded by the amount of gold certificates pledged against them and consequently an interest charge upon the excess of notes over gold security in those years would have produced no results.

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1/23/47

SECURITY HOLDINGS OF 12 AND 20 LARGEST BANKS, DECEMBER 31, 1946

(In Millions)

| <u>Rank</u> | <u>Bank</u> | <u>Total Securities</u> | <u>Total U.S. Govt.</u> | <u>Other Securities</u> |
|-------------|----------------------------------|-----------------------------|-----------------------------|-----------------------------|
| 1. | Bank of America, San Francisco | 2,862 | 2,394 | 468 |
| 2. | National City, New York | 2,388 | 2,093 | 295 |
| 3. | Chase National, New York | 2,492 | 2,221 | 271 |
| 4. | Guaranty Trust, New York | 1,518 | 1,451 | 67 |
| 5. | Manufacturer's Trust, New York | 1,285 | 1,233 | 52 |
| 6. | Continental Illinois, Chicago | 1,236 | 1,179 | 57 |
| 7. | First National, Chicago | 983 | 867 | 116 |
| 8. | Security-First Nat., Los Angeles | 1,071 | 1,030 | 41 |
| 9. | Central Hanover, New York | 836 | 799 | 37 |
| 10. | Bankers Trust, New York | 694 | 643 | 51 |
| | First National, Boston | 578 | 565 | 13 |
| 12. | Chemical, New York | 736 | 628 | 108 |
| | <u>TOTAL LARGEST 12 BANKS</u> | 16,679 | 15,103 | 1,576 |
| 13. | National Bank, Detroit | 691 | 632 | 59 |
| 14. | Bank of Manhattan, New York | 405 | 378 | 27 |
| 15. | Irving Trust, New York | 580 | 574 | 6 |
| 16. | Cleveland Trust, Cleveland | 605 | 583 | 22 |
| 17. | American Trust, San Francisco | 499 | 457 | 42 |
| 18. | Mellon National, Pittsburgh | 637 | 542 | 95 |
| 19. | Corn Exchange, New York | 549 | 538 | 11 |
| 20. | New York Trust Co., New York | 326 | 303 | 23 |
| | <u>TOTAL LARGEST 20 BANKS</u> | 20,971 | 19,110 | 1,861 |

HOLDINGS OF PUBLIC DEBT AND INTEREST ON PUBLIC DEBT

December 31, 1946
(Amounts in millions of dollars)

| | Outstanding par value | Estimated interest ^{1/} | Interest as percentage of outstanding par value |
|------------------------------------|--------------------------|-------------------------------------|--|
| Total interest bearing public debt | 257,980 | 5,304 | 2.06 |
| Holdings of: | | | |
| Commercial banks ^{2/} | 73,700 | 1,307 | ^{3/} 1.77 |
| Federal Reserve Banks | 23,350 | 144 | .62 |

^{1/} Estimated amount of annual interest on amounts outstanding as of December 31, 1946.

^{2/} Total holdings of all commercial banks at par value estimated on basis of figures reported in Treasury survey for a sample of banks.

^{3/} The actual return on the book value of holdings after amortization of premiums on bonds bought above par would be around 1.6 percent.

MEMBER BANK EARNINGS AND EXPENSES 1945-47

Figures for 1946 and 1947 estimated

(In millions of dollars)

| Item | 1945 | 1946 ^{e/} | 1947 ^{e/} |
|--|---------|--------------------|--------------------|
| Earnings | 2,102 | 2,420 | 2,425 |
| Interest and dividends on securities | | | |
| United States Government | 997 | 1,070 | 960 |
| Other | 139 | | |
| Interest and discount on loans | 588 | | |
| Other earnings | 377 | | |
| Expenses | 1,268 | 1,480 | 1,640 |
| Salaries and wages | 580 | | |
| Interest on time deposits | 183 | | |
| Other expenses | 505 | | |
| Net current earnings before taxes on income | 835 | 940 | 785 |
| Recoveries, profits on securities, etc. | 454 | } +160 | } +70 |
| Losses and charge-offs | 230 | | |
| Profits before income taxes | 1,058 | 1,100 | 855 |
| Taxes on net income | 270 | 240 | 220 |
| Net Profits | 788 | 860 | 635 |
| Cash dividends declared^{1/} | 246 | | |
| Asset and liability items:^{2/} | | | |
| United States Government securities | 71,795 | 71,216 | 60,000 |
| Other securities | 5,566 | 6,383 | 6,500 |
| Loans | 19,815 | 24,256 | 25,000 |
| Total assets | 125,132 | | |
| Time deposits | 21,487 | 26,500 | 28,000 |
| Total deposits | 116,983 | | |
| Total capital accounts | 7,243 | 7,904 | 8,400 |
| Ratio of net profits to total capital accounts | 10.9 | 10.8 | 7.6 |
| Ratio of interest on U.S. Government securities to U.S. Government securities | 1.4 | 1.5 | 1.6 |

^{e/} Estimated.

^{1/} Includes interest paid on capital notes and debentures.

^{2/} Figures are averages of the amounts reported for every call date in the current year and for the last call date in the preceding year.