FEDERAL RESERVE BANK OF DALLAS

FISCAL AGENT OF THE UNITED STATES

Dallas, Texas, December 30, 1964

PRELIMINARY ANNOUNCEMENT
ADVANCE REFUNDING OFFER

To All Banking institutions and Others Concerned in the Eleventh Federal Reserve District:

There is quoted below a press statement issued today by the Treasury Department in regard to an advance refunding:

> The Treasury today announced that it is offering holders of the 2⅝% bond due February 15, 1965, and seven other selected note and bond issues maturing from November 1965 to November 1967 an opportunity to extend the maturity of their holdings at attractive yields.
>
> The Treasury also said that it will shortly be offering $1.5 to $2.0 billion of June tax anticipation bills.
>
> The securities eligible for exchange and those being offered in the advance refunding are as follows:

Securities Eligible for Exchange and Their Maturity Dates		Securities Offered in Exchange and Their Maturity Dates
2⅝% bonds	2/15/65	
3½% notes	11/15/65	4% bonds 2/15/70
4% notes	11/15/65	
3⅝% notes	2/15/66	4⅛% bonds 2/15/74
3⅞% notes	2/15/66	
3¾% bonds	5/15/66	4¼% bonds 8/15/87-92
3¾% notes	8/15/67	(reopened issue)
3⅝% bonds	11/15/67	

> The public holds $3.4 billion of the 2⅝% bonds of February 15, 1965, and about $550 million is held by official accounts. This issue is so near to final maturity that its holders are not being offered the nontaxable exchange privilege that is, as has been customary, being made available to the other seven issues eligible for this advance exchange.
>
> The seven eligible issues maturing from November 1965 to November 1967 involve $18.7 billion of public holdings and official accounts hold an additional amount of about $10.4 billion of these maturities. No gain or loss shall be recognized for Federal income tax purposes solely on account of the exchange of these issues. A fuller statement of the treatment of the exchange for tax purposes is given in an attachment hereto.
>
> The 4⅛% bonds of 1974 and the 4¼% bonds of 1987-92 contain the usual provision for redemption at par value prior to maturity in payment of Federal estate taxes.
>
> Exchange subscription books will be open for five days, January 4-8. The exchanges will be made on the basis of par for par with accrued interest adjustments as of January 15, 1965. Because of differences in coupon and maturity among the various eligible issues, cash adjustments will be made to provide all subscribers with appropriately attractive opportunities. The cash and interest adjustments are shown in Table 1 attached.

The payment and delivery date for the new securities is January 19, 1965. All unmatured coupons should be attached to bearer securities presented for exchange. If a net amount is payable to the subscriber (see Table1) it will be made following the acceptance of surrendered bearer securities or the discharge of registration of registered securities. If a net amount is payable by the subscriber it should accompany the subscription.

A holder of the outstanding eligible securities can compare the interest he will receive as a result of exchanging now (plus or minus any payment, other than the adjustment of accrued interest) with the interest he is currently receiving on the eligible issues plus what he might expect to obtain by reinvesting the proceeds of the eligible securities at maturity. The approximate investment yield to the holder who makes the exchange is shown in column 2 of the attached Table 2. The minimum rate of reinvestment return that a holder who does not make the exchange would instead have to earn for the extension period, in order to equal the investment yield that would be received by making the exchange, is shown in the columns of Table 2 headed "Approximate reinvestment rate for the extension period." For example, if the 3¾% notes of 8/15/67 are exchanged for the 4⅛% bonds of 2/15/74, the investor receives 4⅛% for the entire 9 years and 1 month plus $0.10 (per $100 face value) immediately. If the exchange is not made, a 3¾% rate will be received until August 15, 1967, requiring the reinvestment of the proceeds of the 3¾'s of August 1967 at that time at a rate of at least 4.32% for the remaining 6 years and 6 months, all at compound interest to average out to a 4⅛% rate for 9 years and 1 month plus the $0.10 immediate payment.

The official circulars, subscription forms, and other material containing additional details of the offering will be mailed Thursday, December 31.

Yours very truly,

Watrous H. Irons

President

STATEMENT CONCERNING RECOGNITION OF GAIN OR LOSS FOR FEDERAL INCOME TAX PURPOSES JANUARY 1965 ADVANCE REFUNDING

Gain or loss, if any, upon exchanges of the 2⅝ percent bonds of 1965, must be fully recognized under the Internal Revenue Code.

Pursuant to the authority of Section 1037(A) of the Internal Revenue Code no gain or loss shall be recognized for Federal income tax purposes solely on account of the exchange of the remaining seven issues eligible for exchange in this advance refunding; provided, however, that Section 1031(B) of the Code requires recognition of any gain realized on such exchanges to the extent that money (other than interest) is received by the security holder in connection with the exchange as indicated in the following paragraph.

If a cash payment on account of the issue price of the new securities is paid to the investor, and such amount (discount) plus the fair market value[1] of the new securities exceeds the cost basis to the investor of the securities exchanged, such gain (but not to exceed the amount of the payment) must be recognized and accounted for as gain for the taxable year of exchange. The investor will carry the new securities on his books at the same amount as he is now carrying the old securities except that he will reduce the cost basis by the amount of the payment and increase it by the amount of the gain recognized. If the fair market value of the new securities plus the amount of the payment does not exceed the cost basis of the old securities, the basis of the new securities will be the cost basis of the old securities reduced by the amount of the payment. Gain to the extent not recognized in accordance with the above (or loss), if any, upon the old securities surrendered in exchange will be taken into account upon the disposition or redemption of the new securities. (See examples following the next paragraph.)

If a premium is paid by the subscriber no gain or loss will be recognized; but his tax basis in the new securities will be his cost basis of the old securities increased by the amount of the premium.

Examples of Federal Income Tax treatment where a bond is offered by the Treasury with a payment (other than the accrued interest adjustment) to the investor

1. Assume that:

   (a) The fair market value of the security offered by the Treasury on the date the subscription is submitted is $99.50 (per $100 face value).

   (b) The payment to the subscriber (discount) on account of $100 issue price is $.80.

   (c) The amortised cost basis of the security surrendered on the books of the subscriber is $100.50 (per $100 face value). (It is assumed that the security surrendered was bought at a price above $100.50 and that the original premium was reduced prorata over the period from purchase date to maturity.)

   The sum of the fair market value of the security offered by the Treasury and the payment to the subscriber is $99.50 plus $.80 or $100.30. This is less than the cost basis of the issue surrendered, therefore, no gain is recognized. The new issue will be entered on the books of the subscriber at a cost basis of $99.70, the cost basis of the issue surrendered less $.80. The gain or loss between this cost basis and the proceeds of a subsequent sale or redemption of the new issue will be a capital gain or loss to all investors, except those to whom the securities are stock in trade. Under present law, if the combined time that the security surrendered and the new security received in exchange were held exceeds 6 months, the capital gain or loss is long-term, otherwise it is short-term.

[1] The mean of the bid and asked quotations on date subscriptions are submitted.

2. The assumptions are the same as in example 1 except that the payment (discount) to the subscriber is now $1.20 (per $100 face value) instead of $.80 in example 1.

   The sum of the fair market value of the new security received in exchange by the subscriber plus the $1.20 payment (discount) is $100.70. This exceeds the cost basis of the security surrendered by $.20. This excess is a recognized gain reportable for the year in which the exchange takes place. The gain is a capital gain except to those to whom the securities are stock in trade. Under present law, if the time the security surrendered was held exceeds 6 months, the capital gain is long-term, otherwise it is short-term.

   The subscriber will carry the new issue received in exchange at a cost basis equal to the basis of the issue surrendered ($100.50), less the payment ($1.20), plus the amount of the recognized gain ($.20), or ($100.50 minus $1.20 plus $.20) $99.50.

3. The assumptions are the same as in example 1, except that the cost basis on the books of the subscriber, of the security surrendered is $99.00 (per $100 face value) instead of $100.50 in example 1.

   The sum of the fair market value of the new issue received in exchange by the subscriber plus the $.80 payment (discount) is $100.30 (as in example 1). This exceeds the $99.00 cost basis by more than $.80. However, the amount of the gain reportable for the year of the exchange is $.80, since the amount of gain recognized cannot exceed the amount of the payment. The nature of the recognized gain and its treatment is the same as in example 2.

   In this case, the subscriber will enter the new security received in exchange on his books at $99.00, the same cost basis as the security surrendered.

TABLE No. 1

PAYMENTS TO AND BY THE SUBSCRIBER IN THE JANUARY 1965 ADVANCE REFUNDING

(In Dollars Per $100 Face Value)
Amounts To Be Paid To Or By Subscribers

Securities To Be Exchanged	Price Adjustment Payment[1] To Subscriber	Price Adjustment Payment[1] By Subscriber	Accrued Interest To January 15, 1965 To Be Paid To Subscriber[2]	Accrued Interest To January 15, 1965 To Be Paid By Subscriber[3]	Net Amount To Be Paid To Subscriber	Net Amount To Be Paid By Subscriber
For the 4% Bond 2/15/70						
2⅝% Bond, 2/15/65[4]	.600000	—	1.091372	—	1.691372	—
Nov. 1965-Nov. 1967 Maturities:						
3½% Note, 11/15/65	.450000	—	.589779	—	1.039779	—
4% Note, 11/15/65	.900000	—	.674033	—	1.574033	—
3⅝% Note, 2/15/66	.400000	—	1.507133	—	1.907133	—
3⅞% Note, 2/15/66	.700000	—	1.611073	—	2.311073	—
3¾% Bond, 5/15/66	.500000	—	.631906	—	1.131906	—
3¾% Note, 8/15/67	.050000	—	1.559103	—	1.609103	—
3⅝% Bond, 11/15/67	—	.300000	.610843	—	.310843	—
For the 4⅛% Bond 2/15/74						
2⅝% Bond, 2/15/65[4]	.650000	—	1.091372	—	1.741372	—
Nov. 1965-Nov. 1967 Maturities:						
3½% Note, 11/15/65	.500000	—	.589779	—	1.089779	—
4% Note, 11/15/65	.950000	—	.674033	—	1.624033	—
3⅝% Note, 2/15/66	.450000	—	1.507133	—	1.957133	—
3⅞% Note, 2/15/66	.750000	—	1.611073	—	2.361073	—
3¾% Bond, 5/15/66	.550000	—	.631906	—	1.181906	—
3¾% Note, 8/15/67	.100000	—	1.559103	—	1.659103	—
3⅝% Bond, 11/15/67	—	.250000	.610843	—	.360843	—
For the 4¼% Bond 8/15/87-92						
2⅝% Bond, 2/15/65[4]	—	.250000	1.091372	1.766984	—	.925612
Nov. 1965-Nov. 1967 Maturities:						
3½% Note, 11/15/65	—	.400000	.589779	1.766984	—	1.577205
4% Note, 11/15/65	.050000	—	.674033	1.766984	—	1.042951
3⅝% Note, 2/15/66	—	.450000	1.507133	1.766984	—	.709851
3⅞% Note, 2/15/66	—	.150000	1.611073	1.766984	—	.305911
3¾% Bond, 5/15/66	—	.350000	.631906	1.766984	—	1.485078
3¾% Note, 8/15/67	—	.800000	1.559103	1.766984	—	1.007881
3⅝% Bond, 11/15/67	—	1.150000	.610843	1.766984	—	2.306141

OFFICE OF THE SECRETARY OF THE TREASURY
OFFICE OF DEBT ANALYSIS

December 30, 1964

[1] Payment on account of purchase price of offered securities.
[2] On securities exchanged.
[3] On securities offered.
[4] Not eligible for nontaxable exchange privilege.

TABLE No. 2

INVESTMENT RETURNS IN THE JANUARY 1965 ADVANCE REFUNDING

Securities Eligible for Exchange	Approximate Investment Yield From 1/15/65 to Maturity[1]: 4% Bond 2/15/70	4⅛% Bond 2/15/74	4¼% Bond 8/15/87-92[3] To First Call or Maturity	Approximate Reinvestment Rate for the Extension Period[2]: 4% Bond 2/15/70	4⅛% Bond 2/15/74	4¼% Bond 8/15/87-92[3] To First Call	To Maturity
2⅝% Bond, 2/15/65[4]	4.16%	4.23%	4.24%	4.16%	4.23%	4.24%	4.24%
Nov. 1965-Nov. 1967 Maturities:							
3½% Note, 11/15/65	4.18	4.24	4.25	4.23	4.28	4.27	4.26
4% Note, 11/15/65	4.18	4.24	4.25	4.24	4.28	4.27	4.27
3⅝% Note, 2/15/66	4.18	4.24	4.25	4.23	4.28	4.27	4.26
3⅞% Note, 2/15/66	4.18	4.24	4.25	4.24	4.28	4.27	4.27
3¾% Bond. 5/15/66	4.18	4.24	4.25	4.25	4.29	4.27	4.27
3¾% Note, 8/15/67	4.18	4.24	4.25	4.31	4.32	4.28	4.28
3⅝% Bond, 11/15/67	4.17	4.24	4.25	4.37	4.35	4.29	4.29

OFFICE OF THE SECRETARY OF THE TREASURY
OFFICE OF DEBT ANALYSIS

December 30, 1964

[1] Yields to nontaxable holders (or before tax) on issues offered in exchange based on prices of eligible issues (adjusted for payments on account of issue price). Prices are the mean of bid and ask quotations at noon on December 29, 1964.
[2] Rate for nontaxable holder (or before tax).
[3] Reopening of an existing security.
[4] Not eligible for nontaxable exchange privilege.