

DECLASSIFIED
Authority E.O. 12958

Form F. R. 567

END SHEET

KIND OF MATERIAL OR NUMBER

333.343

NAME OR SUBJECT

Allocation of Participations in
System Open Market Account
Federal Open Market Committee

DATES (Inclusive)

~~1937~~ - Jun. 1943

PART NUMBER

Part 2

DECLASSIFIED
Authority E.O. 12958

MAILED IN FILES SECTION
DEC 1 1943

December 31, 1942.

Mr. Robert G. Rouse, Vice President,
Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Rouse:

There is enclosed a statement, prepared in accordance with the formula adopted by the Federal Open Market Committee on December 18, 1940, showing the changes necessary in allocations of Government securities in the System Open Market Account on January 1, 1943.

Current earnings, exclusive of earnings on Government securities, and current expenses have been estimated by multiplying the actual amounts thereof July through November by 2.4. Estimates obtained on this basis for current earnings have been adjusted by deducting estimated net earnings on industrial advances and commitments attributable to funds received from the Secretary of the Treasury.

Very truly yours,

E. L. Smead, Chief,
Division of Bank Operations.

Enclosure

MD: th

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MAILED
J. E. Smead

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 Authority E.O. 12958

Form F. R. 148 D

REC. IN FILES SECTION
 DEC 31 1942

TELEGRAM
BOARD OF GOVERNORS
 OF THE
FEDERAL RESERVE SYSTEM
 LEASED WIRE SERVICE
 WASHINGTON

December 31, 1942

Rouse - New York

This will confirm understanding in telephone conversation that adjustments of participations in System Account will be as follows, in thousands of dollars:

Increases:

New York	70,049
Philadelphia	15,157
Cleveland	33,182
Chicago	928
St. Louis	546
Minneapolis	12,242

Decreases:

Boston	13,024
Richmond	27,294
Atlanta	13,704
Kansas City	8,834
Dallas	8,270
San Francisco	60,978

SMBAD

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ND
 ND:mcw

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DECLASSIFIED
Authority E.O. 12958

*Mr. Daniels ✓
Mr. Van Horn ✓
Mrs. Smith*

REC'D IN RECORDS SECTION
APR 19 1968
333,343

FEDERAL RESERVE BANK
OF NEW YORK

December 1, 1942.

Dear Mr. Smead:

We received your letter of November 30, 1942 (and have today sent to the Reserve banks a copy of the computation showing the adjustments to be made today in participations in the System Open Market Account, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on December 18, 1940.

Enclosed herewith is a copy of the letter of transmittal together with three copies of the computation, also copy of the telegram which was sent to each of the Federal Reserve banks on November 30.

Yours faithfully,

Robert G. Rouse
Robert G. Rouse,
Manager, System Open
Market Account.

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

Encls.(5)

Directive #1

DECLASSIFIED
 Authority E.O. 12958

MISC. 140.8-18M-6-41

SECURITIES DEPT RHB:HS

November 30, 1942

PLEASE SEND THE FOLLOWING TELEGRAM TO PRESIDENT OF EACH FEDERAL RESERVE BANK AS INDICATED BELOW:

In accordance with action of the Federal Open Market Committee at its meeting September 28, 1942, a readjustment of participations in Government securities held in the System Account is called for on December 1 under the plan for reallocation of Government securities adopted by the Federal Open Market Committee December 18, 1940.

The computations showing adjustments to be made in participations of the several Federal Reserve banks on December 1 will be mailed to all Reserve banks on December 1. These computations indicate an increase or decrease of _____ in your participation on December 1. We shall wire you on December 1, 1942 the detailed entries to be made.

		<u>INCREASE</u>	<u>DECREASE</u>
PADDOCK	BOSTON	\$ -	\$ 11,398,000
WILLIAMS	PHILADELPHIA	-	9,600,000
FLEMING	CLEVELAND	-	23,935,000
LEACH	RICHMOND	13,265,000	-
McLARIN	ATLANTA	13,363,000	-
YOUNG	CHICAGO	14,625,000	-
DAVIS	ST. LOUIS	-	1,539,000
PEYTON	MINNEAPOLIS	-	3,465,000
LEEDY	KANSAS CITY	16,771,000	-
GILBERT	DALLAS	9,791,000	-
DAY	SAN FRANCISCO	43,255,000	-

DECLASSIFIED
Authority E.O. 12958

MISC. 140A 75M-12-41

FEDERAL RESERVE BANK OF NEW YORK

December 1, 1942.

Dear Mr. Williams:

In accordance with my telegram of yesterday, I enclose herewith computation of the readjustments to be made today in the participations of the Federal Reserve banks in the System Open Market portfolio.

Yours faithfully,

~~Robert G. Roase,
Manager, System Open
Market Account.~~

Mr. Alfred H. Williams, President,
Federal Reserve Bank of Philadelphia,
Philadelphia, Pa.

Enc.

DECLASSIFIED
 Authority E.O. 12958

Form F. R. 148 b

IN FILES SECTION
 NOV 1 1942

TELEGRAM
BOARD OF GOVERNORS
 OF THE
FEDERAL RESERVE SYSTEM
 LEASED WIRE SERVICE
 WASHINGTON

November 30, 1942.

Reuse - New York

This will confirm understanding in telephone conversation that adjustments of participations in System Account will be as follows, in thousands of dollars:

Increases:

Richmond	13,265
Atlanta	13,363
Chicago	14,625
Kansas City	16,771
Dallas	9,791
San Francisco	43,255

Decreases:

Boston	11,398
New York	61,133
Philadelphia	9,600
Cleveland	23,935
St. Louis	1,539
Minneapolis	3,465

Smead

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[Handwritten initials]

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DECLASSIFIED
Authority E.O. 12958

FOUND IN FILES SECTION
DEC 1 1942
333,273

November 30, 1942.

Mr. Robert G. Reuse, Vice President,
Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Reuse:

There is enclosed a statement, prepared in accordance with the formula adopted by the Federal Open Market Committee on December 18, 1940, showing the changes necessary in allocations of Government securities in the System Open Market Account on December 1, 1942.

Current earnings, exclusive of earnings on Government securities, and current expenses have been estimated by multiplying the actual amounts thereof January through October by one and one-fifth. Estimates obtained on this basis have been adjusted in the same manner as for the previous reallocations this year; namely, by adding \$480,000 to current expenses at New York to cover extraordinary depreciation charges on air-conditioning equipment and by deducting from current earnings estimated net earnings on industrial advances and commitments attributable to funds received from the Secretary of the Treasury.

Very truly yours,

E. L. Smead, Chief,
Division of Bank Operations.

Enclosure

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DEC 1 1942

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT, DECEMBER 1, 1942
(In thousands of dollars)

1942

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minne- apolis	Kansas City	Dallas	San Francisco
A. Expenses													
1. Estimated current expenses, 1942	37,925	2,850	9,197	2,895	3,513	2,567	1,753	4,969	1,979	1,110	1,929	1,542	3,621
B. Estimated dividends, 1942	8,667	566	3,184	708	888	348	303	955	269	183	280	266	717
C. Estimated expenses and dividends, 1942	46,592	3,416	12,381	3,603	4,401	2,915	2,056	5,924	2,248	1,293	2,209	1,808	4,338
D. Earnings													
1. Estimated current earnings, 1942 (exclusive of earnings on Gov'ts)	979	23	166	126	98	35	35	180	35	29	169	18	75
2. Estimated earnings on Gov't securities to Nov. 30	44,632	3,300	12,158	3,437	4,278	2,748	1,946	5,572	2,156	1,267	1,984	1,737	4,049
3. Total	45,611	3,323	12,324	3,563	4,376	2,783	1,981	5,752	2,191	1,286	2,153	1,755	4,124
E. Excess of "C" over "D3"	981	93	57	40	25	132	75	172	57	7	56	53	214
F. Allocation required (on basis of 1.499086% earnings rate on Gov'ts) to produce earnings December equal to "E"	770,506	73,045	44,769	31,417	19,636	103,677	58,907	135,094	44,769	5,498	43,984	41,628	168,082
G. Average daily participations, per cent, in System Account since June 30, 1936	100.	7.3105	28.6913	8.1910	9.9020	5.4282	4.2193	11.4361	4.6017	3.0307	4.7852	3.8536	8.5174
H. Allocation of remainder of System holdings (\$4,929,329,000 less \$770,506,000) on basis of "G"	4,158,823	304,031	1,193,220	310,639	411,807	225,719	176,721	475,607	191,501	126,042	199,008	160,264	354,224
I. Total allocation of Government securities	4,929,329	377,076	1,237,989	372,066	431,443	329,426	235,628	610,701	236,270	131,540	242,992	201,892	522,306
J. Present allocations	4,929,329	388,474	1,299,122	381,666	455,378	316,161	222,265	596,076	237,809	135,005	226,221	192,101	479,051
K. Change in allocations	--	-11,398	-61,133	-9,600	-23,935	+13,265	+13,363	+14,625	-1,539	-3,465	+16,771	+9,791	+43,255

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REC'D IN RECORDS SECTION
APR 19 1968
333,343

*Vance ✓
D. ✓
Mrs. Smith*

FEDERAL RESERVE BANK
OF NEW YORK

November 2, 1942.

Dear Mr. Smead:

We received your letter of October 31 and have today sent to the Reserve banks a copy of the computation showing the adjustments to be made as of November 1 in participations in the System Open Market Account today, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on December 18, 1940.

Enclosed herewith is a copy of the letter of transmittal together with three copies of the computation, also copy of the telegram which was sent to each of the Federal Reserve banks on October 31.

Yours faithfully,

Robert G. Rouse
Robert G. Rouse,
Manager, System Open
Market Account.

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

Encls. 5.

Directive #1

DECLASSIFIED
Authority E.O. 12958

MISC 140A 75M-12-41

FEDERAL RESERVE BANK OF NEW YORK

November 2, 1942.

Dear Mr. Leach:

In accordance with my telegram of October 31, I enclose herewith computation of the readjustments to be made today as of November 1, of the participations of the Federal Reserve banks in the System Open Market portfolio.

Yours faithfully,

Robert G. Rouse,
Manager, System Open
Market Account.

Mr. Hugh Leach, President,
Federal Reserve Bank of Richmond,
Richmond, Virginia.

Enc.
RHB:HS

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DECLASSIFIED Authority E.O. 12958

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SEC-RHB/JM/MH

October 31, 1942

PLEASE SEND THE FOLLOWING TELEGRAM TO PRESIDENT OF EACH FEDERAL RESERVE BANK AS INDICATED BELOW:

In accordance with action of the Federal Open Market Committee at its meeting September 28, 1942, a readjustment of participations in Government securities held in the System Account is called for on November 1 under the plan for reallocation of Government securities adopted by the Federal Open Market Committee December 18, 1940.

The computations showing adjustments to be made in participations of the several Federal Reserve banks on November 1 will be mailed to all Reserve banks on November 2. These computations indicate an increase of _____ or decrease of _____ in your participation on November 1. We shall wire you on November 2, 1942 the detailed entries to be made as of November 1.

		<u>INCREASE</u>	<u>DECREASE</u>
PADDOCK	BOSTON	\$23,988,000	-
WILLIAMS	PHILADELPHIA	-	\$ 872,000
FLEMING	CLEVELAND	4,783,000	-
LEACH	RICHMOND	2,697,000	-
McLARIN	ATLANTA	-	1,003,000
YOUNG	CHICAGO	-	5,122,000
DAVIS	ST. LOUIS	6,340,000	-
PEYTON	MINNEAPOLIS	1,263,000	-
LEEDY	KANSAS CITY	-	3,120,000
GILBERT	DALLAS	-	3,155,000
DAY	SAN FRANCISCO	6,487,000	-

ROUSE

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT, NOVEMBER 1, 1942
(In thousands of dollars)

	System	Boston	New York	Phila- dolphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minne- apolis	Kansas City	Dallas	San Francisco
A. Expenses													
1. Estimated current ex- penses, 1942	37,326	2,822	9,103	2,862	3,487	2,518	1,711	4,872	1,951	1,097	1,882	1,508	3,513
B. Estimated dividends, 1942	8,666	566	3,184	708	888	348	303	954	269	183	280	266	717
C. Estimated expenses and divi- dends, 1942	45,992	3,388	12,287	3,570	4,375	2,866	2,014	5,826	2,220	1,280	2,162	1,774	4,230
D. Earnings													
1. Estimated current earnings, 1942 (exclusive of earnings on Gov'ts)	988	24	166	128	99	36	35	181	34	20	171	19	75
2. Estimated earnings on Gov't securities to Oct. 31	38,837	2,843	10,639	2,992	3,747	2,374	1,685	4,859	1,875	1,109	1,720	1,512	3,482
3. Total	39,825	2,867	10,805	3,120	3,846	2,410	1,720	5,040	1,909	1,129	1,891	1,531	3,557
E. Excess of "C" over "D3"	6,167	521	1,482	450	529	456	294	786	311	151	271	243	673
F. Allocation required (on basis of 1.474505% earnings rate on Gov'ts) to produce earnings November-December equal to "E"	2,502,597	211,424	601,402	182,612	214,671	185,047	119,307	318,962	126,205	61,276	109,973	98,611	273,107
G. Average daily participations, per cent, in System Account since June 30, 1936	100.	7.2958	28.7514	8.2025	9.9190	5.4029	4.2426	11.4193	4.5990	3.0382	4.7903	3.8525	8.4865
H. Allocation of remainder of System holdings (\$4,559,038,000 less \$2,502,597,000) on basis of "G"	2,056,441	150,034	591,256	168,680	203,978	111,107	87,246	234,831	94,576	62,479	98,510	79,224	174,520
I. Total allocations of Government securities	4,559,038	361,458	1,192,658	351,292	418,649	296,154	206,553	553,793	220,781	123,755	208,483	177,835	447,627
J. Present allocation	4,559,038	337,470	1,224,944	352,164	413,866	293,457	207,556	558,915	214,441	122,492	211,603	180,990	441,440
K. Change in allocations	--	+23,988	-32,286	-372	+4,783	+2,697	-1,003	-5,122	+6,340	+1,263	-3,120	-3,155	+6,187

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Authority E.O. 12958

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Form F. R. 148 b

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 NOV 2 1942
 338-343

TELEGRAM
BOARD OF GOVERNORS
 OF THE
FEDERAL RESERVE SYSTEM
 LEASED WIRE SERVICE
 WASHINGTON

October 31, 1942.

Route - New York

This will confirm understanding in telephone conversation that adjustments of participations in System Account will be as follows, in thousands of dollars:

Increases:

Boston	23,988
Cleveland	4,783
Richmond	2,697
St. Louis	6,340
Minneapolis	1,263
San Francisco	6,487

Decreases:

New York	32,286
Philadelphia	872
Atlanta	1,003
Chicago	5,122
Kansas City	3,120
Dallas	3,155

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SM **FILE COPY** *Smead*

For Files
 S. E. Haizer

DECLASSIFIED
 Authority E.O. 12958

FILED IN FILES SECTION

NOV 2 1942

October 31, 1942.

Mr. Robert G. Rouse, Vice President,
 Federal Reserve Bank of New York,
 New York, New York.

Dear Mr. Rouse:

There is enclosed a statement prepared in this Division showing the changes necessary in allocations of Government securities in the System Open Market Account on November 1, 1942, prepared in accordance with the formula adopted by the Federal Open Market Committee on December 18, 1940.

Current earnings, exclusive of earnings on Government securities, and current expenses have been estimated by multiplying the actual amounts thereof January through September by one and one-third. Estimates obtained on this basis have been adjusted in the same manner as for the previous reallocations this year; namely, by adding \$180,000 to current expenses at New York to cover extraordinary depreciation charges on air-conditioning equipment and by deducting from current earnings estimated net earnings on industrial advances and commitments attributable to funds received from the Secretary of the Treasury. Estimated earnings on Treasury bills held by the Reserve Banks under resale option have been included in the figures for item "D2", estimated earnings on Government securities to October 31.

Very truly yours,

E. L. Smead, Chief,
 Division of Bank Operations.

Enclosure

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NOV 2 1942
 E. L. Smead

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT, NOVEMBER 1, 1942
(In thousands of dollars)

NOV 2 1942

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minne- apolis	Kansas City	Dallas	San Francisco
A. Expenses													
1. Estimated current ex- penses, 1942	37,326	2,822	9,103	2,862	3,487	2,518	1,711	4,872	1,951	1,097	1,882	1,508	3,513
2. Estimated dividends, 1942	8,666	566	3,184	708	888	348	303	954	269	183	280	266	717
3. Estimated expenses and divi- dends, 1942	45,992	3,388	12,287	3,570	4,375	2,866	2,014	5,826	2,220	1,280	2,162	1,774	4,230
D. Earnings													
1. Estimated current earnings, 1942 (exclusive of earnings on Gov'ts)	988	24	166	128	99	36	35	181	34	20	171	19	75
2. Estimated earnings on Gov't securities to Oct. 31	38,837	2,843	10,639	2,992	3,747	2,374	1,685	4,859	1,875	1,109	1,720	1,512	3,482
3. Total	39,825	2,867	10,805	3,120	3,846	2,410	1,720	5,040	1,909	1,129	1,891	1,531	3,557
E. Excess of "C" over "D3"	6,167	521	1,482	450	529	456	294	786	311	151	271	243	673
F. Allocation required (on basis of 1.474505% earnings rate on Gov'ts) to produce earnings November-December equal to "E"	2,502,997	211,424	601,402	182,612	214,671	185,047	119,307	318,962	126,205	61,276	109,973	98,611	273,107
G. Average daily participations, per cent, in System Account since June 30, 1936	100.	7.2958	28.7514	8.2025	9.9190	5.4029	4.2426	11.4193	4.5990	3.0382	4.7903	3.8525	8.4865
H. Allocation of remainder of System holdings (\$4,559,038,000 less \$2,502,997,000) on basis of "G"	2,056,441	150,034	591,256	168,680	203,978	111,107	87,246	234,831	94,576	62,479	98,510	79,224	174,520
I. Total allocations of Government securities	4,559,038	361,458	1,192,658	351,292	418,649	296,154	206,553	553,793	220,781	183,755	208,483	177,835	447,627
J. Present allocation	4,559,038	337,470	1,224,944	352,164	413,866	293,457	207,556	558,915	214,441	122,492	211,603	180,990	441,140
K. Change in allocations	--	+23,988	-32,286	-872	+4,783	+2,697	-1,003	-5,122	+6,340	+1,263	-3,120	-3,155	+6,487

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Authority E.O. 12958

W. M. J. 3. W.

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Authority E.O. 12958

FILED IN FILES SECTION
OCT 5 1942

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON



ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

October 3, 1942.

Dear Sir:

This letter is for the purpose of formally advising you of the decision reached by the Federal Open Market Committee at its meeting on September 28, 1942, at which all of the Presidents were in attendance, to change the present procedure with respect to the allocation of securities in the System open market account to provide, in addition to the four quarterly allocations, for allocations as of November 1 and December 1 of each year on the same basis as the quarterly allocations are now being made.

As you know, this change, which will take effect during the last quarter of this year, is for the purpose of effecting a more even distribution among the 12 Federal Reserve Banks, in relation to their expenses, of the earnings during a calendar year on the securities in the System account.

Very truly yours,

Chester Morrill

Chester Morrill, Secretary,
Federal Open Market Committee.

TO THE PRESIDENTS OF ALL FEDERAL RESERVE BANKS



*Orig. filed
FOMC - General*

DECLASSIFIED
Authority E.O. 12958

*Mr. [unclear]
Mr. [unclear]
Mr. Smith*

REC'D IN RECORDS SECT.
APR 19 1968
338,342

FEDERAL RESERVE BANK
OF NEW YORK

October 1, 1942.

Dear Mr. Smead:

We received your letter of September 29 and have today sent to the Reserve banks a copy of the computation showing the adjustments to be made in participations in the System Open Market Account today, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on December 18, 1940.

Enclosed herewith is a copy of the letter of transmittal together with three copies of the computation, also copy of the telegram which was sent to each of the Federal Reserve banks yesterday.

Yours faithfully,

Robert G. Rouse
Robert G. Rouse,
Manager, System Open
Market Account.

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

Encls. 5.

Director #1

DECLASSIFIED
Authority E.O. 12958

140.B-18M-6-41

October 1, 1942

Dear Mr. Williams:

In accordance with my telegram of yesterday, I enclose herewith computation of the readjustments to be made today of the participations of the Federal Reserve banks in the System Open Market portfolio.

Yours faithfully,

Robert G. Rouse,
Manager, System Open
Market Account.

Mr. Alfred H. Williams, President,
Federal Reserve Bank of Philadelphia,
Philadelphia, Pa.

Enc.

RHB:RS

DECLASSIFIED

Authority E.O. 12958

40.B-18M-5-41

SECURITIES DEPT
RHS:HS

September 30, 1942

PLEASE SEND THE FOLLOWING TELEGRAM TO EACH FEDERAL RESERVE BANK AS INDICATED BELOW:

Under the plan for reallocation of Government securities adopted by the Federal Open Market Committee December 18, 1940, a readjustment of participations in Government securities held in the System Account is called for October 1, 1942. The computations showing adjustments to be made in participations of the several Federal Reserve banks will be mailed to all Reserve banks tomorrow. These computations indicate an ^{increase} of _____ in your participation on October 1. We ^{decrease} shall wire you on October 1, 1942; the detailed entries to be made on that date.

		<u>INCREASE</u>	<u>DECREASE</u>
PADDOCK	BOSTON	\$11,113,000	-
WILLIAMS	PHILADELPHIA	4,692,000	-
FLEMING	CLEVELAND	-	18,280,000
LEACH	RICHMOND	25,088,000	-
McLAREN	ATLANTA	11,411,000	-
YOUNG	CHICAGO	-	8,594,000
DAVIS	ST. LOUIS	-	8,175,000
PEYTON	MINNEAPOLIS	-	4,005,000
LEROY	KANSAS CITY	5,970,000	-
GILBERT	DALLAS	4,807,000	-
DAY	SAN FRANCISCO	31,328,000	-

ROUSE

DECLASSIFIED
 Authority E.O. 12958

REC'D IN FILES SECTION
 SEP 30 1942

Form F. R. 148 b

TELEGRAM
BOARD OF GOVERNORS
 OF THE
FEDERAL RESERVE SYSTEM
 LEASED WIRE SERVICE
 WASHINGTON

September 30, 1942.

Rouse - New York

This will confirm understanding in telephone conversation that adjustments of participations in System account in thousands of dollars will be as follows:

Increases:

Boston	11,113
Philadelphia	4,692
Richmond	25,088
Atlanta	11,411
Kansas City	5,970
Dallas	4,807
San Francisco	31,328

Decreases:

New York	55,355
Cleveland	18,280
Chicago	8,594
St. Louis	8,175
Minneapolis	4,005

EMBAD

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MD 49
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 Federal Reserve Bank of St. Louis

DECLASSIFIED
Authority E.O. 12958

NO IN FILES SECTION
OCT 1 1942

September 29, 1942.

Mr. Robert G. Rouse, Vice President,
Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Rouse:

There is enclosed a statement prepared in this Division showing the changes necessary in allocations of Government securities in the System Open Market Account on October 1, 1942, prepared in accordance with the formula adopted by the Federal Open Market Committee on December 18, 1940.

Current earnings, exclusive of earnings on Government securities, and current expenses have been estimated by multiplying the actual amounts thereof January through August by 1.5. Estimates obtained on this basis have been adjusted in the same manner as for the previous reallocations this year, namely, the addition of \$150,000 to current expenses at New York to cover extraordinary depreciation charges on air-conditioning equipment and the deduction from current earnings of estimated net earnings on industrial advances and commitments attributable to funds received from the Secretary of the Treasury.

Very truly yours,

E. L. Smead, Chief,
Division of Bank Operations.

Enclosure

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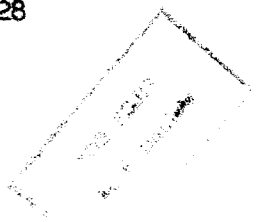
REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT, OCTOBER 1, 1942

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A. Expenses													
(1) Estimated current expenses, 1942	36,962	2,738	9,068	2,838	3,440	2,495	1,702	4,844	1,915	1,085	1,872	1,501	3,464
B. Estimated dividends, 1942	8,665	566	3,184	708	888	348	302	954	269	183	280	266	717
C. Estimated expenses and dividends, 1942	45,627	3,304	12,252	3,546	4,328	2,843	2,004	5,798	2,184	1,268	2,152	1,767	4,181
D. Earnings													
(1) Estimated current earnings, 1942 (exclusive of earnings on Gov'ts)	998	25	162	131	99	37	37	193	32	22	171	17	72
(2) Estimated earnings on Gov't securities to Sept. 30	33,887	2,477	9,325	2,616	3,308	2,048	1,458	4,234	1,640	980	1,492	1,316	2,993
(3) Total	34,885	2,502	9,487	2,747	3,407	2,085	1,495	4,427	1,672	1,002	1,663	1,333	3,065
E. Excess of "C" over "D(3)"	10,742	802	2,765	799	921	758	509	1,371	512	266	489	434	1,116
F. Allocation required (on basis of 1.48128% earnings rate on Gov'ts to produce earnings October-December equal to "E")	2,877,116	214,806	740,572	214,002	246,679	203,021	136,330	367,206	137,133	71,245	130,973	116,242	298,907
G. Average daily participations, per cent, in System account since June 30, 1936	100.	7.2931	28.7987	8.2145	9.9402	5.3769	4.2348	11.3982	4.5964	3.0170	4.7940	3.8196	8.4566
Allocation of remainder of System holdings (\$3,358,765,000 less \$2,877,116,000) on basis of "G"	481,649	35,127	138,709	39,565	47,877	25,898	20,397	54,899	22,139	14,676	23,090	18,541	40,731
I. Total allocations of Government securities	3,358,765	249,933	879,281	253,567	294,556	228,919	156,727	422,105	159,272	85,921	154,063	134,783	339,638
J. Present allocations	3,358,765	238,820	934,636	248,875	312,836	203,831	145,316	430,699	167,447	89,926	148,093	129,976	308,310
K. Change in allocations	--	+11,113	-55,355	+4,692	-18,280	+25,088	+11,411	-8,594	-8,175	-4,005	+5,970	+4,807	+31,328

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REC'D IN FILES SECTION
 AUG 27 1942
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August 26, 1942

Mr. Smead

System Open Market allocations.

Mr. Van Fossen

*not sent to file
 per
 8/27/42*

Referring to your pencil memorandum, I do not find anything in the report of the Committee on Self Insurance in regard to the treatment of losses on Government securities sold. The present procedure, of course, is to allocate any losses in proportion to average participations in the System Open Market account since June 30, 1936, i.e., on the same basis on which profits are allocated.

The present procedure regarding quarterly allocations and the treatment of profits and losses was adopted on December 18, 1940 by the Federal Open Market Committee at a meeting at which all of the Presidents of the Federal Reserve Banks were in attendance. According to the Board's letter of December 27, 1940, approval of the new procedure was given by the Presidents as well as by the Federal Open Market Committee. Presumably any proposed change should have the approval of the Federal Open Market Committee.

As I recall there was an understanding with Mr. Rouse and Mr. Miller that if in the last quarter of any year it appears that there was a likelihood that any Federal Reserve Bank would not have current net earnings sufficient to cover expenses and dividends, there would be special reallocations of the System Open Market account on November 1 and December 1. There is no present likelihood of any such situation arising and, accordingly, there does not appear to be any necessity for a reallocation during the current calendar year subsequent to the forthcoming October 1 reallocation. It is believed, however, that it would be desirable to get as accurate an estimate of probable expenses during the last four months of the year for use in this reallocation as is practicable. We could, of course, ask the Federal Reserve Banks again, as we did last year, to give us an estimate of such expenses. I believe, however, we can do just as good a job and perhaps a better one on the basis of actual expenses to the end of August. The usual procedure is to add 50 per cent to expenses at the end of August to obtain the estimated expenses for use in the October 1 reallocation. In view of the continued increase in expenses during the present year, I believe it would be preferable on this occasion to use expenses to the end of August plus expenses for the four months May to August inclusive. Inasmuch as the method of estimating expenses has not been approved by the Open Market Committee, it is, of course, possible for you and Mr. Rouse to adopt any method of estimating expenses without submitting it to the Open Market Committee for approval.

It is suggested that you discuss this matter with Mr. Rouse at the meeting in New York next week and if it is decided to have reallocations on November 1 and December 1 that an appropriate recommendation be prepared for submission by you and Mr. Rouse to the Federal Open Market Committee at its next meeting.

W

VF:seh

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BOARD OF GOVERNORS
 OF THE
 FEDERAL RESERVE SYSTEM

REC'D IN RECORDS SECTION
 APR 9 1968
 Date August 26, 1942

Office Correspondence

To Mr. Smead

Subject: System Open Market allocations.

From Mr. Van Fossen

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Referring to your pencil memorandum, I do not find anything in the report of the Committee on Self Insurance in regard to the treatment of losses on Government securities sold. The present procedure, of course, is to allocate any losses in proportion to average participations in the System Open Market account since June 30, 1936, i.e., on the same basis on which profits are allocated.

The present procedure regarding quarterly allocations and the treatment of profits and losses was adopted on December 18, 1940 by the Federal Open Market Committee at a meeting at which all of the Presidents of the Federal Reserve Banks were in attendance. According to the Board's letter of December 27, 1940, approval of the new procedure was given by the Presidents as well as by the Federal Open Market Committee. Presumably any proposed change should have the approval of the Federal Open Market Committee.

As I recall there was an understanding with Mr. Rouse and Mr. Miller that if in the last quarter of any year it appears that there was a likelihood that any Federal Reserve Bank would not have current net earnings sufficient to cover expenses and dividends, there would be special reallocations of the System Open Market account on November 1 and December 1. There is no present likelihood of any such situation arising and, accordingly, there does not appear to be any necessity for a reallocation during the current calendar year subsequent to the forthcoming October 1 reallocation. It is believed, however, that it would be desirable to get as accurate an estimate of probable expenses during the last four months of the year for use in this reallocation as is practicable. We could, of course, ask the Federal Reserve Banks again, as we did last year, to give us an estimate of such expenses. I believe, however, we can do just as good a job and perhaps a better one on the basis of actual expenses to the end of August. The usual procedure is to add 50 per cent to expenses at the end of August to obtain the estimated expenses for use in the October 1 reallocation. In view of the continued increase in expenses during the present year, I believe it would be preferable on this occasion to use expenses to the end of August plus expenses for the four months May to August inclusive. Inasmuch as the method of estimating expenses has not been approved by the Open Market Committee, it is, of course, possible for you and Mr. Rouse to adopt any method of estimating expenses without submitting it to the Open Market Committee for approval.

It is suggested that you discuss this matter with Mr. Rouse at the meeting in New York next week and if it is decided to have reallocations on November 1 and December 1 that an appropriate recommendation be prepared for submission by you and Mr. Rouse to the Federal Open Market Committee at its next meeting.

FOR FILE
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*Notes
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333,343

*Van ✓
D ✓
Mrs. Smith*

FEDERAL RESERVE BANK
OF NEW YORK

June 30, 1942

Dear Mr. Smead:

We received your letter of June 29 and have today sent to the Reserve banks a copy of the computation showing the adjustments to be made in participations in the System Open Market Account on July 1, 1942, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on December 18, 1940.

Enclosed herewith is copy of the letter of transmittal together with three copies of the computation, also copy of the telegram which was sent to each of the Federal Reserve banks today.

Yours faithfully,

Robert G. Rouse
Robert G. Rouse,
Manager, System Open
Market Account.

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

Encls. 5.

Directive #1

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Authority E.O. 12958

MISC. 140A 75M-6-41

FEDERAL RESERVE BANK OF NEW YORK

June 30, 1942.

Dear Mr. Fleming:

In accordance with my telegram of today, I enclose herewith computation of the readjustments to be made on July 1, 1942 of the participations of the Federal Reserve banks in the System Open Market portfolio.

Yours faithfully,

~~Robert G. Rouse,
Manager, System Open
Market Account~~

Mr. M. J. Fleming, President,
Federal Reserve Bank of Cleveland,
Cleveland, Ohio.

Enc.

RHB:FD

DECLASSIFIED Authority E.O. 12958

SECURITIES DEPARTMENT
RHB:FD

June 30, 1942.

PLEASE SEND THE FOLLOWING TELEGRAM TO EACH FEDERAL RESERVE BANK AS INDICATED BELOW:

Under the plan for reallocation of Government securities adopted by the Federal Open Market Committee December 18, 1940, a readjustment of participations in Government securities held in the System Account is called for July 1, 1942. The computations showing adjustments to be made in participations of the several Federal Reserve banks is being mailed to all Reserve banks today. These computations indicate an increase of _____ in your participation decrease on July 1. However, these computations are based on holdings at close of business June 29, and are exclusive of purchases made for delivery today and tomorrow. Consequently our wire to you tomorrow will advise entries to be made on that day covering both the quarterly reallocation and additions to holdings since June 29.

		<u>Increase</u>	<u>Decrease</u>
Paddock	Boston	-	9,776,000
Williams	Philadelphia	-	20,519,000
Fleming	Cleveland	-	27,446,000
Leach	Richmond	9,761,000	-
McLarin	Atlanta	2,534,000	-
Young	Chicago	25,162,000	-
Davis	St. Louis	11,799,000	-
Peyton	Minneapolis	-	10,288,000
Leedy	Kansas City	3,082,000	-
Gilbert	Dallas	1,203,000	-
Day	San Francisco	21,231,000	-

ROUSE

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A. Expenses													
(1) Estimated current expenses, 1942	36,710	2,664	9,161	2,719	3,459	2,428	1,654	4,903	1,952	1,078	1,825	1,477	3,360
B. Estimated dividends, 1942	8,650	565	3,182	709	887	348	297	952	268	183	279	265	715
C. Estimated expenses and dividends, 1942	45,360	3,229	12,343	3,428	4,346	2,776	1,951	5,855	2,220	1,261	2,104	1,742	4,075
D. Earnings													
(1) Estimated current earnings, 1942 (exclusive of earnings on Gov'ts)	998	19	168	119	104	17	34	183	32	25	176	19	72
(2) Estimated earnings on Gov't securities to June 30	21,607	1,605	5,912	1,710	2,167	1,299	926	2,653	1,026	653	952	841	1,863
(3) Total	22,605	1,624	6,080	1,829	2,271	1,316	960	2,836	1,058	678	1,128	860	1,935
E. Excess of "C" over "D(3)"	22,755	1,605	6,263	1,629	2,075	1,130	991	3,019	1,162	583	976	882	2,140
F. Allocation required (on basis of 1.73983% earnings rate on Gov'ts) to produce earnings July-December equal to "E"	2,594,463	182,998	711,090	185,734	236,586	163,045	112,991	341,218	132,488	66,472	111,281	100,563	243,997
G. Average daily participations, per cent in System account since June 30, 1936	100.	7.3037	28.8556	8.2614	9.9764	5.3365	4.2295	11.3119	4.5737	3.0686	4.8167	3.8184	8.4146
H. Allocation of remainder of System holdings (\$2,617,083,000 less \$2,594,463,000) on basis of "G"	22,620	1,652	6,527	1,869	2,257	1,207	957	2,559	1,035	694	1,089	871	1,903
I. Total allocation of Government securities ("F" plus "H")	2,617,083	184,650	720,617	187,603	238,843	164,252	113,948	343,777	133,523	67,166	112,370	101,434	245,900
J. Present allocations	2,617,083	194,426	727,360	208,122	266,289	154,191	111,414	321,615	121,724	77,154	109,288	100,231	221,669
K. Change in allocations	--	-9,776	-6,743	-20,519	-27,446	+9,761	+2,534	+25,162	+11,799	-10,288	+3,082	+1,203	+21,231

NOTE: Computations are based on holdings in the Account June 29, 1942.

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June 29, 1942.

Mr. Robert G. Rouse, Vice President,
Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Rouse:

There is enclosed a statement prepared in this Division showing the changes necessary in allocations of Government securities in the System Open Market Account on July 1, 1942, prepared in accordance with the formula adopted by the Federal Open Market Committee on December 18, 1940.

Current earnings, exclusive of earnings on Government securities, and current expenses have been estimated by multiplying the actual amounts thereof January through May by 2.4. Estimates obtained on this basis have been adjusted in the same manner as for the January 1 and April 1 reallocations, namely, the addition of \$480,000 to current expenses at New York to cover extraordinary depreciation charges on air-conditioning equipment and the deduction from current earnings of estimated net earnings on industrial advances and commitments attributable to funds received from the Secretary of the Treasury.

Very truly yours,

E. L. Smead, Chief,
Division of Bank Operations.

Enclosure

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(In thousands of dollars)

RECORDED IN FILES SECTION 2

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A. Expenses													
(1) Estimated current expenses, 1942	36,710	2,664	9,161	2,749	3,459	2,428	1,654	4,903	1,952	1,078	1,825	1,477	3,360
(2) Estimated dividends, 1942	8,650	565	3,182	709	887	348	297	952	268	183	279	265	715
C. Estimated expenses and dividends, 1942	45,360	3,229	12,343	3,458	4,346	2,776	1,951	5,855	2,220	1,261	2,104	1,742	4,075
D. Earnings													
(1) Estimated current earnings, 1942 (exclusive of earnings on Gov'ts)	998	19	168	119	104	47	34	183	32	25	176	19	72
(2) Estimated earnings on Gov't securities to June 30	21,607	1,605	5,912	1,710	2,167	1,299	926	2,653	1,026	653	952	841	1,863
(3) Total	22,605	1,624	6,080	1,829	2,271	1,346	960	2,836	1,058	678	1,128	860	1,935
E. Excess of "C" over "D(3)"	22,755	1,605	6,263	1,629	2,075	1,430	991	3,019	1,162	583	976	882	2,140
F. Allocation required (on basis of 1.73983% earnings rate on Gov'ts) to produce earnings July-December equal to "E"	2,594,463	182,998	714,090	185,734	236,586	163,045	112,991	344,218	132,488	66,472	111,281	100,563	243,997
G. Average daily participations, per cent, in System account since June 30, 1936	100.	7.3037	28.8556	8.2614	9.9764	5.3365	4.2295	11.3149	4.5737	3.0686	4.8167	3.8184	8.4146
H. Allocation of remainder of System holdings (\$2,617,083,000 less \$2,594,463,000) on basis of "G"	22,620	1,652	6,527	1,869	2,257	1,207	957	2,559	1,035	694	1,089	871	1,903
I. Total allocation of Government securities ("F" plus "H")	2,617,083	184,650	720,617	187,603	238,843	164,252	113,948	346,777	133,523	67,166	112,370	101,434	245,900
J. Present allocations	2,617,083	194,426	727,360	208,122	266,289	154,491	111,414	321,615	121,724	77,454	109,288	100,231	224,669
K. Change in allocations	-	-9,776	-6,743	-20,519	-27,446	+9,761	+2,534	+25,162	+11,799	-10,288	+3,082	+1,203	+21,231

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*Value
of
Smead*

FEDERAL RESERVE BANK
OF NEW YORK

March 30, 1942.

Dear Mr. Smead:

We received your letter of March 28 and have today sent to the Reserve banks a copy of the computation showing the adjustments to be made in participations in the System Open Market Account on April 1, 1942, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on December 18, 1940.

Enclosed herewith is copy of the letter of transmittal together with three copies of the computation, also copy of the telegram which was sent to each of the Federal Reserve banks today.

Yours faithfully,

Robert G. Rouse
Robert G. Rouse,
Manager, System Open
Market Account.

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

Encls. (5).

Director #1

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MISC. 140A 75M-5-41

FEDERAL RESERVE BANK OF NEW YORK

March 30, 1942

Dear Mr. Day:

In accordance with my telegram of today, I enclose herewith computation of the readjustments to be made on April 1, 1942 of the participations of the Federal Reserve banks in the System Open Market portfolio.

Yours faithfully,

Robert G. Rouse,
Manager, System Open
Market Account.

Mr. W. A. Day, President,
Federal Reserve Bank of San Francisco,
San Francisco, Calif.

Enc.
RHB:HS

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SECURITY FILE DEPT.
 RAB:FD

March 30, 1942.

Please send the following telegram to each Federal Reserve Bank as indicated below:

Under the plan for reallocation of Government securities adopted by the Federal Open Market Committee December 18, 1940, a readjustment of participations in Government securities held in the System Account is called for April 1, 1942. The computations showing adjustments to be made in participations of the several Federal Reserve Banks is being sent to all Reserve banks today. These computations indicate an increase or decrease of _____ in your participation on April 1. We shall wire you on April 1, 1942 the detailed entries to be made on that date.

		<u>Increase</u>	<u>Decrease</u>
Young	Boston	4,817,000	-
Williams	Philadelphia	71,000	-
Fleming	Cleveland	5,800,000	-
Leach	Richmond	5,315,000	-
McLarin	Atlanta	3,106,000	-
Young	Chicago	7,288,000	-
Davis	St. Louis	4,117,000	-
Peyton	Minneapolis	1,796,000	-
Leedy	Kansas City	-	5,375,000
Gilbert	Dallas	1,202,000	-
Day	San Francisco	-	249,000

HOUSE

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT
APRIL 1, 1942

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleveland	Richmond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A. Expenses													
1. Estimated current expenses, 1942	36,631	2,802	8,925	2,898	3,666	2,391	1,659	4,700	1,894	1,190	1,842	1,486	3,178
B. Earnings													
1. Estimated current earnings, 1942 (exclusive of earnings on Gov'ts)	1,059	57	158	116	94	44	42	186	36	24	175	22	85
2. Estimated earnings on Gov't securities to Mar. 31	10,625	782	2,933	839	1,051	635	452	1,292	502	321	486	414	918
3. Total	11,684	839	3,091	955	1,145	679	494	1,478	538	345	681	436	1,003
C. Excess of "A-1" over "B-3"	24,947	1,963	5,834	1,943	2,521	1,712	1,165	3,222	1,356	845	1,161	1,050	2,175
D. Allocation required (on basis of 1.90823% earnings rate on Gov'ts) to produce earnings Apr.-Dec. equal to "C"	1,735,189	136,537	405,784	135,145	175,348	119,078	81,032	224,106	94,317	58,774	80,753	73,033	151,282
E. Estimated dividends, 1942	8,592	564	3,133	711	886	345	296	950	267	132	278	265	715
F. Allocation of remainder of System holdings (\$2,244,236,000 less \$1,735,189,000) on basis of "E"	509,047	33,415	185,620	42,124	92,433	20,440	17,537	56,234	15,819	10,783	16,471	15,700	42,361
G. Total allocation of Gov't securities ("D" + "F")	2,244,236	169,952	591,404	177,269	227,841	139,518	98,569	280,340	110,136	69,557	97,224	88,733	193,643
H. Present allocations	2,244,236	165,135	619,452	177,198	221,961	134,203	95,463	273,102	106,019	67,761	102,599	87,451	193,892
I. Change in allocations	--	+4,817	-28,048	+71	+5,880	+5,315	+3,106	+7,238	+4,117	+1,796	-5,375	+1,282	-249

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IN FILE SECTION
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SECTION
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March 28, 1942.

Mr. Robert G. Rouse, Vice President,
Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Rouse:

There is enclosed a statement prepared in this Division showing the changes necessary in allocations of Government securities in the System Open Market Account on April 1, 1942, prepared in accordance with the formula adopted by the Federal Open Market Committee on December 18, 1940.

Current earnings, exclusive of earnings on Government securities, and current expenses have been estimated by multiplying the actual amounts thereof October through February by 2.4. Estimates obtained on this basis have been adjusted in the same manner as was done in connection with the January 1 reallocation, namely, the addition of \$480,000 to current expenses at New York to cover extraordinary depreciation charges on air-conditioning equipment and the deduction from current earnings of estimated net earnings on industrial advances and commitments attributable to funds received from the Secretary of the Treasury.

Very truly yours,

E. L. Smead, Chief,
Division of Bank Operations.

Enclosure.

MD: **FILE COPY**

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT
APRIL 1, 1942

(In thousands of dollars)

	System	Boston	New York	Philadelphia	Cleveland	Richmond	Atlanta	Chicago	St. Louis	Minneapolis	Kansas City	Dallas	San Francisco
A. Expenses													
1. Estimated current expenses, 1942	36,631	2,802	8,925	2,898	3,666	2,391	1,659	4,700	1,894	1,190	1,842	1,486	3,178
B. Earnings													
1. Estimated current earnings, 1942 (exclusive of earnings on Gov'ts)	1,059	57	158	116	94	44	42	186	36	24	195	22	85
2. Estimated earnings on Gov't securities to Mar. 31	10,625	782	2,933	839	1,051	635	452	1,292	502	321	486	414	918
3. Total	11,684	839	3,091	955	1,145	679	494	1,478	538	345	681	436	1,003
C. Excess of "A-1" over "B-3"	24,947	1,963	5,834	1,943	2,521	1,712	1,165	3,222	1,356	845	1,161	1,050	2,175
D. Allocation required (on basis of 1.9082% earnings rate on Gov'ts) to produce earnings Apr.-Dec. equal to "C"	1,735,189	136,537	405,784	135,145	175,348	119,078	81,032	224,106	94,317	58,774	80,753	73,033	151,282
E. Estimated dividends, 1942	8,592	564	3,133	711	886	345	296	950	267	182	278	265	715
F. Allocation of remainder of System holdings (\$2,244,236,000 less \$1,735,189,000) on basis of "E"	509,047	33,415	135,620	42,124	52,493	20,440	17,537	56,284	15,819	10,783	16,471	15,700	42,361
G. Total allocation of Gov't securities ("D" + "F")	2,244,236	169,952	541,404	177,269	227,841	139,518	98,569	280,390	110,136	69,557	97,224	88,733	193,643
H. Present allocations	2,244,236	165,135	619,452	177,198	221,961	134,203	95,463	273,102	106,019	67,761	102,599	87,451	193,892
I. Change in allocations	--	+4,817	-28,048	+71	+5,880	+5,315	+3,106	+7,288	+4,117	+1,796	-5,375	+1,282	-249

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FEDERAL RESERVE BANK
OF NEW YORK

December 30, 1941

Dear Mr. Smead:

We received your letter of December 29 and have today sent to the Reserve banks a copy of the computation showing the adjustments to be made in participations in the System Open Market Account on January 2, 1942 as of January 1, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on December 18, 1940.

Enclosed herewith is copy of the letter of transmittal together with three copies of the computation, also copy of the telegram which was sent to each of the Federal Reserve banks today.

Yours faithfully,



Robert G. Rouse,
Manager, System Open
Market Account.

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

Encls. (5)

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SECURITIES DEPT.
REB:MS

December 30, 1941

Please send the following telegram to each Federal Reserve Bank as indicated below:

Under the plan for reallocation of Government securities adopted by the Federal Open Market Committee December 18, 1940, a readjustment of participations in Government securities held in the System Account is called for January 1, 1942. The computations showing adjustments to be made in participations of the several Federal Reserve Banks is being sent to all Reserve banks today. These computations indicate an increase of _____ in your participation on January 1. We shall advise you decrease on January 2, 1942 the detailed entries to be made on that date as of January 1.

		<u>Increase</u>	<u>Decrease</u>
Young	Boston	-	8,153,000
Williams	Philadelphia	66,000	-
Fleming	Cleveland	-	180,000
Leach	Richmond	-	2,993,000
Holarin	Atlanta	231,000	-
Young	Chicago	-	31,466,000
Davis	St. Louis	-	6,784,000
Peyton	Minneapolis	1,566,000	-
Looby	Kansas City	6,891,000	-
Gilbert	Dallas	9,155,000	-
Day	San Francisco	1,444,000	-

ROUSE

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MISC. 140A 75M-8-41

FEDERAL RESERVE BANK OF NEW YORK

December 30, 1941.

Dear Mr. Fleming:

In accordance with my telegram of today, I enclose herewith computation of the readjustments to be made on January 2, 1942, as of January 1, of the participations of the Federal Reserve banks in the System Open Market portfolio.

Yours faithfully,

Robert G. Rouse,
Manager, System Open
Market Account.

Mr. M. J. Fleming, President,
Federal Reserve Bank of Cleveland,
Cleveland, Ohio.

Encl.

CONFIDENTIAL

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON JANUARY 1, 1942

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	At- lanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A. Expenses													
Estimated current expenses, 1942	34,523	2,549	8,682	2,709	3,371	2,222	1,520	4,366	1,757	1,112	1,823	1,400	3,012
B. Estimated dividends, 1942	8,526	564	3,108	714	878	342	293	935	264	180	276	262	710
C. Estimated expenses and dividends, 1942	43,049	3,113	11,790	3,423	4,249	2,564	1,813	5,301	2,021	1,292	2,099	1,662	3,722
D. Estimated earnings, 1942 (exclusive of earnings on Gov'ts)	1,016	20	191	105	92	49	25	184	35	23	178	21	90
E. Excess of "C" over "D"	42,033	3,093	11,599	3,318	4,157	2,515	1,788	5,117	1,986	1,269	1,921	1,638	3,632
F. Allocation required (on basis of 1.88225% earning rate on Gov'ts) to produce earnings equal to "E"	2,233,125	164,325	616,230	176,278	220,853	133,617	94,993	271,855	105,512	67,419	102,059	87,021	192,060
G. Allocation of remainder of System holdings (\$2,254,475,000 less \$2,233,125,000) on basis of average daily participations in System Account since June 30, 1936	21,350	1,557	6,189	1,770	2,129	1,127	902	2,397	973	656	1,036	821	1,793
H. Total allocation of Gov'ts	2,254,475	165,882	622,419	178,048	222,982	134,744	95,895	274,252	106,485	68,075	103,095	87,845	194,753
I. Present allocations	2,254,475	174,035	592,196	177,982	223,162	137,737	95,664	305,718	113,269	66,509	96,204	78,690	193,309
J. Change in allocations	--	-8,153	+30,223	+ 66	-180	-2,993	+231	-31,466	-6,784	+1,566	+6,891	+9,155	+ 1,444

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MAIL ROOM SECTION
DEC 29 1941

December 29, 1941.

Mr. R. G. Rouse, Vice President,
Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Rouse:

There is enclosed a copy of the statement prepared in this Division showing the changes necessary in allocations of Government securities in the System Open Market Account on January 1, 1942, prepared in accordance with the formula adopted by the Federal Open Market Committee on December 18, 1940.

Current earnings, exclusive of earnings on Government securities, and current expenses have been estimated by multiplying the actual amounts thereof from July through November by 2.4. To the estimates of current expenses obtained on this basis we have added \$480,000 for New York to cover extra depreciation charges on air-conditioning equipment. We have adjusted the estimates of current earnings obtained on this basis by deducting estimated net earnings on industrial advances and commitments attributable to funds received from the Secretary of the Treasury, which of course are not available to cover Bank expenses, dividends, or transfers to Section 7 surplus.

Very truly yours,

E. L. Smead, Chief,
Division of Bank Operations.

Enclosure

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MD: th

CONFIDENTIAL

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON JANUARY 1, 1942

REC'D IN FILES SECTION
DEC 30 1941

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	At- lanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A. Expenses													
Estimated current expenses, 1942	34,523	2,519	8,682	2,709	3,371	2,222	1,520	4,366	1,757	1,112	1,823	1,100	3,012
B. Estimated dividends, 1942	8,526	564	3,108	714	878	342	293	935	264	180	276	262	710
C. Estimated expenses and dividends, 1942	43,049	3,113	11,790	3,423	4,249	2,564	1,813	5,301	2,021	1,292	2,099	1,662	3,722
Estimated earnings, 1942 (exclusive of earnings on Gov'ts)	1,016	20	191	105	92	49	85	184	35	23	178	24	90
D. Excess of "C" over "D"	42,033	3,093	11,599	3,318	4,157	2,515	1,728	5,117	1,986	1,269	1,921	1,638	3,632
F. Allocation required (on basis of 1.8822% earning rate on Gov'ts) to produce earnings equal to "D"	2,233,125	164,325	616,230	176,278	220,853	133,617	94,993	271,855	105,512	67,419	102,099	87,024	192,960
G. Allocation of remainder of System holdings (\$2,251,175,000 less \$2,233,125,000) on basis of average daily participations in System Account since June 30, 1936	21,350	1,557	6,189	1,770	2,129	1,127	902	2,397	973	656	1,036	821	1,793
H. Total allocation of Gov'ts	2,251,175	165,882	622,419	178,048	222,982	134,744	95,895	274,252	106,485	68,075	103,095	87,845	194,753
I. Present allocations	2,251,175	174,035	592,196	177,982	223,162	137,737	95,664	305,718	113,269	66,509	96,204	78,690	193,309
J. Change in allocations	--	-8,153	+30,223	+66	-180	-2,993	+231	-31,466	-6,784	+1,566	+6,891	+9,155	+1,444

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Advised
John
JAN 1 1942
FEDERAL RESERVE BANK OF ST. LOUIS

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TELEGRAM
Board of Governors
of the
Federal Reserve System
Leased Wire Service
Received at Washington, D. C.

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1941 DEC 29 PM 4 14
REC'D IN FILES SECTION
DEC 30 1941
FR

W28WASH B361 BOS 29-351P
MORRILL

to all FR Banks

YOUR WIRE DECEMBER 24. WE SEE NO OBJECTION TO OMITTING NET
EARNINGS ON INDUSTRIAL ADVANCES AND COMMITMENTS RE QUARTERLY
ALLOCATION OF GOVERNMENT SECURITIES

YOUNG.

FOR FILES
M. B. Daniels

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TELEGRAM
Board of Governors
of the
Federal Reserve System
Leased Wire Service
Received at Washington, D. C.

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DEC 30 1941
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12/24/41

W48WASH B271 NY 24-41 OP

MORRILL

12/24 to all FR Banks
ANSWERING YOUR WIRE WE APPROVE SUGGESTION EARNINGS ON INDUSTRIAL
ADVANCES AND COMMITMENTS BE OMITTED IN CALCULATION FOR
REALLOCATION OF GOVERNMENT ~~SECURITIES~~ SECURITIES
ROUNDS.

FOR FILES
M. B. Daniels

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TELEGRAM
Board of Governors
of the
Federal Reserve System
Leased Wire Service
Received at Washington, D. C.

1941 DEC 24

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REC'D IN FILES SECTION
DEC 28 1941

W28WASH C46 PHILA 24-251P
MORRILL

to all FR Banks

RETEL DECEMBER 24. THIS BANK IS IN FAVOR OF THE PROPOSED CHANGE IN
THE BASIS FOR QUARTERLY REALLOCATION OF GOVERNMENT SECURITIES.

DRINNEN.

FRASER
Mr. R. Drinnens

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Van

TELEGRAM
Board of Governors
of the
Federal Reserve System
Leased Wire Service
Received at Washington, D. C.

REC'D IN FILES SECTION
DEC 30 1941

1941 DEC 24 PM 2 06

W98WASH G253 CLEV 24-146

MORRILL

RETEL 24TH

12/24 to all Fed Banks

I HAVE NO OBJECTION TO ELIMINATION OF EARNINGS 13-B REFERRED TO
T IN YOUR TELEGRAM IN THE CONSIDERATION OF REALLOCATION OF
GOVERNMENT SECURITIES

FLEMING.

FILES
H. B. Daniels

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Van

TELEGRAM
Board of Governors
of the
Federal Reserve System
Leased Wire Service
Received at Washington, D. C.

REC'D IN FILES SECTION
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W91WASH RH 76 RICH 24-140

MORRILL

12/24 to all FR Banks

RETEL. SEE NO OBJECTION TO OMITTING ESTIMATED EARNINGS
ON INDUSTRIAL ADVANCES AND COMMITMENTS IN QUARTERLY
REALLOCATION OF GOVERNMENT SECURITIES

WALDEN.

FOR FILES
M. B. Daniels

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Van

TELEGRAM
Board of Governors
of the
Federal Reserve System
Leased Wire Service
Received at Washington, D. C.

Mr. Daniels

1941 DEC 24 PM 3 22
REC'D IN FILES SECTION
DEC 30 1941

W23WASH F122 38 ATLA 24-317P

MORRILL - BOARD

12/24 to all 11/13/41
AFTER CONSIDERATION OF YOUR WIRE ATLANTA OFFICERS FEEL THAT THE
PROPOSAL TO OMIT IN QUARTERLY REALLOCATION OF GOVERNMENT SECURITIES
THE NET EARNINGS ON INDUSTRIAL ADVANCES AND COMMITMENTS ATTRIBUTABLE
TO TREASURY FUNDS SHOULD BE ADOPTED

BRYAN.

FOR FILES
H. B. Daniels

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TELEGRAM
Board of Governors
of the
Federal Reserve System
Leased Wire Service
Received at Washington, D. C.

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DEC 30 1941
333 ● 345

1941 DEC 24 PM 4 05

W44WASH G405 CGO 24-245
MORRILL BOARD

12/24 to all FR Banks

RETEL YOUR WIRE THE PROCEDURE IN YOUR WIRE AS TO ESTIMATED EARNINGS ON
INDUSTRIAL ADVANCES AND COMMITMENTS MEETS WITH OUR APPROVAL. WITH
REFERENCE REALLOCATION OF SECURITIES WISH TO ADVISE THAT SALARY
ADJUSTMENTS WILL NOT BE EFFECTIVE UNTIL JANUARY 1 BUT WILL AMOUNT IN
AGGREGATE \$115,000

YOUNG.

FOR FILES
M. B. Daniels

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M. B. Daniels

TELEGRAM
Board of Governors
of the
Federal Reserve System
Leased Wire Service
Received at Washington, D. C.

1941 DEC 24 PM 3 30

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DEC 30 1941
233 ● 343

W30WASH G367 STL 24-155

MORRILL

NO OBJECTION TO CHANGE SUGGESTED IN WIRE TODAY *to all FR Banks* RELATIVE TO
OMITTING FIGURES IN CONNECTION WITH 13B ACTIVITIES FROM EARNINGS
IN ARRIVING AT BASIS FOR REALLOCATION OF GOVERNMENT SECURITIES

DAVIS.

FOR FILES
M. B. Daniels

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Van

TELEGRAM
Board of Governors
of the
Federal Reserve System
Leased Wire Service
Received at Washington, D. C.

W. Dineen

1941 DEC 24 PM 3 22

REC'D IN FILES SECTION
DEC 30 1941
333 ● 343

W22WASH G342 MPLS 24-147

MORRILL

to all FR Banks

RETEL 24 REALLOCATION WITH OMISSION OF EARNINGS OF INDUSTRIAL
ADVANCES AND COMMITMENTS SATISFACTORY TO US

PEYTON.

FOR FILES
M. B. Daniels

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TELEGRAM
Board of Governors
of the
Federal Reserve System
Leased Wire Service
Received at Washington, D. C.

1941 DEC 24 PM 3 24

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W25WASH G355 KC 24-201

MORRILL

12/24 to all FR Banks

REPLYING YOUR WIRE WE SEE NO OBJECTION TO SUGGESTED CHANGE
IN REALLOCATION OF GOVERNMENT SECURITIES BY ELIMINATING
ESTIMATED EARNINGS ON INDUSTRIAL ADVANCES AND COMMITMENTS
LEEDY.

FOR FILES
M. B. Daniels

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Van

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DEC 30 1941

W29WASH G364 DLS 24-2
MORRILL

TELEGRAM
Board of Governors
of the
Federal Reserve System
Leased Wire Service
Received at Washington, D. C.

1941 DEC 24 PM 5 30

4 all FRB's
REPLYING TELEGRAM DATE. ELIMINATION OF ESTIMATED EARNINGS ON
INDUSTRIAL ADVANCES AND COMMITMENTS IN DETERMINING
QUARTERLY REALLOCATIONS OF GOVERNMENT SECURITIES IS
ENTIRELY SATISFACTORY AND WE THINK PROPOSED CHANGE SHOULD
BECOME EFFECTIVE AT CLOSE OF YEAR

GILBERT.



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TELEGRAM
Board of Governors
of the
Federal Reserve System
Leased Wire Service
Received at Washington, D. C.

REC'D IN FILES SECTION
DEC 30 1941

1941 DEC 24 PM 4 04

W43WASH G401 SF 24-1224
BOARD

to all FR Banks
REPLYING YOUR WIRE DEC 24 UNDER PRESENT CONDITIONS NO
OBJECTION TO OMITTING EARNINGS ON INDUSTRIAL ADVANCES AND
COMMITMENTS FROM CONSIDERATION IN MAKING REALLOCATION OF
GOVERNMENT SECURITIES.

DAY.

FOR FILES
M. B. Daniels

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Form F. R. 148 b

TELEGRAM
BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
LEASED WIRE SERVICE
WASHINGTON

Young - Boston
Spreul - New York
Williams - Philadelphia
Fleming - Cleveland

Leach - Richmond
McLarin - Atlanta
Young - Chicago
Davis - St. Louis

Peyton - Minneapolis
Leedy - Kansas City
Gilbert - Dallas
Day - San Francisco

Under present procedure, total estimated earnings on industrial advances and commitments are taken into account in quarterly reallocation of Government securities. Since net earnings on industrial advances and commitments attributable to funds received from Treasury are not available to cover Bank expenses and dividends or for transfer to Section 7 Surplus, it has been suggested that reallocation would be more equitable if such earnings were omitted. Please advise whether you see any objection to change.

MERRILL

Appd.
MINUTES ON

DEC 24 1941
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ON BEHALF OF
Sumner
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FEDERAL RESERVE BANK
OF NEW YORK

September 29, 1941

Dear Mr. Smead:

We received your letter of September 27 and have today sent to the Reserve banks a copy of the computation showing the adjustments to be made in participations in the System Open Market Account on October 1, 1941, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on December 18, 1940.

Enclosed herewith is copy of the letter of transmittal together with three copies of the computation, also copy of the telegram which was sent to each of the Federal Reserve banks today.

Yours faithfully,

Robert G. Rouse
Robert G. Rouse,
Manager, System Open
Market Account.

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

Encls. (5)

Directive #

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FORM 140A 35M 1-40

FEDERAL RESERVE BANK OF NEW YORK

September 29, 1941.

Dear Mr. Gilbert:

In accordance with my telegram of today, I enclose herewith computation of the readjustments to be made on October 1, 1941, of the participations of the Federal Reserve banks in the System Open Market portfolio.

Yours faithfully,

Robert G. Rouse,
Manager, System Open
Market Account.

Mr. R. R. Gilbert, President,
Federal Reserve Bank of Dallas,
Dallas, Texas.

Enc.

DECLASSIFIED
 Authority E.O. 12958

MISC. 140A 18M 8-33

FEDERAL RESERVE BANK OF NEW YORK

SEC-RMB/JN

September 29, 1941

Please send the following telegram to each Federal Reserve Bank as indicated below:

Under the plan for reallocation of Government securities adopted by the Federal Open Market Committee December 18, 1940, a readjustment of participations in Government securities held in the System Account is called for October 1, 1941. The computations showing adjustments to be made in participations of the several Federal Reserve Banks is being sent to all Reserve banks today. These computations indicate an increase of _____ or decrease of _____ in your participation on October 1. We shall wire you on October 1 the detailed entries to be made on that date.

		<u>Increase</u>	<u>Decrease</u>
Young	Boston	10,312,000	-
Williams	Philadelphia	175,000	-
Fleming	Cleveland	-	11,350,000
Leach	Richmond	15,333,000	-
Melarin	Atlanta	1,169,000	-
Young	Chicago	30,795,000	-
Davis	St. Louis	5,527,000	-
Peyton	Minneapolis	3,384,000	-
Leedy	Kansas City	-	12,212,000
Gilbert	Dallas	-	9,278,000
Day	San Francisco	14,853,000	-

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SEP 27 1941
FEDERAL RESERVE BANK OF ST. LOUIS

September 27, 1941.

Mr. R. G. Rouse, Vice President,
Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Rouse:

There is enclosed a copy of a statement prepared in this Division showing the changes necessary in allocations of Government securities in the System Open Market Account on October 1, 1941, in accordance with the formula adopted by the Federal Open Market Committee on December 18, 1940.

Current expenses for the year have been estimated by taking actual amounts for January through August plus estimates for the remainder of the year obtained from the Federal Reserve Banks, except that the estimate of original cost of Federal Reserve currency was made by this Division. We have included an additional \$500,000 for New York and \$120,000 for St. Louis, as was done in connection with the previous allocations this year. Current earnings for 1941 exclusive of earnings on Government securities have been estimated by multiplying the actual amounts thereof for January through August by 1.5.

Very truly yours,

E. L. Smead, Chief,
Division of Bank Operations.

Enclosure

FILE COPY

CONFIDENTIAL

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT OCTOBER 1, 1941
(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minne- apolis	Kansas City	Dallas	San Francisco
Expenses													
1. Estimated current expenses, 1941	33,262	2,480	8,466	2,653	3,294	2,048	1,435	4,231	1,709	1,047	1,812	1,329	2,758
Earnings													
1. Estimated current earnings, 1941 (exclusive of earnings on Gov'ts)	1,174	55	215	156	95	85	7	208	24	29	166	27	107
2. Estimated earnings on Gov't securities to Sept. 30	29,763	2,159	8,498	2,361	3,004	1,640	1,263	3,468	1,408	883	1,462	1,184	2,433
3. Total	30,937	2,214	8,713	2,517	3,099	1,725	1,270	3,676	1,432	912	1,628	1,211	2,540
C. Excess of "A-1" over "B-3"	2,325	266	-247	136	195	323	165	555	277	135	184	118	218
D. Allocation required (on basis of 1.84657% earnings rate on Gov'ts) to produce earnings Oct.-Dec. equal to "C"	499,531	57,150	-53,068	29,220	41,896	69,397	35,450	119,243	59,514	29,005	39,533	25,353	46,838
E. Estimated dividends, 1941	8,423	561	3,097	714	870	328	289	895	258	180	272	256	703
F. Allocation of remainder of System holdings (\$2,184,100,000 less \$199,531,600) on basis of "E"	1,684,569	112,198	619,389	142,797	173,997	65,599	57,799	178,997	31,999	35,999	54,399	51,199	140,997
G. Total allocation of Gov't securities ("D" + "F")	2,184,100	169,348	566,321	172,017	215,893	134,996	93,249	298,240	111,113	65,004	93,932	76,552	187,435
H. Present allocations	2,184,100	199,006	615,149	171,842	227,243	119,663	92,060	267,445	105,526	61,620	106,144	85,830	172,582
I. Change in allocations	--	+10,342	-48,828	+175	-11,350	+15,333	+1,189	+30,795	+5,997	+3,384	-12,212	-9,278	+14,853

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Authority E.O. 12958MAILED IN FILED SECTION
SEP 27 1941
3-2343
September 26, 1941.

Governor Srymsoak

Mr. Smead

Expenses of the Federal Reserve Banks have been going up rapidly since the beginning of the present fiscal year, July 1, and it now appears that the expenses for the year as a whole will be substantially in excess of the estimates given you in my memorandum of July 28. Expenses for both July and August were substantially in excess of those for previous months and because of this we have obtained from the Federal Reserve Banks their estimates of expenses for the last four months of this year for use in connection with the October 1 reallocation of securities in the System Open Market Account.

On the basis of these estimates, it appears that total current expenses of the Federal Reserve Banks for the year 1941 will aggregate approximately \$33,300,000 or about \$1,100,000 in excess of the total for the year 1940. Dividend payments in 1941 will total about \$8,400,000. It is expected that total current expenses and dividends will exceed estimated earnings, \$11,100,000, by about \$600,000. Up to the present time the Federal Reserve Banks have received profits aggregating \$504,000 on sales of United States Government securities, and it is anticipated that this amount, after adjustment for other credits and debits to profit and loss account, will be just about sufficient to offset the excess of expenses and dividends over earnings. Because of the two per cent payments to the Treasury on earnings on industrial advances, a few of the Banks may possibly have to charge their Section 7 Surplus accounts with small amounts at the end of the year. For the System as a whole, however, it is probable that Section 7 Surplus will increase slightly.

Increased expenses during recent months have been caused largely by increases in the following:

Salaries

Personnel, principally in the Check Collection, Currency and Coin Departments, and in the administration of Regulation W unit.

Shipping expense on currency and coin to and from member banks.

Cost of printing Federal Reserve notes and shipping them to Federal Reserve Banks and Branches.

Postage and expressage in connection with installment credit and other activities.

The increase in demand for currency during recent months has been such that we have had to increase our printing order for Federal Reserve notes to the maximum extent the Bureau of Engraving and Printing can produce under the present setup. If the demand for currency continues to increase, it may be necessary for the Bureau to work Saturdays, as it is understood it is having difficulty in obtaining additional technical help.

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For Files
S. H. Board

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Authority E.O. 12958

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m m

September 23, 1941

Young - Boston	Leach - Richmond	Peyton - Minneapolis
Spreul - New York	McLarin - Atlanta	Leedy - Kansas City
Williams - Philadelphia	Young - Chicago	Gilbert - Dallas
Fleming - Cleveland	Davis - St. Louis	Day - San Francisco

Please wire estimated expenses of your Bank, exclusive of original cost of Federal Reserve currency, Item 26 less Item 21, of Form F.R. 96, for September and also for the last quarter of the year. If estimated expenses are materially above or below average for past few months, please state briefly reason for change.

✓

SMEAD

*Oct. 1 reallocation
of System acct*

*File copy 323.12
VF:jbs*

For Files
S. E. Hainer

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Authority E.O. 12958

✓

REC'D IN RECORDS SECTION
APR 9 1968
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FEDERAL RESERVE BANK
OF NEW YORK

cx

June 27, 1941

Dear Mr. Smead:

We received your letter of June 26 and have today sent to the Reserve banks a copy of the computation showing the adjustments to be made in participations in the System Open Market Account on July 1, 1941, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on December 18, 1940.

Enclosed herewith is copy of the letter of transmittal together with three copies of the computation, also copy of the telegram which was sent to each of the Federal Reserve banks today.

Yours faithfully,



Robert G. Rouse,
Manager, System Open
Market Account.

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

Encls. (5)

Directive #1

DECLASSIFIED
Authority E.O. 12958

MISC. 140A 15M 9-38

FEDERAL RESERVE BANK OF NEW YORK

June 27, 1941

Dear Mr. Fleming:

In accordance with my telegram of today, I enclose herewith computation of the readjustments to be made on July 1, 1941, of the participations of the Federal Reserve banks in the System Open Market portfolio.

Yours faithfully,

Robert G. Rouse,
Manager, System Open
Market Account.

Mr. M. J. Fleming, President,
Federal Reserve Bank of Cleveland,
Cleveland, Ohio.

Encl.

DECLASSIFIED
 Authority E.O. 12958

MISC. 140A 15M 9-38

FEDERAL RESERVE BANK OF NEW YORK
 SECURITIES DEPARTMENT

June 27, 1941

Please send the following telegram to each Federal Reserve bank as indicated below:

Under the plan for reallocation of Government securities adopted by the Federal Open Market Committee December 18, 1940, a readjustment of participations in Government securities held in the System Account is called for July 1, 1941. The computations showing adjustments to be made in participations of the several Federal Reserve banks is being sent to all Reserve banks today. These computations indicate an increase of _____ in your participation on July 1. We shall wire you on July 1 the detailed entries to be made on that date.

		<u>Increase</u>	<u>Decrease</u>
Young	Boston	1,189,000	-
Sinclair	Philadelphia	-	1,295,000
Fleming	Cleveland	8,702,000	-
Lench	Richmond	-	1,823,000
Walarin	Atlanta	-	2,824,000
Young	Chicago	16,803,000	-
Davis	St. Louis	4,171,000	-
Peyton	Minneapolis	-	4,327,000
Leedy	Kansas City	4,000	-
Gilbert	Dallas	-	2,217,000
Day	San Francisco	-	10,057,000

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HOUSE

BANK OPERATIONS
 DIVISION OF
 JUL 2 8 1941

RECEIVED

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON JULY 1, 1941

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A. Expenses													
(1) Estimated current expenses, 1941	31,627	2,311	8,176	2,505	3,181	1,901	1,364	3,923	1,618	986	1,793	1,314	2,555
B. Estimated dividends, 1941	8,405	561	3,093	714	867	326	288	890	257	180	271	256	702
C. Estimated expenses and dividends, 1941	40,032	2,872	11,269	3,219	4,048	2,227	1,652	4,813	1,875	1,166	2,064	1,570	3,257
D. Earnings													
(1) Estimated current earnings, 1941 (exclusive of earnings on Gov'ts)	1,145	49	212	145	90	84	4	215	23	29	159	26	109
(2) Estimated earnings on Gov't. securities to June 30	19,644	1,422	5,648	1,565	1,951	1,086	837	2,229	919	597	970	787	1,633
(3) Total	20,789	1,471	5,860	1,710	2,041	1,170	841	2,444	942	626	1,129	813	1,742
E. Excess of "C" over "D-3"	19,243	1,401	5,409	1,509	2,007	1,057	811	2,369	933	540	935	757	1,515
F. Allocation required (on basis of 84.657% earnings rate on Gov'ts) to produce earnings July-December equal to "E"	2,067,198	150,504	581,067	162,106	215,604	113,549	87,123	254,492	100,228	58,010	100,443	81,322	162,750
G. Average daily participations, per cent, in System account since June 30, 1936	100.0	7.2732	29.1541	8.3285	9.9561	5.2298	4.2231	11.0798	4.5237	3.0882	4.8766	3.8562	8.4107
H. Allocation of remainder of System holdings (\$2,184,100,000 less \$2,067,198,000) on basis of "G"	116,902	8,502	34,082	9,736	11,639	6,114	4,937	12,953	5,288	3,610	5,701	4,508	9,832
I. Total allocation of Government securities ("F" plus "H")	2,184,100	159,006	615,149	171,842	227,243	119,663	92,060	267,445	105,516	61,620	106,144	85,830	172,582
J. Present allocations	2,184,100	157,817	623,475	173,137	218,541	121,486	94,884	250,642	101,345	65,947	106,140	88,047	182,639
K. Change in allocations	--	+1,189	-8,326	-1,295	+8,702	-1,823	-2,824	+16,803	+4,171	-4,327	+4	-2,217	-10,057

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June 26, 1941.

Mr. Smead

Earnings of the Federal

Mr. Van Fossen

Reserve Banks.

In the July 1, 1941, reallocation of Government securities in the System Open Market Account, the Federal Reserve Bank of Chicago will receive the largest increase in allocation, approximately \$17,000,000, and the Federal Reserve Bank of San Francisco will have the largest decrease, approximately \$10,000,000.

Estimated current expenses for 1941 as used for the July 1 reallocation are lower for the Federal Reserve Banks of San Francisco, Atlanta, and Minneapolis than the estimate used for the April 1 reallocation. These three banks and the New York, Philadelphia, Richmond, and Dallas Banks, which had relatively small increases in estimated current expenses, will all have smaller participations than they received on the April 1 reallocation.

The large increase in Chicago's participation is due to a very substantial increase in estimated expenses. In this connection you will recall that the Chicago Bank is the only one that will probably not have sufficient earnings on June 30 to cover dividends for the first half of the year. There has been an increase in expenses of the Federal Reserve Bank of Chicago each month during the year, the increase for May being exceptionally large. The principal items showing an increase during that month were printing, stationery, and supplies in which there was an increase of \$22,000 to approximately \$30,000, and in furniture and equipment in which there was an increase of about \$17,000 to approximately \$19,000. It is assumed that the increase in furniture and equipment was due to the purchase of currency counting machines, which, it is understood, the Chicago Bank has purchased in order to be able to furnish the Chicago banks certain services that have not heretofore been furnished. Following is a tabulation showing estimated expenses for 1941 for the Chicago and San Francisco Banks, and for all Federal Reserve Banks combined, as estimated for the January 1, April 1, and July 1 allocations of the System Account, also actual expenses in 1940:

Estimated Expenses for 1941

	<u>Chicago</u>	<u>San Francisco</u>	<u>All F.R. Banks</u>
For January 1 allocation	\$3,508,000	\$2,497,000	\$30,017,000
For April 1 allocation	3,685,000	2,586,000	30,931,000
For July 1 allocation	3,923,000	2,555,000	31,627,000
Actual expenses in 1940	3,471,000	2,493,000	29,165,000

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Authority E.O. 12958

IN NEWS SECTION
40 JUN 27 1941
10333 243

June 26, 1941.

Mr. R. G. Rouse, Vice President,
Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Rouse:

There is enclosed a copy of the statement prepared in this Division showing the changes necessary in allocations of Government securities in the System Open Market Account on July 1, 1941, in accordance with the formula adopted by the Federal Open Market Committee on December 18, 1940.

Current expenses and current earnings, exclusive of earnings on Governments, have been estimated by multiplying the actual amounts thereof from January through May 1941 by 2.4. To the estimates of current expenses obtained on this basis, we have added \$500,000 for New York and \$120,000 for St. Louis as was done in connection with the January 1 and April 1 reallocations.

Very truly yours,

E. L. Smead, Chief,
Division of Bank Operations.

Enclosure

VF:seh

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JUN 27 1941

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON JULY 1, 1941

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A. Expenses													
(1) Estimated current expenses, 1941	31,627	2,311	8,176	2,505	3,181	1,901	1,364	3,923	1,618	986	1,793	1,314	2,555
B Estimated dividends, 1941	8,405	561	3,093	714	867	326	288	890	257	180	271	256	702
C. Estimated expenses and dividends, 1941	40,032	2,872	11,269	3,219	4,048	2,227	1,652	4,813	1,875	1,166	2,064	1,570	3,257
D. Earnings													
(1) Estimated current earnings, 1941 (exclusive of earnings on Gov'ts)	1,115	49	212	115	90	84	4	215	23	29	159	26	109
(2) Estimated earnings on Gov't. securities to June 30	19,614	1,422	5,648	1,565	1,751	1,086	837	2,229	919	597	970	787	1,633
(3) Total	20,789	1,471	5,860	1,710	2,041	1,170	841	2,444	942	626	1,129	813	1,742
E. Excess of "C" over "D-3"	19,213	1,401	5,409	1,509	2,007	1,057	811	2,369	933	540	935	757	1,515
F. Allocation required (on basis of 1.84657% earnings rate on Gov'ts) to produce earnings July-December equal to "E"	2,067,198	150,504	581,067	162,106	215,604	113,519	87,123	254,492	100,228	58,010	100,443	81,322	162,750
G. Average daily participations, per cent, in System account since June 30, 1936	100.0	7.2732	29.1541	8.3285	9.9561	5.2298	4.2231	11.0798	4.5237	3.0882	4.8766	3.8562	8.4107
H. Allocation of remainder of System holdings (\$2,184,100,000 less \$2,067,198,000) on basis of "G"	116,902	8,502	34,082	9,736	11,639	6,114	4,937	12,953	5,288	3,610	5,701	4,508	9,832
I. Total allocation of Government securities ("F" plus "H")	2,184,100	159,006	615,149	171,842	227,243	119,663	92,060	267,445	105,516	61,620	106,144	85,830	172,582
J. Present allocations	2,184,100	157,817	623,475	173,137	218,541	121,186	94,884	250,612	101,345	65,947	106,110	88,047	182,639
K. Change in allocations	--	+1,189	-8,326	-1,295	+8,702	-1,823	-2,824	+16,803	+4,171	-4,327	+4	-2,217	-10,057

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JUL 21 1941

EXPLANATION OF COMPUTATION OF ITEMS INDICATED

(Reallocation of Government Securities July 1, 1941)

- A-1 and D-1 2.4 times actual figures January to May, 1941, with A-1 adjusted by adding \$500,000 to New York and \$120,000 to St. Louis, as was done for the January 1 and April 1 reallocations.
- B. Accrued dividends May 31 plus 3.5 per cent of paid-in capital June 18.
- D-2 and G As telephoned from New York by Mr. Behrens June 23.
- F. Earnings rate as of June 30 telephoned by Mr. Behrens June 23. Actual rate used .9308736 per cent (184 X 365th of annual rate).

54
JUL 21 1941

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Form F. R. 131

BOARD OF GOVERNORS
 OF THE
 FEDERAL RESERVE SYSTEM

REC'D IN RECORDS SECTION

APR 19 1968

Date June 13, 1941.

Office Correspondence

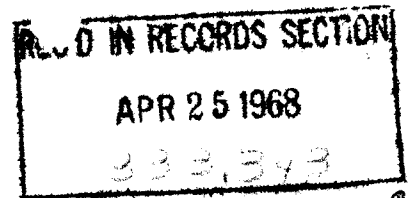
To Mr. SmeadSubject: Losses and participations inFrom Mr. Van FossenSystem account.

M

Beginning with the January 1, 1941, reallocation of the System Open Market account, profits and losses on sales of Government securities have been disregarded in the reallocation as approved by the Open Market Committee. The procedure is to allocate to each Federal Reserve Bank an amount of securities sufficient to cover its estimated expenses not covered by earnings, if any, already accrued on Government securities and estimated earnings from other sources; next to allocate participations sufficient to cover dividend requirements, and finally to allocate the remaining securities in proportion to average daily participations in the System account since June 30, 1936. Where a sufficient volume of securities are held to necessitate a third step, the first and second steps ^{can} ~~can~~ and ~~will~~ be combined into a single step.

If it were desired to have the quarterly allocations of the System account cover losses not provided for by insurance or insurance reserves, it would be possible to do this in a number of ways. For example, such losses could be included with expenses in step one, or they could be provided for separately in a new step following the provision for expenses ~~by~~ preceding the provision for dividend requirements. The suggestion has been made that the entire profit and loss account of each Federal Reserve Bank be taken into consideration in making the quarterly reallocations. This could be done very readily, of course, either by combining the profit and loss account with estimated expenses or in a separate step. It would seem that if the entire profit and loss account is to be taken into consideration, it would be appropriate to modify the procedure as regards any securities remaining after expenses, profit and loss, and dividends have all been covered to allocate such remaining securities on a basis designed to equalize the capital position of the various Federal Reserve Banks. As you know, a number of suggestions have been made as to how this might be accomplished. I do not believe that it is worth while at this time to consider the methods that would be most appropriate for the purpose.

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Extract from Appropriation Act of May 31, 1941, making appropriations for the Treasury Department for the fiscal year ending June 30, 1942:

5/31/41

"Expenses of loans: The indefinite appropriation 'Expenses of loans, Act of September 24, 1917, as amended and extended' (31 U. S. C. 760, 761), shall not be used during the fiscal year 1942 to supplement the appropriation herein made for the current work of the Bureau of the Public Debt, and the amount obligated under such indefinite appropriation during such fiscal year shall not exceed \$4,292,000: Provided, That the proviso in the Act of June 16, 1921 (31 U. S. C. 761), limiting the availability of this appropriation for expenses of operations on account of any public debt issue to the close of the fiscal year next following the fiscal year in which such issue was made, shall not apply to savings bond transactions handled by the Federal Reserve banks for account of the Secretary of the Treasury."

Directive #1

May

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FEDERAL RESERVE BANK
OF NEW YORK

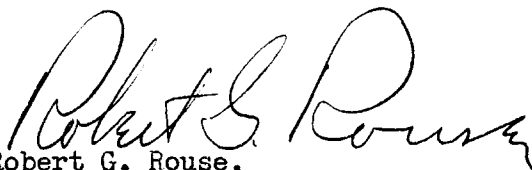
March 28, 1941.

Dear Mr. Van Fossen:

We received your letter of March 27 and have today sent to the Reserve banks a copy of the computation showing the adjustments to be made in participations in the System Open Market Account on April 1, 1941, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on December 18, 1940.

Enclosed herewith is copy of the letter of transmittal together with three copies of the computation, also copy of the telegram which was sent to each of the Federal Reserve banks today.

Yours faithfully,


Robert G. Rouse,
Manager, System Open
Market Account.

Mr. John R. Van Fossen, Assistant Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

Encls. (5)

Director

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Authority E.O. 12958

Similar letter sent to Mr. John S. Sinclair, Pres., FRB of Philadelphia
" M. J. Fleming, " " Cleveland
" Hugh Leach, " " Richmond
" William S. McLarin, Jr., First Vice President, FRB of Atlanta
" Clifford S. Young, " " Chicago
" F. Guy Hitt, First Vice President, FRB of St. Louis
" John N. Peyton, Pres., FRB of Minneapolis
" Harold G. Leedy, First Vice President, FRB of Kansas City
" R. R. Gilbert, Pres., FRB of Dallas
" W. A. Day, Pres., FRB of San Francisco

March 28, 1941

Dear Mr. Young:

In accordance with my telegram of today, I enclose herewith computation of the readjustments to be made on April 1, 1941, of the participations of the Federal Reserve banks in the System Open Market portfolio.

Yours faithfully,

Robert G. Rouse,
Manager, System Open
Market Account.

Honorable Roy A. Young, President,
Federal Reserve Bank of Boston,
Boston, Mass.

Encl.

DECLASSIFIED
 Authority E.O. 12958

SECURITIES DEPARTMENT RMB HS

March 28, 1941

Please send the following telegram to each Federal Reserve bank as indicated below:

Under the plan for reallocation of Government securities adopted by the Federal Open Market Committee December 18, 1940, a readjustment of participations in Government securities held in the System Account is called for April 1, 1941. The computations showing adjustments to be made in participations of the several Federal Reserve banks is being sent to all Reserve banks today. These computations indicate an ^{increase} of _____ in your participation on April 1. We shall wire you on April 1 the detailed entries to be made on that date.

	<u>Increase</u>	<u>Decrease</u>
Young Boston	-	661,000
Sinclair Philadelphia	-	1,705,000
Fleeding Cleveland	3,238,000	-
Leach Richmond	1,510,000	-
McLarin Atlanta	3,775,000	-
Young Chicago	5,732,000	-
Hitt St. Louis	-	1,793,000
Payton Minneapolis	-	905,000
Leedy Kansas City	-	3,555,000
Gilbert Dallas	1,212,000	-
Day San Francisco	2,183,000	-

ROUSE

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON APRIL 1, 1941

(In thousands of dollars)

	System	Boston	New York	Philadelphia	Cleveland	Richmond	Atlanta	Chicago	St. Louis	Minneapolis	Kansas City	Dallas	San Francisco
A. Expenses													
(1) Estimated current expenses, 1941	30,931	2,248	8,019	2,453	3,060	1,877	1,373	3,685	1,549	1,004	1,767	1,310	2,586
B. Estimated dividends, 1941	8,380	561	3,091	713	863	325	287	880	255	179	270	256	700
C. Estimated expenses and dividends, 1941	39,311	2,809	11,110	3,166	3,923	2,202	1,660	4,565	1,804	1,183	2,037	1,566	3,286
D. Earnings													
(1) Estimated current earnings, 1941 (exclusive of earnings on Gov'ts)	1,211	54	205	145	124	84	19	211	26	30	170	32	111
(2) Estimated earnings on Gov't securities to March 31	9,676	702	2,802	775	954	531	404	1,085	457	296	486	385	799
(3) Total	10,887	756	3,007	920	1,078	615	423	1,296	483	326	656	417	910
E. Excess of "C" over "D -3"	28,424	2,053	8,103	2,246	2,845	1,587	1,237	3,269	1,321	857	1,381	1,149	2,376
F. Allocation required (on basis of 1.83183% earnings rate on Gov'ts) to produce earnings April-December equal to "E"	2,059,486	148,751	587,110	162,736	206,137	114,988	89,628	236,858	95,714	62,095	100,062	83,252	172,155
G. Average daily participations, per cent, in System account since June 30, 1936	100.0	7.2754	29.1821	8.3469	9.9538	5.2145	4.2175	11.0616	4.5183	3.0914	4.8774	3.8482	8.4129
H. Allocation of remainder of System holdings (\$2,184,100,000 less \$2,059,486,000) on basis of "G"	124,614	9,066	36,365	10,401	12,404	6,498	5,256	13,784	5,631	3,852	6,078	4,795	10,484
I. Total allocation of Government securities ("F" plus "H")	2,184,100	157,817	623,475	173,137	218,541	121,486	94,884	250,642	101,345	65,947	106,140	88,047	182,639
J. Present allocations	2,184,100	158,481	632,503	174,842	215,303	119,976	91,109	244,910	103,138	66,852	109,695	86,835	180,456
K. Change in allocations	--	-664	-9,028	-1,705	+3,238	+1,510	+3,775	+5,732	-1,793	-905	-3,555	+1,212	+2,183

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Authority E.O. 12958

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON APRIL 1, 1941

(In thousands of dollars)

	System	Boston	New York	Philadelphia	Cleveland	Richmond	Atlanta	Chicago	St. Louis	Minneapolis	Kansas City	Dallas	San Francisco
A. Expenses													
(1) Estimated current expenses, 1941	30,931	2,248	8,019	2,453	3,060	1,877	1,373	3,685	1,549	1,004	1,767	1,310	2,586
B. Estimated dividends, 1941	8,380	561	3,091	713	863	325	287	880	255	179	270	256	700
C. Estimated expenses and dividends, 1941	39,311	2,809	11,110	3,166	3,923	2,202	1,660	4,565	1,804	1,183	2,037	1,566	3,286
D. Earnings													
(1) Estimated current earnings, 1941 (exclusive of earnings on Gov'ts)	1,211	54	205	145	124	84	19	211	26	30	170	32	111
(2) Estimated earnings on Gov't securities to March 31	9,676	702	2,802	775	954	531	404	1,085	457	296	486	385	799
(3) Total	10,887	756	3,007	920	1,078	615	423	1,296	483	326	656	417	910
E. Excess of "C" over "D -3"	28,424	2,053	8,103	2,246	2,845	1,587	1,237	3,269	1,321	857	1,381	1,149	2,376
F. Allocation required (on basis of 1.83183% earnings rate on Gov'ts) to produce earnings April-December equal to "E"	2,059,486	148,751	587,110	162,736	206,137	114,988	89,628	236,858	95,714	62,095	100,062	83,252	172,155
G. Average daily participations, per cent, in System account since June 30, 1936	100.0	7.2754	29.1821	8.3469	9.9538	5.2145	4.2175	11.0616	4.5183	3.0914	4.8774	3.8482	8.4129
H. Allocation of remainder of System holdings (\$2,184,100,000 less \$2,059,486,000) on basis of "G"	124,614	9,066	36,365	10,401	12,404	6,498	5,256	13,784	5,631	3,852	6,078	4,795	10,484
I. Total allocation of Government securities ("F" plus "H")	2,184,100	157,817	623,475	173,137	218,541	121,486	94,884	250,642	101,345	65,947	106,140	88,047	182,639
J. Present allocations	2,184,100	158,481	632,503	174,842	215,303	119,976	91,109	244,910	103,138	66,852	109,695	86,835	180,456
K. Change in allocations	--	-664	-9,028	-1,705	+3,238	+1,510	+3,775	+5,732	-1,793	-905	-3,555	+1,212	+2,183

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Authority E.O. 12958

DECLASSIFIED
 Authority E.O. 12958

RECORDED IN FILES SECTION
 MAR 27 1941
 3232-542

March 27, 1941.

Mr. R. G. Rouse, Vice President,
 Federal Reserve Bank of New York,
 New York, New York.

Dear Mr. Rouse:

There is enclosed a copy of the statement prepared in this Division showing the changes necessary in allocations of Government securities in the System Open Market Account on April 1, 1941, in accordance with the formula adopted by the Federal Open Market Committee on December 18, 1940.

Current expenses and current earnings, exclusive of earnings on Governments, have been estimated by multiplying the actual amounts thereof from October 1940 through February 1941 by 2.4. To the estimates of current expenses obtained on this basis, we have added \$500,000 for New York and \$120,000 for St. Louis as was done in connection with the January 1 reallocation.

Very truly yours,

Jf
 J. R. Van Poyken, Asst. Chief,
 Division of Bank Operations.

Enclosure

Jf
 ID: seh

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1941
 MAR 27

DECLASSIFIED
Authority E.O. 12958

PLACED IN FILES SECTION
MAR 27 1941

EXPLANATION OF COMPUTATION OF ITEMS INDICATED

(Reallocation of Government Securities April 1, 1941)

- A-1 and B-1 2.4 times actual figures October 1940 to February 1941, with A-1 adjusted by adding \$500,000 to New York and \$120,000 to St. Louis, as was done for the January 1 reallocation.
- B. Accrued dividends February 28 plus 5 per cent of paid-in capital March 19.
- D-2 and G As telephoned from New York by Mr. Behrens March 25.
- F. Earnings rate as of March 31 telephoned by Mr. Behrens March 25. Actual rate used 1.38015 per cent (275 X 365 of annual rate).

W. H. H. H.
S. E. H. H.

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON APRIL 1, 1941

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A. Expenses													
(1) Estimated current expenses, 1941	30,931	2,248	8,019	2,453	3,060	1,877	1,373	3,685	1,549	1,004	1,767	1,310	2,586
Estimated dividends, 1941	8,380	561	3,091	713	863	325	287	330	255	179	270	256	700
C. Estimated expenses and dividends, 1941	39,311	2,809	11,110	3,166	3,923	2,202	1,660	4,565	1,804	1,183	2,037	1,566	3,286
D. Earnings													
(1) Estimated current earnings, 1941 (exclusive of earnings on Gov'ts)	1,211	54	205	145	124	84	19	211	26	30	170	32	111
(2) Estimated earnings on Gov't securities to March 31	9,676	702	2,802	775	954	531	404	1,085	457	296	486	385	799
(3) Total	10,887	756	3,007	920	1,078	615	423	1,296	483	326	656	417	910
E. Excess of "C" over "D -3"	28,424	2,053	8,103	2,246	2,845	1,587	1,237	3,269	1,321	857	1,381	1,149	2,376
F. Allocation required (on basis of 1.83183% earnings rate on Gov'ts) to produce earnings April-December equal to "E"	2,059,486	148,751	587,110	162,736	206,137	114,988	89,628	236,858	95,714	62,095	100,062	83,252	172,155
G. Average daily participations, per cent, in System account since June 30, 1936	100.0	7.2754	29.1821	8.3469	9.9538	5.2145	4.2175	11.0616	4.5183	3.0914	4.8774	3.8482	8.4129
H. Allocation of remainder of System holdings (\$2,184,100,000 less \$2,059,486,000) on basis of "G"	124,614	9,066	36,365	10,401	12,404	6,498	5,256	13,784	5,631	3,852	6,078	4,795	10,484
I. Total allocation of Government securities ("F" plus "H")	2,184,100	157,817	623,475	173,137	218,541	121,486	94,884	250,642	101,345	65,947	106,140	88,047	182,639
J. Present allocations	2,184,100	158,481	632,503	174,842	215,303	119,976	91,109	244,910	103,138	66,852	109,695	86,835	180,456
K. Change in allocations	--	-664	-9,028	-1,705	+3,238	+1,510	+3,775	+5,732	-1,793	-905	-3,555	+1,212	+2,183

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FEDERAL RESERVE BANK
OF NEW YORK

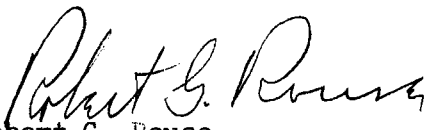
December 28, 1940.

Dear Mr. Smead:

We received your letter of December 26 and have today sent to the Reserve banks a copy of the computation showing the adjustments to be made in participations in the System Open Market Account on January 2, 1941, as of January 1, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on December 18, 1940.

Enclosed herewith is copy of the letter of transmittal together with three copies of the computation, also copy of the telegram which was sent to each of the Federal Reserve banks today.

Yours faithfully,



Robert G. Rouse,
Manager, System Open
Market Account.

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

Encls. (5)

Directive #1

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MISC. 140A 15M 9 38

FEDERAL RESERVE BANK OF NEW YORK

Similar letter written to the President of each Federal Reserve bank except New York

December 28, 1940

Dear Mr. Fleming:

In accordance with my telegram of today, I enclose herewith computation of the readjustments to be made on January 2, 1941 as of January 1, of the participations of the Federal Reserve banks in the System Open Market portfolio.

Yours faithfully,

Robert G. Rouse,
Manager, System Open
Market Account.

Mr. M. J. Fleming, President,
Federal Reserve Bank of Cleveland,
Cleveland, Ohio.

Encl.

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MISC. 140A 15M 9-38

FEDERAL RESERVE BANK OF NEW YORK

SECURITIES DEPT. - RMB FES

December 28, 1940

Please send following telegram to the President of each Federal Reserve bank as indicated below:

At the meeting of the Federal Open Market Committee on December 18, the plan of allocation of Government securities held in the System Open Market Account was revised effective January 1, 1941. The plan adopted at that meeting is as follows: "(1) allocate sufficient securities to each bank to cover expenses not covered by accrued earnings on Government securities and estimated earnings from other sources, (2) allocate a sufficient amount of additional securities to each bank to cover dividend requirements, and (3) allocate any remaining securities among the banks on the basis of average daily participations in the System Account since June 30, 1936. When estimated earnings equal or exceed estimated expenses and dividends, steps 1 and 2, indicated above, could be combined thus simplifying the allocation procedure."

The quarterly reallocation called for on January 1, 1941 is in accordance with this plan, and the computations showing adjustments to be made in participations of the several Federal Reserve banks is being sent to all Reserve banks today. These computations indicate an increase decrease of _____ in your participation on January 1. We shall wire you on January 2 the detailed entries to be made as of January 1.

		<u>Increase</u>	<u>Decrease</u>
Young	Boston	\$1,700,000	-
Sinclair	Philadelphia	-	8,165,000
Fleming	Cleveland	-	3,428,000
Leach	Richmond	4,076,000	-
Parker	Atlanta	7,325,000	-
Schaller	Chicago	-	4,429,000
Martin	St. Louis	8,763,000	-
Poyton	Minneapolis	4,605,000	-
Hamilton	Kansas City	2,652,000	-
Gilbert	Dallas	1,912,000	-
Day	San Francisco	-	2,159,000

ROUSE

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON JANUARY 1, 1941

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Kinn- eapolis	Kansas City	Dallas	San Francisco
A. Expenses													
(1) Estimated current expenses, 1941	30,017	2,188	7,895	2,396	2,901	1,800	1,284	3,508	1,533	982	1,769	1,264	2,497
B. Estimated dividends, 1941	8,297	560	3,066	713	852	322	282	858	251	179	267	250	697
C. Estimated expenses and dividends, 1941	38,314	2,748	10,961	3,109	3,753	2,122	1,566	4,366	1,784	1,161	2,036	1,514	3,194
D. Estimated earnings, 1941 (exclusive of earnings on Gov'ts)	1,278	61	240	151	104	82	22	210	31	28	173	39	137
E. Excess of "C" over "D"	37,036	2,687	10,721	2,958	3,649	2,040	1,544	4,156	1,753	1,133	1,863	1,475	3,057
F. Allocation required (on basis of 1.78281% earning rate on Gov'ts) to produce earnings equal to "E"	2,077,394	150,717	601,354	165,918	204,677	114,126	86,605	233,115	98,328	63,551	104,198	82,731	171,471
G. Allocation of remainder of System holdings (\$2,184,100,000 less \$2,077,394,000) on basis of average daily participations in System account since June 30, 1936	106,706	7,744	31,119	8,921	10,626	5,550	4,504	11,795	4,811	3,301	5,197	4,100	8,985
H. Total allocation of Gov'ts	2,184,100	158,461	632,503	174,839	215,303	119,676	91,109	244,910	103,139	66,852	109,395	86,831	180,456
I. Present allocations	2,184,100	156,781	645,355	183,007	218,731	115,900	83,784	240,339	94,376	62,217	107,043	84,922	132,615
J. Change in allocations	--	+1,700	-12,852	-8,168	-3,428	+3,776	+7,325	+4,571	+8,763	+4,635	+2,352	+1,909	-2,159

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BOARD OF GOVERNORS
 OF THE
 FEDERAL RESERVE SYSTEM
 WASHINGTON

REF ID IN FILES SECTION
 DEC 30 1940
 333 ● 343



ADDRESS OFFICIAL CORRESPONDENCE
 TO THE BOARD

December 27, 1940

Dear Sir:

All of the Presidents of Federal Reserve Banks were in attendance at the meeting of the Federal Open Market Committee on December 18, 1940, and are familiar with the actions taken following the consideration of the report submitted by Messrs. Smead and Rouse under date of September 26, 1940, with respect to the basis for the allocation of securities in the System open market account and the accounting procedures that might be adopted for the account. Therefore, this letter is written for the purpose of formally advising your Bank of the actions taken.

Approval was given by the Presidents and by the Federal Open Market Committee to a basis for the quarterly allocation of securities in the System open market account, as recommended by Messrs. Smead and Rouse, which would allocate (1) sufficient securities to each Federal Reserve Bank to cover expenses not covered by accrued earnings on Government securities and estimated earnings from other sources, (2) a sufficient amount of additional securities to each Bank to cover dividend requirements, and (3) any remaining securities among the Banks on the basis of average daily participations in the System account since June 30, 1936, which is the basis on which profits on sales of securities in the System account are distributed among Federal Reserve Banks at the present time. This action was taken by the Federal Open Market Committee with the understanding that, if possible, the new procedure would be followed in connection with the January 1, 1941, re-allocation of securities in the System account.

The decision was also reached to recommend to the Board of Governors that no change be made in the manner in which Government securities held in the System open market account are shown in the weekly statement of condition of Federal Reserve Banks, and that for the current year profits on securities sold from the

*Indepd copy
 Form 2-22-41*

See memo 8/26/42

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-2-

System open market account should be transferred to reserves for contingencies.

Very truly yours,



Chester Morrill, Secretary,
Federal Open Market Committee.

TO THE PRESIDENTS OF ALL FEDERAL RESERVE BANKS

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Authority E.O. 12958

REC'D IN FILES SECTION
R DEC 27 1940
333 343

December 26, 1940.

Mr. R. G. Rouse, Vice President,
Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Rouse:

There is enclosed a copy of a statement prepared in this Division showing the changes necessary in allocations of Government securities in the System Open Market Account on January 1, 1941, in accordance with the revised formula adopted by the Federal Open Market Committee at its meeting on December 18, 1940.

Current expenses and current earnings (exclusive of earnings on Governments) have been estimated by multiplying the actual amounts thereof from July through November, 1940, by 2.4. We have added \$500,000 to the estimate of current expenses for New York, obtained on this basis, in view of a prospective increase in annual depreciation charges and in repairs and alterations in connection with air-conditioning the New York building, and \$120,000 to the estimate of current expenses for St. Louis to complete the program of setting aside a 100 percent reserve on fixed machinery and equipment in connection with air-conditioning the head office and branch buildings. We have deducted from the estimate of current expenses for Chicago \$70,000 in view of a temporary increase for the months of September to November, inclusive, in depreciation charges on fixed machinery and equipment in the Chicago building.

Very truly yours,

E. L. Smead, Chief,
Division of Bank Operations.

Enclosure

[Handwritten signature]

VF:seh

FILE COPY

FOR FILES
I. B. Smith

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON JANUARY 1, 1941

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A. Expenses													
(1) Estimated current expenses, 1941	30,017	2,188	7,895	2,396	2,901	1,800	1,284	3,508	1,533	982	1,769	1,264	2,497
b. Estimated dividends, 1941	8,297	560	3,066	713	852	322	282	858	251	179	267	250	697
c. Estimated expenses and dividends, 1941	38,314	2,748	10,961	3,109	3,753	2,122	1,566	4,366	1,784	1,161	2,036	1,514	3,194
D. Estimated earnings, 1941 (exclusive of earnings on Gov'ts)	1,278	61	240	151	104	82	22	210	31	28	173	39	137
E. Excess of "C" over "D"	37,036	2,687	10,721	2,958	3,649	2,040	1,544	4,156	1,753	1,133	1,863	1,475	3,057
F. Allocation required (on basis of 1.78281% earning rate on Gov'ts) to produce earnings equal to "E"	2,077,394	192,717	601,354	165,918	204,677	114,126	86,605	233,115	98,328	63,551	104,498	82,734	171,471
G. Allocation of remainder of System holdings (\$2,184,100,000 less \$2,077,394,000) on basis of average daily participations in System account since June 30, 1936	106,706	7,764	31,119	8,924	10,625	5,550	4,504	11,795	4,811	3,301	5,197	4,100	8,985
H. Total allocation of Gov'ts	2,184,100	192,481	632,503	174,842	215,303	119,676	91,109	244,910	103,139	66,852	109,695	86,834	180,456
I. Present allocations	2,184,100	196,781	645,355	183,007	214,731	115,900	83,784	249,339	94,376	62,217	107,043	84,922	182,615
J. Change in allocations	—	+1,700	-12,852	-8,165	-3,428	+4,076	+7,325	-4,429	+8,763	+4,635	+2,652	+1,912	-2,159

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON JANUARY 1, 1941

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A. Expenses													
(1) Estimated current expenses, 1941	30,017	2,188	7,895	2,396	2,901	1,800	1,284	3,508	1,533	982	1,769	1,264	2,497
B. Estimated dividends, 1941	8,297	560	3,066	713	852	322	282	858	251	179	267	250	697
C. Estimated expenses and dividends, 1941	38,314	2,748	10,961	3,109	3,753	2,122	1,566	4,366	1,784	1,161	2,036	1,514	3,194
D. Estimated earnings, 1941 (exclusive of earnings on Gov'ts)	1,278	61	240	151	104	82	22	210	31	28	173	39	137
E. Excess of "C" over "D"	37,036	2,687	10,721	2,958	3,649	2,040	1,544	4,156	1,753	1,133	1,863	1,475	3,057
F. Allocation required (on basis of 1.78281% earning rate on Gov'ts) to produce earnings equal to "E"	2,077,394	192,717	603,354	165,918	204,677	114,126	86,605	233,115	98,328	63,551	104,498	82,734	171,471
G. Allocation of remainder of System holdings (\$2,184,100,000 less \$2,077,394,000) on basis of average daily participations in System account since June 30, 1936	106,706	7,744	31,119	8,924	10,626	5,550	4,504	11,795	4,811	3,301	5,197	4,100	8,985
H. Total allocation of Gov'ts	2,184,100	192,481	632,503	174,842	215,303	119,676	91,109	244,910	103,139	66,852	109,695	86,834	180,456
I. Present allocations	2,184,100	196,781	645,355	183,007	214,731	115,900	83,784	249,339	94,376	62,217	107,043	84,922	182,615
J. Change in allocations	--	+4,700	-12,852	+8,165	-3,428	+4,076	+7,325	-4,429	+8,763	+4,605	+2,652	+1,912	-2,159

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December 16, 1940.

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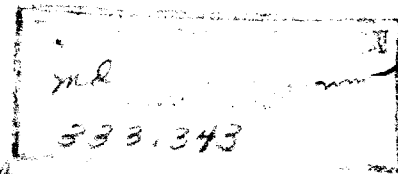
Mr. Sneed,

The attached represents my recommendation
to Mr. Harrison in connection with our report.

R.G.R.

FOR FILES
L. B. Smith

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12/16/40

"As you recall, the Committee on Accounting Procedure in connection with the System Open Market Account (Smead-Rouse) filed a report at the September 27th meeting which I understand is to be considered on Tuesday. If I am called on for recommendations, I shall recommend -

- (1) No change be made in the form of the weekly press statement.
- (2) It should be regarded as System policy to transfer profits realized on the sale of Government securities to reserves for contingencies, however, without any binding resolutions that might have to be revised in event of changes in circumstances. If it were generally urged that profits arising out of switches (particularly those involving the sale of "rights") be used to write down the cost of the replacement securities, I would not oppose it.
- (3) The proposed formula for allocation of securities be adopted, as it seems to me the best available.

Mr. Smead and I are in substantial agreement on these recommendations. This formula would tend to reduce the interest income of the New York, Philadelphia and Cleveland banks, as their dividend ratios are in excess of their holding ratios over a period of years. However, the theory that the apportionment of excess securities should bear a direct relationship to the profit and loss or holding ratio, seems to me to be the governing principle."

December 16, 1940.

FOR FILE
 L. B. S. 1940

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REC'D IN FILES SECTION
OCT 2 - 1940

October 2, 1940.

Mr. Roy A. Young, President,
Federal Reserve Bank of Boston,
Boston, Massachusetts.

Dear Mr. Young:

In accordance with a request received over the telephone from Mr. Rouse, I am enclosing herewith a copy of the report made by Mr. Rouse and myself on September 26, 1940, to the members of the Federal Open Market Committee and the Presidents of the Federal Reserve Banks on accounting procedure in connection with the System Open Market Account.

Sincerely yours,

E. L. Smead, Chief,
Division of Bank Operations.

Enclosure

FILE COPY

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REC. IN FILES SECTION
OCT 2 - 1940
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October 2, 1940.

Mr. R. G. Rouse, Vice President,
Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Rouse:

In accordance with your telephone
request, I am enclosing herewith two additional
copies of our September 26 report on accounting
procedure in connection with the System Open
Market Account.

Sincerely yours,

E. L. Smead, Chief,
Division of Bank Operations.

Enclosures 2

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See files
of E. Smead

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FEDERAL RESERVE BANK
OF NEW YORK

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September 28, 1940

Dear Mr. Smead:

We received your letter of September 26 and have today sent to the Reserve banks a copy of the computation showing the adjustments to be made in participations in the System Open Market Account on October 1, 1940, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on November 30, 1937.

Enclosed herewith is copy of the letter of transmittal together with three copies of the computation, also copy of the telegram which was sent to each of the Federal Reserve banks today.

Yours faithfully,

Robert G. Rouse
Robert G. Rouse,
Manager, System Open
Market Account.

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

Encls. (5)

Directive #1

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MISC 140A 13M 8-39

**FEDERAL RESERVE BANK OF NEW YORK
 SECURITIES DEPT. - RHB FMS**

September 28, 1940

Please send following telegram to the President of each Federal Reserve bank as indicated below:

Under the plan for reallocation of Government securities adopted by the Federal Open Market Committee November 30, 1937, a readjustment of participations in Government securities held in the System Account is called for October 1, 1940. The computations showing adjustments to be made in participations of the several Federal Reserve banks is being sent to all Reserve banks today. These computations indicate an ~~increase~~ of _____ in your participation on October 1. We shall wire you on October 1 the detailed entries to be made on that date.

		<u>Increase</u>	<u>Decrease</u>
Young	Boston	-	\$3,788,000
Sinclair	Philadelphia	11,699,000	-
Fleming	Cleveland	-	5,284,000
Leach	Richmond	3,571,000	-
Parker	Atlanta	2,976,000	-
Schaller	Chicago	16,090,000	-
Martin	St. Louis	-	10,958,000
Peyton	Minneapolis	-	4,102,000
Hamilton	Kansas City	-	133,000
Gilbert	Dallas	-	2,544,000
Day	San Francisco	-	1,031,000

ROUSE

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MISC. 140A 18M 8-39

FEDERAL RESERVE BANK OF NEW YORK

Similar letter written to the President of each Federal Reserve bank except New York

September 28, 1940

Dear Mr. Young:

In accordance with my telegram of today, I enclose herewith computation of the readjustments to be made on October 1, 1940, of the participations of the Federal Reserve banks in the System Open Market portfolio.

Yours faithfully,

Robert G. Rouse
Manager, System Open
Market Account.
BANK OBSERVATIONS
DIVISION OF

Honorable Roy A. Young, President,
Federal Reserve Bank of Boston,
Boston, Mass.

SEP 30 1940
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CONFIDENTIAL

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON OCTOBER 1, 1940

(In thousands of dollars)

	System	Boston	New York	Philadelphia	Cleveland	Richmond	Atlanta	Chicago	St. Louis	Minneapolis	Kansas City	Dallas	San Francisco
A - Expenses													
1. Estimated current expenses, 1940	28,897	2,127	7,297	2,341	2,862	1,717	1,243	3,372	1,518	974	1,731	1,243	2,452
B - Earnings													
1. Estimated current earnings, 1940 (exclusive of earnings on Govts.)	1,420	69	262	200	104	97	55	218	26	26	172	39	152
2. Estimated earnings on Govts. to September 30	31,935	2,314	9,687	2,568	3,266	1,616	1,272	3,442	1,458	949	1,492	1,230	2,641
3. Net profits on Govts. to Sept. 26	3,003	219	872	252	298	157	128	332	136	94	147	115	253
4. Total	36,358	2,602	10,821	3,020	3,668	1,870	1,455	3,992	1,620	1,069	1,811	1,384	3,046
C. Estimated dividends, 1940	8,210	560	3,065	714	841	318	279	825	248	177	264	217	672
D. Excess of A-1 plus C over B-4	749	85	-459	35	55	165	67	205	146	82	184	106	78
E. Allocation required (on basis of 1.72353% earnings rate on Govts.) to provide earnings October-December equal to D	172,444	19,566	105,658	8,057	12,661	37,982	15,423	17,189	33,608	18,876	42,355	24,100	17,955
F. Allocation of remainder of System holdings (\$2,433,600,000 less \$172,444,000) on basis of C	2,261,186	154,234	844,158	196,649	231,627	87,583	76,843	227,220	68,304	48,719	72,710	68,028	185,081
G. Total allocation of Govts. (E plus F)	2,433,600	173,800	738,500	204,706	244,288	125,565	92,266	274,409	101,912	67,625	115,065	92,428	203,036
H. Present allocations	2,433,600	177,588	744,996	193,007	249,572	121,994	89,290	258,319	112,870	71,727	115,198	94,972	204,067
I. Change in allocations	--	-3,788	-6,496	+11,699	-5,284	+3,571	+2,976	+16,090	-10,958	-4,102	-133	-2,544	-1,031

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REC'D - N FILES SECTION
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September 26, 1940. *fb*

REPORT TO MEMBERS OF THE FEDERAL OPEN MARKET COMMITTEE AND
PRESIDENTS OF THE FEDERAL RESERVE BANKS ON ACCOUNTING PROCEDURE
IN CONNECTION WITH THE SYSTEM OPEN MARKET ACCOUNT

At the meetings of the Federal Open Market Committee in Washington on March 20 and May 28, 1940, we were requested to study the present basis for the allocation of securities in the System Open Market Account and the accounting procedure followed in connection with the Account, to make a report to the Federal Open Market Committee and to the Presidents of the Federal Reserve Banks which would include a statement of the various accounting procedures that might be adopted for the System Account, and to be prepared to make recommendations as to the procedure that should be followed.

As we see the problem, there are three main questions to be considered: (1) how should United States Government securities owned by the Federal Reserve Banks be shown in the weekly press statement, (2) what should be the disposition of profits on sales of securities, and (3) should there be any change in the procedure under which participations in the System Account are now allocated among the Federal Reserve Banks?

Draft filed 9/25/40

See attached note

copy filed

see letter 10/2/40 To Rouse
see letter 10/2/40 To Young

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Amounts at which securities are shown in published condition statements.

The Federal Reserve Act, section 11, paragraph 2 (a), provides: "The Board of Governors of the Federal Reserve System shall be authorized and empowered: To examine at its discretion the accounts, books and affairs of each Federal reserve bank and of each member bank and to require such statements and reports as it may deem necessary. The said board shall publish once each week a statement showing the condition of each Federal reserve bank and a consolidated statement for all Federal reserve banks. Such statements shall show in detail the assets and liabilities of the Federal reserve banks, single and combined, and shall furnish full information regarding the character of the money held as reserve and the amount, nature and maturities of the paper and other investments owned or held by Federal reserve banks."

It is the present practice to show Government securities in the statement at par and to include premium on securities purchased in "Other Assets" and discount on securities purchased in "Other Liabilities". Two alternative methods have been suggested for showing the System's holdings of Government securities in the weekly Federal Reserve Bank condition statement, as follows: (1) show securities at book value, i.e., at par plus premium and less discount, and (2) show the par value of the securities as at present and show the amount of premium less discount as a separate asset item in the statement.

With respect to the current method, the following comments are offered: It has been the practice since early in the history of

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the System to show securities in published statements at their par value. A schedule is also appended to the weekly publication of the statement of condition, showing at par value the maturity distribution of U. S. Government securities. Securities in the statement are shown at par value principally, we understand, in order to indicate as clearly as possible any increase or decrease in the System account, and to obviate any possibility of the public's gaining the impression that there has been a change in the System's holdings, when, as a matter of fact, no change has taken place. Par value is used in the maturity schedule for the same reason and also to indicate as clearly as possible in what maturity categories changes occur. Changes in security holdings as disclosed by the statement are likely to be interpreted by the public as reflecting purchases and sales. Under the present arrangement all purchases and sales, except those that represent switches within a given maturity group, are reflected in the statement. Shifts of equal amounts within a given maturity grouping would not be clarified by either of the alternative methods.

With respect to the first alternative method, i.e., that securities be shown at book value, reported holdings would fluctuate as a result of the following, as well as through purchases, sales and shifts: (1) amortization of premium, which would reduce book value, (2) accumulation of discount, which would increase book value, and (3) valuation reserves and charge-offs. If United States Government securi-

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ties were shown among assets in press statements at book value, they would normally be shown likewise in the maturity classification, but if thought desirable, they could continue to be shown in the maturity classification at par value.

With respect to the second suggestion, it would be a simple matter to show "Net premium on U. S. Securities" as an asset item, say, following "Total bills and securities". Opinion has been expressed that minor changes in book value brought about by amortization of premium, accumulation of discount, shifts within maturity categories and application of reserves and charge-offs, should be shown clearly. It has also been suggested that if public attention were called to such changes by inclusion of an item in the published statement, the public might get an impression of a change in System holdings when no real change has occurred.

No accounting difficulties would be involved in showing United States Government securities in the weekly press statements in either of the above alternative ways, and neither would involve any material changes in the accounting procedure now followed.

What should be the disposition of profits on sales of securities?

Present Procedure

In accordance with the plans approved by the Federal Open Market Committee on November 30, 1937, effective January 1, 1938, profits on sales of United States Government securities have been distributed among the Federal Reserve Banks in proportion to their average

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daily holdings in the System Account since June 30, 1936, and are now treated as an addition to current net earnings and used to cover expenses or dividends, or are transferred to surplus, or to reserves for contingencies through surplus, depending upon the situation at each Federal Reserve Bank.

Reasons for Present Procedure

From 1924 to 1929, inclusive, profits were distributed daily on the holding ratio. From 1930 to 1936, inclusive, they were held by the New York Reserve Bank in a suspense account and distributed at the end of each year on ratios based on daily average holdings in the Account for the last 12 months preceding. In 1937 profits were distributed daily on ratios based on average daily holdings in the Account for the last twelve months preceding. Since January 1, 1938, as outlined in the memorandum on accounting procedure for handling transactions in the System Open Market Account adopted beginning January 1, 1938, profits have been distributed daily on ratios based on the average daily holdings in the Account since June 30, 1936. This relating of profits and losses more nearly to the period over which securities are held by lengthening the period over which the average holdings are figured in distributing profits, largely removes the apprehension that a bank might, in some time of emergency, find it necessary to take over from other banks a substantial block of Governments on which, within a short period, it might sustain serious loss, for the loss, if any, would be distributed in accordance with the bank's holdings of securities over an extended period rather than for any short period.

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A change has been suggested in our accounting procedure with respect to the treatment of profits realized on sales of securities. The principal reasons advanced therefor, are that during the generally rising market of the past few years, principally through switches, (1) the book value of the Account has been written up, and (2) profits have been treated in a manner not in accord with the practice which the System recommends to member banks. The view has been expressed that the System's "Reserves for Contingencies" should be increased at least to the point that they equal the net premium on securities in the Account, and that the writing up of the Account by switches should be minimized by the application of profits so realized to the reduction of the book value of the replacement securities.

Reserves for contingencies now held by the Federal Reserve Banks as a whole amount to \$34,627,011, as compared with \$38,131,196 of premium carried in the System Account as of September 11, 1940. Of the total contingent reserves, \$31,481,946 were set up out of current net earnings and \$3,145,068 out of surplus. Reserves for contingencies vary from slightly over 57 per cent of the premium account at Boston to more than 100 per cent of the premium account at four of the banks.

Realized profits might be used as indicated in one of the following alternative suggestions as to our accounting procedure:

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Alternative Suggestions for Accounting of Security Profits

Profits on sales of securities could be--

1. Transferred to Reserves for Contingencies;
2. Set aside as a valuation reserve and deducted in the balance sheet from premium on U. S. securities;
3. Used to write down the book value of the System Account.

Profits may be realized not only on outright sales of securities but also on switches, i.e., the simultaneous sale of one security and purchase of a like par value of another. Under our present practice, when securities carried on the books at amortized price of, say, 101 are sold at a profit of 2 points and other securities are bought at 103, profits on securities sold are increased and the net book value of the portfolio is increased by a like amount. Switches in the account might leave the net book value of the account unchanged and at the same time reduce current earnings. The advisability of this so-called writing-up of the portfolio as a result of sales and purchases may be questioned, but if profits on switches or outright sales of securities, or both, are to be used to write down the book value of the System Account they should, in our opinion, continue to be shown as profits on sales of securities in published statements of earnings and expenses of the Federal Reserve Banks.

With respect to the first alternative, the transfer of profits on sales of securities to reserves for contingencies would regularize

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a practice which has existed to a substantial extent for a number of years. Prior to 1937, transfers to reserves for contingencies were charged against the current year's earnings. Since that date, they have been charged to surplus. Reserves for contingencies are included in the balance sheet of the Reserve Banks among "Other Capital Accounts". They are not shown as a reduction in the carrying value of assets.

With respect to the second alternative, that is, that profits on sales of securities be set aside as a valuation reserve and deducted in the balance sheet from the premium account, it may be pointed out that if this were done and a substantial portion of our present contingent reserves were also allocated for that purpose, the time would come when the valuation reserve would equal the value of the premium account. In such case the amortization of premium would not have to be discontinued, but the combined result of the valuation reserve and true amortization of premium would reduce, in effect, the book value of the System Account below par value. The latter course would not be inconsistent, as there is no particular connection between the amount of profits taken and the premium account. The amount of possible loss that might be realized is not limited to the premium account. It is regarded as sound practice to set up such reserves when funds are available and to maintain them at a point adequate for the contingency. That point obviously is a variant and requires constant consideration.

The third alternative, i.e., the use of profits on sales of securities to write down the book value of the System Account, would

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make it necessary to distribute these profits among the Federal Reserve Banks on the basis of their current participations in the System Account. It would not be practicable to apply them on the basis of average participations in the System Account since June 30, 1936, and retain the present set-up of the pool account.

We should like to point out that the use of profits to write off premiums would probably result soon in losing sight of the true earnings on any given issue and of the true profit and loss on a sale. We assume that if profits were used to write down book value, such action would be arbitrary and not involve the writing up of securities if losses are sustained.

In the event that consideration is given to partial revision, it may again be mentioned that switches in the Account that result in a profit from the sale, often write up the account. In such transactions the sale and purchase are practically simultaneous, and it may be argued that the profit realized is not a true profit until the replacement security is sold, and therefore the profit on the sale should be used to write down the cost of the replacement security. However, if the securities sold and purchased are not of the same general maturity, the switch may appear in a different light. The sale of "rights" and their replacement with other securities represents perhaps the clearest case arguing for application of the profit on the sale to reduce the cost of the replacement security because the profit results primarily from the exchange value of "rights" and because the replacement securities

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purchased in the open market would produce a relatively lower yield than if the "rights" had been exercised.

Should it be decided to reduce book value and charge off all or a large part of the present premium account, the amount to be charged off by each Federal Reserve Bank, in the absence of instructions to the contrary, would be applied on the basis of its current participation in the System Account in accordance with the present method of apportioning accrued interest, premium and discount.

Should it be decided to allocate profits realized on sales of securities to contingency reserves until further notice or until the amount of such reserves bore some certain relation to the System Account, such profits should be taken into the books of the several banks on the basis of the present formula for distributing profits.

Had profits on sales of United States Government securities been used during recent years to write down book value of the portfolio or to establish valuation reserves, there would have been deficits in net earnings of the Federal Reserve Banks, after dividends, in 1935, 1936, and 1938.

Quarterly allocations of securities among Federal Reserve Banks.

The procedure now followed in allocating participations in the System Account among the Federal Reserve Banks provides, first, for allocating a sufficient amount of securities to each Federal Reserve Bank to cover its expenses not taken care of by other earnings, and, second, to allocate the remaining securities in the System Account

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among the Federal Reserve Banks on the basis of their dividend requirements. The relationship between the expenses of individual Federal Reserve Banks and total expenses of the System is quite different from the relationship between dividend payments by individual Federal Reserve Banks and total dividend payments by the System. Since profits on sales of securities are now taken into earnings and thus reduce the amount of securities needed by the Federal Reserve banks to produce sufficient income to cover expenses, it is apparent that as profits increase, the amount of securities allocated to the Federal Reserve Banks to cover their expenses decreases, and the amount of securities allocated to the Federal Reserve Banks on the basis of dividend requirements increases. When these profits are substantial there is a substantial fluctuation in participations in the System Account on quarterly reallocation dates. These fluctuations could be materially reduced if realized profits were not taken into account in making allocations of securities among the Federal Reserve Banks. There would also be considerable merit in distributing securities not needed to cover expenses and dividends on the basis of each Bank's average participation in the System Account as, during periods when the bulk of the portfolios of the Federal Reserve Banks is made up of Government securities, losses, if any, which the Federal Reserve Banks sustain, would result principally from depreciation in market value of Government securities. This is the basis on which profits on sales of securities in the System Account are now distributed among the Federal Reserve Banks.

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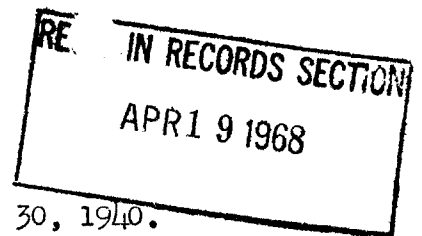
If this procedure were adopted, the quarterly reallocation would be as follows: (1) allocate sufficient securities to each Bank to cover expenses not covered by accrued earnings on Government securities and estimated earnings from other sources, (2) allocate a sufficient amount of additional securities to each Bank to cover dividend requirements, and (3) allocate any remaining securities among the Banks on the basis of average daily participations in the System Account since June 30, 1936. When estimated earnings equal or exceed estimated expenses and dividends, steps 1 and 2, indicated above, could be combined thus simplifying the allocation procedure.

If the Federal Open Market Committee desires, we shall be prepared to make recommendation on points discussed above.

R. G. Rouse

E. L. Smead

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September 30, 1940.

NOTE:

With respect to the last paragraph of the attached memorandum, my recommendations would, in general, be as follows:

1. Weekly press statements.

Recommend no change, but see no particular objection to showing net premium as a separate item.

2. Treatment of profits.

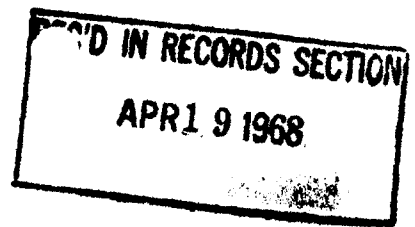
Recommend no change. Use of profits to write down premium would increase current earnings and thus give an exaggerated impression as to real earnings on System Account and would make it impossible to determine real earnings or real profits from the published statements.

3. Allocations of securities in System Account.

Recommend that securities be distributed as follows: (1) Allocate sufficient securities to each bank to cover expenses not covered by accrued earnings on Government securities and estimated earnings from other sources, (2) Allocate a sufficient amount of securities to each bank to cover dividend requirements, and (3) allocate any remaining securities among the banks on the basis of average daily participations in the System Account since June 30, 1936.

E. L. Smead

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If this procedure were adopted, the quarterly reallocation would be as follows: (1) allocate sufficient securities to each Bank to cover expenses not covered by accrued earnings on Government securities and estimated earnings from other sources, (2) allocate a sufficient amount of additional securities to each Bank to cover dividend requirements, and (3) allocate any remaining securities among the Banks on the basis of average daily participations in the System Account since June 30, 1936. When estimated earnings equal or exceed estimated expenses and dividends, steps 1 and 2, indicated above, could be combined thus simplifying the allocation procedure.

If the Federal Open Market Committee desires, we shall be prepared to make recommendation on points discussed above.

R. G. Rouse

E. L. Smith

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SEP 26 1940
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September 26, 1940.

Mr. R. G. Rouse, Vice President,
Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Rouse:

There is enclosed a copy of the statement prepared in this Division showing the changes necessary in allocations of Government securities in the System Open Market Account on October 1, 1940. Current expenses and current earnings other than on Government securities are estimated on the basis of actual earnings January through August. The St. Louis figure for estimated current expenses on this basis was adjusted by adding \$150,000, as was done in previous reallocations this year.

Very truly yours,

E. L. Smead, Chief,
Division of Bank Operations.

Handwritten initials and scribbles

Enclosure
MD:ts

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For Files
S. E. Hamor

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SEP 26 1940

Explanation of basis for items indicated

- A-1 1.5 times current expenses January-August adjusted by adding \$150,000 to the estimate for St. Louis, as in previous reallocations this year.
- B-1 1.5 times earnings exclusive of earnings on Governments January-August.
- B-2 and B-3 Obtained or confirmed by telephone from Mr. Behrens at New York, September 25.
- C Dividends paid and accrued, August 31 plus two per cent of paid-in capital on August 31.
- E Actual rate used .004342.

REC'D IN FILES SECTION

CONFIDENTIAL

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON OCTOBER 1, 1940

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A - Expenses													
1. Estimated current expenses, 1939	28,897	2,127	7,297	2,311	2,852	1,717	1,213	3,372	1,518	974	1,731	1,213	2,152
B - Earnings													
1. Estimated current earnings, 1940 (exclusive of earnings on Govts.)	1,120	69	262	200	104	97	55	218	26	26	172	39	152
2. Estimated earnings on Govts. to September 30	31,935	2,311	9,687	2,568	3,266	1,616	1,272	3,112	1,158	919	1,192	1,230	2,611
3. Net profits on Govts. to Sept. 26	3,003	219	872	252	298	157	128	332	136	91	117	115	253
4. Total	36,358	2,602	10,821	3,020	3,668	1,870	1,455	3,992	1,620	1,069	1,811	1,384	3,016
C. Estimated dividends, 1940	8,210	560	3,065	711	811	318	279	825	218	177	261	217	672
D. Excess of A-1 plus C over B-4	719	85	-159	35	55	165	67	205	116	82	181	106	78
E. Allocation required (on basis of 1.72353% earnings rate on Govts.) to provide earnings October-December equal to D	172,111	19,566	105,658	8,057	12,661	37,982	15,123	17,189	33,608	18,876	12,355	21,100	17,955
F. Allocation of remainder of System holdings (\$2,133,600,000 less \$172,111,000) on basis of C	2,261,186	151,231	811,158	196,619	231,627	87,583	76,813	227,220	68,301	118,719	72,710	68,028	185,081
G. Total allocation of Govts. (E plus F)	2,133,600	173,800	738,500	201,706	211,288	125,565	92,266	271,109	101,912	67,625	115,065	92,128	203,036
H. Present allocations	2,133,600	177,588	711,996	193,007	219,572	121,991	89,290	258,319	112,870	71,727	115,198	91,972	201,067
I. Change in allocations	—	-3,788	-6,196	+11,699	-5,281	+3,571	+2,976	+16,090	-10,958	-4,102	-133	-2,511	-1,031

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*Draft sent to
 on Wednesday Sept 25
 file 9/26/40*

At the meetings of the Federal Open Market Committee in Washington on March 20 and May 28, 1940, we were requested to study the present basis for the allocation of securities in the System Open Market Account and the accounting procedure followed in connection with the Account, to make a report to the Federal Open Market Committee and to the Presidents of the Federal Reserve Banks which would include a statement of the various accounting procedures that might be adopted for the System Account, and to be prepared to make recommendations as to the procedure that should be followed.

As we see the problem, there are three main questions to be considered: (1) how should United States Government securities owned by the Federal Reserve Banks be shown in the weekly press statement, (2) what should be the disposition of profits on sales of securities, and (3) should there be any change in the procedure under which participations in the System Account are now allocated among the Federal Reserve Banks?

see 9/26/40

Directive #

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Amounts at which securities are shown in published condition statements.

The Federal Reserve Act, section 11, paragraph 2 (a), provides:

"The Board of Governors of the Federal Reserve System shall be authorized and empowered: To examine at its discretion the accounts, books and affairs of each Federal reserve bank and of each member bank and to require such statements and reports as it may deem necessary. The said board shall publish once each week a statement showing the condition of each Federal reserve bank and a consolidated statement for all Federal reserve banks. Such statements shall show in detail the assets and liabilities of the Federal reserve banks, single and combined, and shall furnish full information regarding the character of the money held as reserve and the amount, nature and maturities of the paper and other investments owned or held by Federal reserve banks."

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With respect to the current method, the following comments are

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Present Procedure

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Reasons for Present Procedure

From 1921 to 1929, inclusive, profits were distributed daily on the holding ratio. From 1930 to 1936, inclusive, they were held by the New York Reserve Bank in a suspense account and distributed at the end of each year on ratios based on daily average holdings in the Account for the last 12 months preceding. In 1937 profits were distributed daily on ratios based on average daily holdings in the Account for the last twelve months preceding. Since January 1, 1938, as outlined in the memorandum on accounting procedure for handling transactions in the System Open Market Account adopted beginning January 1, 1938, profits have been distributed daily on ratios based on the average daily holdings in the Account since June 30, 1936. This relating of profits and losses more nearly to the period over which securities are held by lengthening the period over which the average holdings are figured in distributing profits, largely removes the apprehension that a bank might, in some time of emergency, find it necessary to take over from other banks a substantial block of Governments on which, within a short period, it might sustain serious loss, for the loss, if any, would be distributed in accordance with the bank's holdings of securities over an extended period rather than

- 6 -

for any short period.

A change has been suggested in our accounting procedure with respect to the treatment of profits realized on sales of securities. The principal reasons advanced therefor, are that during the generally rising market of the past few years, principally through switches, (1) the book value of the Account has been written up, and (2) profits have been treated in a manner not in accord with the practice which the System recommends to member banks. The view has been expressed that the System's "Reserves for Contingencies" should be increased at least to the point that they equal the net premium on securities in the Account, and that the writing up of the Account by switches should be minimized by the application of profits so realized to the reduction of the book value of the replacement securities.

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With respect to the second alternative, that is, that profits on sales of securities be set aside as a valuation reserve and deducted in the balance sheet from the premium account, it may be pointed out that if this were done and a substantial portion of our present contingent reserves were also allocated for that purpose, the time would come when the valuation reserve would equal the value of the premium account. In such case the amortization of premium would not have to be discontinued, but the combined result of the valuation reserve and true amortization of premium would reduce, in effect, the book value of the System Account below par value. The latter course would not be inconsistent, as there is no particular connection between the amount of profits taken and the premium account. The amount of possible loss that might be realized is not limited to the premium account. It is regarded as sound practice to set up such reserves when funds are available and to maintain them at a point adequate for the contingency. That point obviously is a variant and requires constant consideration.

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necessary to distribute these profits among the Federal Reserve Banks on the basis of their current participations in the System Account. It would not be practicable to apply them on the basis of average participations in the System Account since June 30, 1936, and retain the present set-up of the pool account.

We should like to point out that the use of profits to write off premiums would probably result soon in losing sight of the true earnings on any given issue and of the true profit and loss on a sale. We assume that if profits were used to write down book value, such action would be arbitrary and not involve the writing up of securities if losses are sustained.

In the event that consideration is given to partial revision, it may again be mentioned that switches in the Account that result in a profit from the sale, often write up the account. In such transactions the sale and purchase are practically simultaneous, and it may be argued that the profit realized is not a true profit until the replacement security is sold, and therefore the profit on the sale should be used to write down the cost of the replacement security. However, if the securities sold and purchased are not of the same general maturity, the switch may appear in a different light. The sale of "rights" and their replacement with other securities represents perhaps the clearest case arguing for application of the profit on the sale to reduce the cost of the replacement security because the profit results primarily from the exchange value of "rights" and because the replacement securities purchased in the open market would

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produce a relatively lower yield than if the "rights" had been exercised.

Should it be decided to reduce book value and charge off all or a large part of the present premium account, the amount to be charged off by each Federal Reserve Bank, in the absence of instructions to the contrary, would be applied on the basis of its current participation in the System Account in accordance with the present method of apportioning accrued interest, premium and discount.

Should it be decided to allocate profits realized on sales of securities to contingency reserves until further notice or until the amount of such reserves bore some certain relation to the System Account, such profits would be taken into the books of the several banks on the basis of the present formula for distributing profits.

Had profits on sales of United States Government securities been used during recent years to write down book value of the portfolio or to establish valuation reserves, there would have been deficits in net earnings of the Federal Reserve Banks, after dividends, in 1935, 1936, and 1938.

Quarterly allocations of securities among Federal Reserve Banks.

The procedure now followed in allocating participations in the System Account among the Federal Reserve Banks provides, first, for allocating a sufficient amount of securities to each Federal Reserve Bank to cover its expenses not taken care of by other earnings, and, second, to allocate the remaining securities in the System Account among the Federal Reserve Banks on the basis of their dividend requirements. The relationship

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between the expenses of individual Federal Reserve Banks and total expenses of the System is quite different from the relationship between dividend payments by individual Federal Reserve Banks and total dividend payments by the System. Since profits on sales of securities are now taken into earnings and thus reduce the amount of securities needed by the Federal Reserve banks to produce sufficient income to cover expenses, it is apparent that as profits increase, the amount of securities allocated to the Federal Reserve Banks to cover their expenses decreases, and the amount of securities allocated to the Federal Reserve Banks on the basis of dividend requirements increases. When these profits are substantial there is a substantial fluctuation in participations in the System Account on quarterly reallocation dates. These fluctuations could be materially reduced if United States securities in System Account not needed to cover expense and dividend requirements were allocated among the Federal Reserve Banks on the basis of their average daily participation in the Account since June 30, 1936. This is the basis on which profits on sales of securities in the System Account are now distributed among the Federal Reserve Banks. During periods when the bulk of the portfolio of the Federal Reserve Banks is made up of Government securities, losses, if any, which the Federal Reserve Banks sustain would result principally from depreciation in market value of Government securities and, consequently, there would appear to be considerable merit in distributing securities not needed to cover expense and dividend requirements on the basis of each bank's average participation in the System Account. If this were done, an additional third step would

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be involved in the quarterly reallocation of the System Account. The reallocation would be as follows: (1) allocate sufficient securities to each Bank to cover expenses not covered by accrued earnings on Government securities, estimated earnings from other sources, and profits, (2) allocate a sufficient amount of additional securities to each Bank to cover dividend requirements, and (3) allocate any remaining securities among the Banks on the basis of average daily participations in the System Account since June 30, 1936.

If the Federal Open Market Committee desires, we shall be prepared to make recommendations with respect to the points discussed above.

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FEDERAL RESERVE BANK
OF NEW YORK

September 4, 1940.

Dear Mr. Smead:

Enclosed is a new draft of our pending joint report to the Federal Open Market Committee on the subject of allocation of securities in System Open Market Account and the accounting procedure in connection with it. I had hoped to prepare a letter to go along with it, but there was not an opportunity today and there will not be tomorrow. Accordingly, it seems better to let it go to you "as is" rather than to hold it up for comment or further editing.

In accordance with our recent telephone conversation, I suggest that after you have had a chance to check the report, you spend a day here so that we may have whatever discussion is necessary as to the report and our recommendations.

With kind regards, I am

Very truly yours,

Robert G. Rouse
Robert G. Rouse,
Vice President.

Mr. Edward L. Smead,
Chief, Division of Bank Operations,
Board of Governors of the Federal Reserve System,
Washington, D. C.

Enc.

FOR FILE
L. S. SMITH

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REVISED DRAFT OF MEMORANDUM TO FEDERAL OPEN MARKET COMMITTEE

September 3, 1940.

At the meeting of the Federal Open Market Committee in Washington on March 20, 1940, we were requested to study the present basis for the allocation of securities in the System Open Market Account and the accounting procedure followed in connection with the Account, to make a report to the Federal Open Market Committee and to the Presidents of the Federal Reserve banks which would include a statement of the various accounting procedures that might be adopted for the System Account, and to be prepared to make recommendations as to the procedure that should be followed.

As we see the problem, there are three main questions to be considered: (1) how should United States Government securities owned by the Federal Reserve banks be shown in the weekly press statement, (2) what should be the disposition of profits on sales of securities, and (3) should there be any change in the procedure under which participations in the System Account are now allocated among the Federal Reserve banks?

Amounts at which securities are shown in published condition statements.

The Federal Reserve Act, section 11, paragraph 2 (a), provides: "The Board of Governors of the Federal Reserve System shall be authorized and empowered: To examine at its discretion the accounts, books and affairs of each Federal reserve bank and of each member bank and to require such statements and reports as it may deem necessary. The said board shall publish once each week a statement showing the condition of each Federal reserve bank and a consolidated statement for all Federal reserve banks. Such statements shall show in detail the assets and liabilities of the Federal reserve banks, single and combined, and shall furnish full information regarding the character of the money held as reserve and the amount, nature and maturities of the paper and other investments owned or held by Federal reserve banks."

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It is the present practice to show Government securities in the statement at par and to include premium on securities purchased in "Other Assets" and discount on securities purchased in "Other Liabilities". Two alternative methods have been suggested for showing the System's holdings of Government securities in the weekly Federal Reserve bank condition statement, as follows: (1) show securities at book value, i.e., at par plus premium and less discount, and (2) show the par value of the securities as at present and show the amount of premium less discount as a separate asset item in the statement.

With respect to the current method, the following comments are offered: It has been the practice since early in the history of the System to show securities in published statements at their par value. A schedule is also appended to the weekly publication of the statement of condition, showing at par value the maturity distribution of U. S. Government securities. Securities in the statement are shown at par value principally, we understand, in order to indicate as clearly as possible any increase or decrease in the System account, and to obviate any possibility of the public's gaining the impression that there has been a change in the System's holdings, when, as a matter of fact, no change has taken place. Par value is used in the maturity schedule for the same reason and also to indicate as clearly as possible in what maturity categories changes occur. Therefore, all security changes in the account are indicated with the exception of shifts of equal amounts within a given maturity grouping, which would not be clarified by either of the alternative methods.

The present method is well understood by the public and is simple in operation. It also appears to meet the requirements of the statute.

With respect to the first alternative method, i.e., that securities be shown at book value, reported holdings would fluctuate as a result of the

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following, as well as through purchases, sales and shifts: (1) amortization of premium, which would reduce book value, (2) accumulation of discount, which would increase book value, and (3) valuation reserves and charge-offs. If United States Government securities were shown among assets in press statements at book value, they would normally be shown likewise in the maturity classification, but if thought desirable, they could continue to be shown in the maturity classification at par value.

With respect to the second suggestion, it would be a simple matter to show "Net premium on U. S. Securities" as an asset item, say, following "Total bills and securities". Opinion has been expressed that minor changes in book value brought about by amortization of premium, accumulation of discount, shifts within maturity categories and application of reserves and charge-offs, should be shown clearly. On the other hand, such changes, if public attention were called to them by means of such a balance sheet item, carry the possibility of a public impression of a change in System holdings when no real change has occurred, and in themselves do not clarify the statement.

No accounting difficulties would be involved in showing United States Government securities in the weekly press statements in either of the above alternative ways, and neither would involve any material changes in the accounting procedure now followed, although the present method is somewhat simpler to handle.

What should be the disposition of profits on sales of securities?

Present Procedure

In accordance with the plans approved by the Federal Open Market Committee on November 30, 1937, effective January 1, 1938, profits on sales of United States Government securities have been distributed among the Federal Reserve banks in proportion to their average daily holdings in the System Account

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since June 30, 1936, and are now treated as an addition to current net earnings and used to cover expenses or dividends, or are transferred to surplus, or to reserves for contingencies through surplus, depending upon the situation at each Federal Reserve bank.

Reasons for Present Procedure

From 1924 to 1929, inclusive, profits were distributed daily on the holding ratio. From 1930 to 1936, inclusive, they were held by the New York Reserve bank in a suspense account and distributed at the end of each year on ratios based on daily average holdings in the Account for the last 12 months preceding. In 1937 profits were distributed daily on ratios based on average daily holdings in the Account for the last twelve months preceding. Since January 1, 1938, as outlined in the memorandum on accounting procedure for handling transactions in the System Open Market Account adopted beginning January 1, 1938, profits have been distributed daily on ratios based on the average daily holdings in the Account since June 30, 1936, on the theory that under this plan Reserve banks are less affected as to any profits or losses by current readjustments in the amount of their holdings. This relating of profits and losses to the period over which securities are held by lengthening the period over which the average holdings (profit and loss ratio) are figured, largely removes the apprehension that a bank might, in some time of emergency, find it necessary to take over from other banks a substantial block of Governments on which, within a short period, it might sustain serious loss, for the loss, if any, would be distributed in accordance with the bank's holdings of securities over an extended period rather than for any short period.

A change has been suggested in our accounting procedure with respect to the treatment of profits realized on sales of securities and the principal

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reasons advanced therefor, are that the System Account, during the generally rising market of the past few years through switches, (1) has written up the book value of the Account, and (2) has treated profits in a manner not in accord with the practice which the System recommends to member banks. The view has been expressed that the System's "Reserves for Contingencies" should be increased at least to the point that they equal the net premium on securities in the Account and that the writing up of the Account by switches should be minimized by the application of profits so realized to the reduction of the cost of the replacement securities on our books.

Reserves for contingencies now held by the Federal Reserve banks as a whole amount to \$ _____, as compared with \$ _____ of premium carried in the System Account as of September _____, 1940. Of the total contingent reserves, \$ _____ were set up out of current net earnings and \$ _____ out of surplus. The System could use \$ _____ of contingent reserves set aside out of earnings as an offset to the premium carried on its books, if at any time it should determine that these reserves are in reality reserves for the contingencies related to our securities rather than "capital accounts". Such application might be along the line indicated in #2 or #3 of the following alternative suggestions as to our accounting procedure:

Alternative Suggestions for Accounting of Security Profits *

Profits on sales of securities could be -

1. Transferred to Reserves for Contingencies;
2. Set aside as a valuation reserve and deducted in the balance sheet from premium on U. S. securities in the item "Other Assets";
3. Used to write down the book value of the System Account.

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* Profits may be realized not only on outright sales of securities but also on switches, i.e., the simultaneous sale of one security and purchase of a like par value of another. Under our present practice, when securities carried on the books at amortised price of, say, 101 are sold at a profit of 2 points and other securities are bought at 103, profits on securities sold are increased and the net book value of the portfolio is increased by a like amount. This ~~writing-up could consist of no change in net book value with a reduction in earnings.~~ As the advisability of this so-called writing-up of the portfolio as a result of such sales and purchases may be questioned, the two sources of profits may be considered separately in studying this problem. If profits on switches or outright sales of securities, or both, should be used to write down the book value of the System Account, in our opinion, they should continue to be shown as profits on sales of securities in published statements of earnings and expenses of the Federal Reserve banks.

With respect to the first alternative, the transfer of profits on sales of securities to reserves for contingencies would regularize a practice which has existed to a substantial extent for a number of years. Prior to 1937, transfers to reserves for contingencies were charged against the current year's earnings. Since that date, they have been charged to surplus. Reserves for contingencies are included in the balance sheet of the Reserve banks among "Other Capital Accounts". They are not shown as a reduction in the carrying value of assets. The current plan up to this time has been regarded as sound from an accounting standpoint, and is flexible in that it can meet changing conditions. The principal criticisms have been those stated above.

With respect to the second alternative, that is, that profits on sales of securities be set aside as a valuation reserve and deducted in the

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balance sheet from the present title "Other Assets", it may be pointed out that if this were done and a substantial portion of our present contingent reserves were also allocated for that purpose, the time would come when the valuation reserve would equal the value of the premium account. In such case the amortization of premium would not have to be discontinued, but the combined result of the valuation reserve and true amortization of premium would reduce, in effect, the book value of the System Account below par value. The latter course would not be inconsistent, as there is no particular connection between the amount of profits taken and the premium account. The amount of possible loss that might be realized is not limited to the premium account. It is regarded as sound practice to set up such reserves when funds are available and to maintain them at a point adequate for the contingency. That point obviously is a variant and requires constant consideration.

The third alternative, i.e., the use of profits on sales of securities to write down the book value of the System Account, would make it necessary to distribute these profits among the Federal Reserve banks on the basis of their current participations in the System Account. It would not be practicable to apply them on the basis of average participations in the System Account since June 30, 1936, and retain the present set-up of the pool account.

We should like to point out that the arbitrary ~~write-down~~ of book values would probably result soon in losing sight of the cost of any given issue in terms of current book value^{and} of the true profit and loss on a sale. We assume that if profits were used to write down book value, such action would be arbitrary and not involve the writing up of securities if losses are sustained.

In the event that consideration is given to partial revision, it may again be mentioned that switches in the Account that result in a profit from

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the sale, often write up the account. In such transactions the sale and purchase are practically simultaneous, and it may be argued that the profit realized is not a true profit until the replacement security is sold, and therefore the profit on the sale should be used to write down the cost of the replacement security. However, if the securities sold and purchased are not of the same general maturity, the switch may appear in a different light. The sale of "rights" and their replacement with other securities represents perhaps the clearest case arguing for application of the profit on the sale to reduce the cost of the replacement security because the profit results primarily from the exchange value of "rights" and because the replacement securities purchased in the open market would produce a relatively lower yield than if the "rights" had been exercised.

Should it be decided to reduce book value and charge off all or a large part of the present premium account, the amount to be charged off by each Federal Reserve bank, in the absence of instructions to the contrary, would be applied on the basis of its current participation in the System Account and not on the ratios based on average daily participation in the Account since June 30, 1936, in order to avoid (1) changing the present method of treating the Account as a pool account, and (2) changing the present method of apportioning of accrued interest, premium and discount.

Should it be decided to allocate profits realized on sales of securities to contingency reserves until further notice or until the amount of such reserves bore some certain relation to the System Account, such profits would be taken into the books of the several banks on the basis of the present formula for distributing profits.

Had profits on sales of United States Government securities been used during recent years to write down book value of the portfolio or to

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establish valuation reserves, there would have been deficits in net earnings of the Federal Reserve banks, after dividends, in 1935, 1936 and 1938.

Quarterly allocations of securities among Federal Reserve banks.

The procedure now followed in allocating participations in the System Account among the Federal Reserve banks provides, first, for allocating a sufficient amount of securities to each Federal Reserve bank to cover its expenses not taken care of by other earnings, and, second, to allocate the remaining securities in the System Account among the Federal Reserve banks on the basis of their dividend requirements. The relationship between the expenses of individual Federal Reserve banks and total expenses of the System is quite different from the relationship between dividend payments by individual Federal Reserve banks and total dividend payments by the System. Since profits on sales of securities are now taken into earnings and thus reduce the amount of securities needed by the Federal Reserve banks to produce sufficient income to cover expenses, it is apparent that as profits increase, the amount of securities allocated to the Federal Reserve banks to cover their expenses decreases, and the amount of securities allocated to the Federal Reserve banks on the basis of dividend requirements increases. When these profits are substantial there is a substantial fluctuation in participations in the System Account on quarterly reallocation dates. These fluctuations could be materially reduced if profits on sales of securities were set aside as realized as a protection against future losses and if our formula for allocating securities among the Federal Reserve banks were expanded to embrace three steps instead of the present two. These steps might be as follows: (1) allocate sufficient securities to each Federal Reserve bank to cover expenses not taken care of by other earnings, (2) allocate to each

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Federal Reserve bank a sufficient amount of securities to cover dividend requirements, and (3) allocate the remaining securities among the Federal Reserve banks in proportion to their profit and loss ratio in the System Account. It would further minimize the size of periodic adjustments in participations if total expenses and dividends were combined into one ratio in years in which we would be justified in estimating earnings equal to or in excess of dividend requirements.

In presenting the various alternative suggestions given in this report we have assumed that any policies which you might adopt would be those which could be followed consistently through changing conditions and which would require simplicity of operation.

If the Federal Open Market Committee desires, we shall be prepared to make recommendations with respect to the points discussed above.

R.G.Rouse.

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Mr. Smead
Mr. [unclear]

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FEDERAL RESERVE BANK
OF NEW YORK

July 1, 1940.

ref

Dear Mr. Smead:

Receipt is acknowledged of your letter of June 28 enclosing statement showing changes in allocations in System Open Market Account as of July 1 on the basis of estimated expenses and earnings of each Federal Reserve bank during 1940.

The statement is in agreement with the one which we prepared on June 28 on the basis of figures received by telephone from Mr. Van Fossen and which, with your approval, was mailed to the Reserve banks on that day.

Yours faithfully,

Robert G. Rouse,
Manager, System Open
Market Account.

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

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FEDERAL RESERVE BANK
OF NEW YORK

June 28, 1940.

Dear Mr. Smead:

In accordance with the figures received over the telephone from Mr. Van Fossen this morning covering the quarterly reallocation of securities in the System Open Market Account, we have today sent to the Reserve banks a copy of the computation showing the adjustments to be made in participations in the System Open Market Account on July 1, 1940, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on November 30, 1937.

Enclosed herewith is copy of the letter of transmittal together with three copies of the computation, also copy of the telegram which was sent to each of the Federal Reserve banks today.

Yours faithfully,



Robert G. Rouse,
Manager, System Open
Market Account

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

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Directive #1

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FEDERAL RESERVE BANK OF NEW YORK
Similar letter sent to the President of each Federal Reserve bank except New York.

June 28, 1940.

Dear Mr. Young:

In accordance with my telegram of today, I enclose herewith computation of the readjustments to be made on July 1, 1940, of the participations of the Federal Reserve banks in the System Open Market portfolio.

Yours faithfully,

Robert G. Rouse,
Manager, System Open
Market Account

Honorable Roy A. Young, President,
Federal Reserve Bank of Boston,
Boston, Mass.

Encl.

RHR
JN

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MISC. 140A 18M 8-39

FEDERAL RESERVE BANK OF NEW YORK
 SECURITIES DEPARTMENT - MAH FMS

June 28, 1940

Please send following telegram to the President of each Federal Reserve bank as indicated below:

Under the plan for reallocation of Government securities adopted by the Federal Open Market Committee November 30, 1937, a readjustment of participations in Government securities held in the System Account is called for July 1, 1940. The computations showing adjustments to be made in participations of the several Federal Reserve banks is being sent to all Reserve banks today. These computations indicate an ^{increase} decrease of _____ in your participation on July 1. We shall wire you on July 1 the detailed entries to be made on that date.

		<u>Increase</u>	<u>Decrease</u>
Young	Boston	-	\$ 21,000
Sinclair	Philadelphia	-	1,075,000
Fleming	Cleveland	\$ 711,000	-
Leach	Richmond	-	2,599,000
Parker	Atlanta	-	13,782,000
Schaller	Chicago	-	8,350,000
Martin	St. Louis	769,000	-
Peyton	Minneapolis	-	1,829,000
Hamilton	Kansas City	2,400,000	-
Gilbert	Dallas	959,000	-
Day	San Francisco	4,939,000	-

ROUSE

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REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON JULY 1, 1940

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A - Expenses													
1. Estimated current expenses, 1940	28,569	2,111	7,283	2,285	2,869	1,679	1,221	3,261	1,529	973	1,697	1,231	2,430
F - Earnings													
1. Estimated current earnings, 1940 (exclusive of earnings on Govts.)	1,477	72	261	229	104	105	70	218	20	29	171	39	159
2. Estimated earnings on Govt. securities to June 30	21,372	1,543	6,451	1,730	2,183	1,087	884	2,321	969	638	993	818	1,755
3. Net profits on sales of Govt. securities to June 28	1,555	113	451	131	154	81	67	172	70	49	76	60	131
4. Total	24,404	1,728	7,163	2,090	2,441	1,273	1,021	2,711	1,059	716	1,240	917	2,045
C - Excess of "A-1" over "B-4"	4,165	383	120	195	428	406	200	550	470	257	457	314	385
D - Allocation required (on basis of 1.729016% earnings rate on Govts.) to produce earnings July-December equal to "C"	477,851	43,942	13,768	22,372	49,104	46,580	22,946	63,102	53,923	29,486	52,432	36,025	44,171
E - Estimated dividends	8,195	560	3,064	715	840	316	278	818	247	177	263	247	670
F - Allocation of remainder of System holdings (\$2,466,276,000 less \$477,851,000) on basis of "E"	1,988,425	135,878	743,445	173,487	203,817	76,674	67,453	198,478	59,932	42,947	63,814	59,932	162,568
G - Total allocation of Government securities ("D" plus "F")	2,466,276	179,820	757,213	195,859	252,921	123,254	90,399	261,580	113,855	72,433	116,246	95,957	206,739
H - Present Allocations	2,466,276	179,841	739,335	196,934	252,210	125,853	104,181	269,930	113,086	74,262	113,846	94,998	201,800
I - Change in Allocations	- -	-21	+17,878	-1,075	+711	-2,599	-13,782	-8,350	+769	-1,829	+2,400	+959	+4,939

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CONFIDENTIAL

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON JULY 1, 1940

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A - Expenses													
1. Estimated current expenses, 1940	28,569	2,111	7,283	2,285	2,869	1,679	1,221	3,261	1,529	973	1,697	1,231	2,430
Earnings													
1. Estimated current earnings, 1940 (exclusive of earnings on Govts.)	1,477	72	261	229	104	105	70	218	20	29	171	39	159
2. Estimated earnings on Govt. securities to June 30	21,372	1,543	6,451	1,730	2,183	1,087	884	2,321	969	638	993	818	1,755
3. Net profits on sales of Govt. securities to June 28	1,555	113	451	131	154	81	67	172	70	49	76	60	131
4. Total	24,404	1,728	7,163	2,090	2,441	1,273	1,021	2,711	1,059	716	1,240	917	2,045
C - Excess of "A-1" over "B-4"	4,165	383	120	195	428	406	200	550	470	257	457	314	385
D - Allocation required (on basis of 1.729016% earnings rate on Govts.) to produce earnings July-December equal to "C"	477,851	43,942	13,768	22,372	49,104	46,580	22,946	63,102	53,923	29,486	52,432	36,025	44,171
E - Estimated dividends	8,195	560	3,064	715	840	316	278	818	247	177	263	247	670
F - Allocation of remainder of System holdings (\$2,466,276,000 less \$477,851,000) on basis of "E"	1,988,425	135,878	743,445	173,487	203,817	76,674	67,453	198,478	59,932	42,947	63,814	59,932	162,568
G - Total allocation of Government securities ("D" plus "F")	2,466,276	179,820	757,213	195,859	252,921	123,254	90,399	261,580	113,855	72,433	116,246	95,957	206,739
H - Present Allocations	2,466,276	179,841	739,335	196,934	252,210	125,853	104,181	269,930	113,086	74,262	113,846	94,998	201,800
I - Change in Allocations	- -	-21	+17,878	-1,075	+711	-2,599	-13,782	-8,350	+769	-1,829	+2,400	+959	+4,939

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RECORDED IN FILES SECTION
JUN 28 1940

June 28, 1940.

Mr. R. G. Rouse, Manager,
System Open Market Account,
c/o Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Rouse:

There is enclosed a statement prepared from available information showing changes in allocations necessary in the System Open Market Account as of July 1 on the basis of our estimates of expenses and earnings of each Federal Reserve bank during 1940.

In estimating current earnings and current expenses, actual earnings (other than earnings on Government securities) and actual expenses for January through May of the current year have been used as a base, in accordance with the formula. Estimated current expenses arrived at on this basis have been adjusted for all of the banks by making allowance for the pro-ration in June and December of the net expense of the New York Bank in handling foreign accounts and transactions and by adding \$150,000 for St. Louis, as was done at the time of the last reallocation.

Very truly yours,

E. L. Smead, Chief,
Division of Bank Operations.

Handwritten initials: S, M, R, etc.

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For Mr. S. E. ...

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Explanation of basis for items indicated:

- A-1 2.4 times actual current expenses January to May adjusted by:
1. Adding \$150,000 at St. Louis as in previous reallocations this year, and
 2. Adding for 11 banks and deducting the total thereof from the New York figure, estimated portion of net expense of foreign department of New York Bank for year, using estimates for first six months obtained from New York by telephone June 26.
- B-1 2.4 times actual earnings, exclusive of earnings on Governments, January to May.
- B-2 and B-3 Obtained by telephone from Mr. Behrens at New York, June 28.
- D Actual rate used, .0087161 ($\frac{184}{305} \times 1.729016\%$).
- E Accrued dividends at May 31 plus 3.5 times paid-in capital on May 31, adjusted by addition of \$28,000 at San Francisco to cover increase of \$910,000 in paid-in capital at San Francisco during week ended June 19.

RE-ALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON JULY 1, 1940

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A. EXPENSES													
(1) Estimated current expenses, 1940	28,569	2,111	7,283	2,285	2,869	1,679	1,221	3,261	1,529	973	1,697	1,231	2,430
B. EARNINGS													
(1) Estimated current earnings, 1940 (exclusive of earnings on Governments)	1,477	72	261	229	104	105	70	218	20	29	171	39	159
(2) Estimated earnings on Govern- ments to June 30	21,372	1,543	6,451	1,730	2,183	1,087	884	2,321	969	638	993	818	1,755
(3) Net profits on Governments to June 28	1,555	113	451	131	154	81	67	172	70	49	76	60	131
(4) Total	24,404	1,728	7,163	2,090	2,441	1,273	1,021	2,711	1,099	716	1,210	917	2,045
C. Excess of A-1 over B-4	4,165	383	120	195	428	406	200	550	470	257	457	314	385
D. Allocation required (on basis of 1.729016% per annum earn- ing rate on Gov'ts) to provide earnings July-December equal to "C"	477,851	43,942	13,768	22,372	49,104	46,580	22,946	63,102	53,923	29,486	52,432	36,025	44,171
E. Estimated dividends, 1940	8,195	560	3,064	715	840	316	278	818	247	177	263	247	670
F. Allocation of remainder of System holdings (\$2,466,276,000 less \$477,851,000) on basis of "E"	1,988,425	135,878	743,445	173,487	203,817	76,674	67,453	198,478	59,932	42,947	63,814	59,932	162,568
G. Total allocation of Governments ("D" plus "F")	2,466,276	179,820	757,213	195,859	252,921	123,254	90,399	261,580	113,855	72,433	116,246	95,957	206,739
H. Present allocations	2,466,276	179,841	739,335	196,934	252,210	125,853	104,181	269,930	113,086	74,262	113,846	94,998	201,800
I. Change in allocations	--	-21	+17,878	-1,075	+711	-2,599	-13,782	-8,350	+769	-1,829	+2,400	+959	+4,939

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MAY 21 1940 R

333 ● 343

MEMORANDUM

To: Messrs. Van Fossen and Smead

May 20, 1940

From: Mr. Daniels

Subject: Estimates of Earnings
and Expenses in Reallocations of
System Open Market Account.

There are attached two tables comparing changes in participations in the System Open Market Account at the last three reallocations with changes which would have resulted (1) had "Furniture and equipment" and "Depreciation on bank building" been excluded from estimated expenses and (2) had earnings and expenses on industrial advances and commitments been excluded from estimated earnings and expenses.

Table I indicates, if proof were needed, that we should not exclude depreciation and furniture and equipment from expenses in making these estimates, but rather continue to make adjustments as they appear necessary in view of anticipated or recent abnormal charges to expense for depreciation and furniture and equipment.

Table II shows that the changes in allocations omitting industrial loan earnings and expenses would generally have been in the same direction. New York and Cleveland, especially, would have received smaller participations, due primarily to the fact that the part of the total account allocated in proportion to expense requirements would have been larger. Philadelphia would have gained considerably, and Atlanta and Minneapolis would have gained to a lesser extent, owing mainly to relatively large net earnings on industrial advances. These are the principal differences.

I believe we should in the future omit earnings and expenses of industrial loans and commitments in estimating earnings and expenses, especially since only Cleveland, Atlanta, and San Francisco now have any Federal Reserve bank funds involved in industrial loans. At Cleveland industrial loan earnings and expenses are running about equal to one another, and at San Francisco all current net earnings are being appropriated to cover estimated losses. This leaves Atlanta as the only bank for which it would be appropriate to include industrial loan earnings and expenses (about 12 per cent) in making the estimates of earnings and expenses in the reallocations.

Attachments 2

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MEMORANDUM

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M. B. Daniels

Attachments 2

I believe the arguments in favor of omitting sec. 13 b earnings + expenses are unanswerable.

WJ

TABLE I
CHANGES IN RECENT ALLOCATIONS OF SYSTEM OPEN MARKET ACCOUNT COMPARED
WITH CHANGES HAD DEPRECIATION AND FURNITURE AND EQUIPMENT BEEN EXCLUDED FROM ESTIMATED EXPENSES.

(In thousands of dollars)

Federal Reserve Bank	October 1, 1939		January 1, 1940		April 1, 1940	
	Under present formula	Excluding depreciation and furniture and equipment*	Under present formula	Excluding depreciation and furniture and equipment*	Under present formula	Excluding depreciation and furniture and equipment*
Boston	-2,111	+4,605	-2,726	-191	+3,428	+5,816
New York	+43,226	+113,341	-16,568	+623	-8,873	+20,192
Philadelphia	+2,009	-3,816	-8,914	-8,901	-5,255	-6,768
Cleveland	+10,405	-775	-5,842	-8,298	+674	-592
Richmond	-9,740	-17,705	-3,005	-4,752	+695	-1,789
Atlanta	-4,793	-14,079	+285	-3,825	+4,114	-1,701
Chicago	+4,670	+10,186	-5,430	-5,661	+4,006	+1,494
St. Louis	-30,050	-35,277	+27,079	+26,073	+2,328	+1,017
Minneapolis	-2,879	-5,018	+6,015	+4,931	+1,195	-1,333
Kansas City	-10,419	-44,289	+3,946	-3,298	-1,729	-11,967
Dallas	-4,446	-11,116	+4,527	+2,607	+967	-2,427
San Francisco	+4,128	+3,943	+633	+692	-1,550	-1,942

* But not excluding special adjustments on account of depreciation on fixed machinery and equipment.

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TABLE II

CHANGES IN RECENT ALLOCATIONS OF SYSTEM OPEN MARKET ACCOUNT COMPARED WITH CHANGES HAD EARNINGS AND EXPENSES ON INDUSTRIAL LOANS BEEN EXCLUDED FROM ESTIMATED EARNINGS AND EXPENSES, RESPECTIVELY.

(In thousands of dollars)

Federal Reserve Bank	October 1, 1939		January 1, 1940		April 1, 1940	
	Under present formula	Excluding industrial loan operations	Under present formula	Excluding industrial loan operations	Under present formula	Excluding industrial loan operations
Boston	-2,111	+214	-2,726	-2,876	+3,428	+3,032
New York	+43,226	+26,439	-16,568	-21,261	-8,873	-12,627
Philadelphia	+2,009	+18,165	-8,914	-4,603	-5,255	+961
Cleveland	+10,405	+1,475	-5,842	-7,486	+674	-2,099
Richmond	-9,740	-10,749	-3,005	-1,863	+695	+2,775
Atlanta	-4,793	+1,729	+285	+1,567	+4,114	+7,183
Chicago	+4,670	+1,107	-5,430	-6,280	+4,006	+1,943
St. Louis	-30,050	-34,183	+27,079	+26,095	+2,328	+688
Minneapolis	-2,879	+3,673	+6,015	+7,535	+1,195	+2,200
Kansas City	-10,419	-11,919	+3,946	+3,441	-1,729	-3,044
Dallas	-4,446	-3,224	+4,527	+4,685	+967	+863
San Francisco	+4,128	+6,973	+633	+1,046	-1,550	-1,875

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MAY 6 - 1940
333 ● 343

May 4, 1940

*System Open Market
Accounting Procedure*

Mr. R. G. Rouse, Vice President,
Federal Reserve Bank of New York,
New York, N. Y.

Dear Mr. Rouse:

As I told you over the telephone on Thursday, we have prepared a draft of the report that might be submitted to the Federal Open Market Committee on accounting connected with the System Open Market Account. This draft is, of course, in preliminary form and in any case would need considerable editing. You may have an entirely different way of approaching the problem than is followed in the attached draft, and, if so, I shall be very glad to have you rewrite the report accordingly. I am also enclosing a copy of a memorandum from Mr. Van Fossen with regard to the formula for reallocations of the System Account. This takes a somewhat different view than is embodied in the draft.

dated 4/30/40

The draft of the report, as enclosed, may be so worded as to enable one to infer the kind of recommendations I would be in favor of, but in any case I assume we will have to get together to agree upon what our recommendations will be if we are called upon by the Committee to make them.

Sincerely yours,

E. L. Smead, Chief,
Division of Bank Operations.

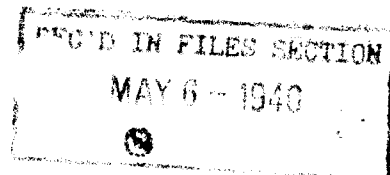
Enclosures 2

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J. B. Smith

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DRAFT OF MEMORANDUM TO FEDERAL OPEN MARKET COMMITTEE

May 4, 1940.

At the meeting of the Federal Open Market Committee in Washington on March 20, 1940, we were requested to study the present basis for the allocation of securities in the System Open Market Account and the accounting procedure followed in connection with the Account, to make a report at the next meeting of the Federal Open Market Committee which would include a statement of the various accounting procedures that might be adopted for the System Account, and to be prepared to make recommendations as to the procedure that should be followed.

As we see the problem, there are three main questions to be considered: (1) how should United States Government securities owned by the Federal Reserve banks be shown in the weekly press statement, (2) should profits on sales of securities be used to write down the book value of security holdings, and (3) should there be any change in the procedure under which participations in the System Account are now allocated among the Federal Reserve banks?

Amounts at which securities are shown in published condition statements.

With respect to the first question, it is the present practice to show Government securities in the statement at par and to include premium on securities purchased in "Other assets" and discount on securities purchased in "Other liabilities". The premium is currently amortized into earnings to the call date of the securities and the discount is accumulated into earnings to the maturity date of the securities.

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To: Federal Open Market Committee - 2 -

Two alternative methods have been suggested for showing the System's holdings of Government securities in the weekly Federal Reserve bank condition statement, as follows: (1) show securities at book value, i.e., at par plus premium and less discount, and (2) show the par value of the securities as at present and show the amount of premium less discount as a separate asset item in the statement.

With respect to the first suggestion, i.e., that securities be shown in the weekly statement at book value, the following comments are offered. It has been the practice since early in the history of the System to show securities in published statements at their par value, principally, we understand, in order to obviate any possibility of the public's gaining the impression that there has been a change in the System's holdings, when, as a matter of fact, no change has taken place. Should securities be shown at book value in published statements, reported holdings would fluctuate as a result of the following, as well as through purchases and sales: (1) amortization of premium, which would reduce book value, (2) accumulation of discount, which would increase book value, and (3) valuation reserves and charge-offs. If United States Government securities were shown among assets in press statements at book value, they would normally be shown likewise in the maturity classification, but if thought desirable they could continue to be shown in the maturity classification at par value.

With respect to the second suggestion, it would be a simple matter to show "Net premium on U. S. Securities" as an asset item, say, following "Total bills and securities".

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To: Federal Open Market Committee - 3 -

No accounting difficulties would be involved in showing United States Government securities in the weekly press statements in either of the above ways, and neither would involve any material changes in the accounting procedure now followed.

Profits on sales of United States Government securities.

Profits on sales of United States Government securities are now treated as an addition to current net earnings and are used to cover expenses or dividends or are transferred to surplus, or to reserves for contingencies through surplus, depending upon the situation at each Federal Reserve bank. In accordance with the plan approved by the Federal Open Market Committee on November 30, 1937, profits on sales of United States Government securities beginning January 1, 1938, have been distributed among the Federal Reserve banks in proportion to their average holdings in the System Account since June 30, 1936.

Instead of accounting for profits on sales of United States Government securities as at present they could (a) be used to write down the book value of the System account, (b) be set aside as a valuation reserve and deducted in the balance sheet from "Premium on securities", or (c) be transferred to reserves for contingencies.

With respect to (a) under our present practice when securities carried on the books at an amortized price of, say, 101 are sold at a profit of two points and other securities are bought at 103, profits on securities sold are increased and the net book value of the portfolio is increased by a like amount. The advisability of this so-called writing up the port-

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To: Federal Open Market Committee - 4 -

folio as a result of such sales and purchases may be questioned.

Should profits on sales of securities, either on so-called switches or on outright sales, be used to write down the book value of the System Account it would be necessary to distribute profits among the Federal Reserve banks on the basis of their current participations in the System Account. It would not be practicable to distribute them among the Federal Reserve banks on the basis of average participations in the System Account since June 30, 1936.

If profits on switches or outright sales of securities are used to write down the book value of the System Account they should, in our opinion, continue to be shown as profits on sales of securities in published statements of earnings and expenses of the Federal Reserve banks.

With respect to the second alternative, i.e., the use of profits on sales of securities to establish valuation reserves which would be deducted from the premium account, it may be pointed out that if this were done, and a substantial portion of our present contingent reserves were also allocated for that purpose, the time would presumably come in the course of the next few years when the valuation reserve would equal the amount of the premium account. In such case the amortization of premium would have to be discontinued unless a portion of the valuation reserve were either returned to profit and loss or used as a reserve to reduce the book value of the System Account below par value. The purpose sought to be accomplished by this method, i.e., reduction in the premium account, could be achieved equally as well and more simply by using profits to write off premium as

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To: Federal Open Market Committee - 5 -

outlined in alternative (a).

Had profits on sales of United States Government securities been used during recent years to write down the book value of the portfolio or to establish valuation reserves, there would have been deficits in net earnings of the Federal Reserve banks, after dividends, in 1935, 1936 and 1938.

The third alternative mentioned above, i.e., the transfer of profits on sales of securities to reserves for contingencies, would regularize a practice which has existed to a substantial extent for a number of years. Prior to 1937 transfers to reserves for contingencies were charged against the current year's earnings. Since that date they have been charged to surplus.

Reserves for contingencies now held by the Federal Reserve banks as a whole amount to \$34,627,014, as compared with \$41,596,606 of premium carried on the System Account as of April 22, 1940. Of the total contingent reserves, \$31,481,946 were set up out of current net earnings and \$3,115,068 out of surplus. The System could, of course, at any time it saw fit, use the \$31,481,946 of contingent reserves set aside out of earnings to write off an equal amount of the premium now carried on United States Government securities. If such were done, however, the rate of earnings on Government securities as shown in the earnings reports of the Federal Reserve banks would be much nearer the coupon rate than at present, as the premium amortization charge against earnings would be greatly reduced. Should it be decided to charge off all or a large part of the present premium account,

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To: Federal Open Market Committee - 6 -

the amount to be charged off by each Federal Reserve bank, in the absence of instructions to the contrary, would be based on its current participations in the System Account. If desired, however, the amount of the charge-off to be made by each Federal Reserve bank could be based on its average daily participation in the Account since June 30, 1936.

Quarterly allocations of securities among Federal Reserve banks.

The procedure now followed in allocating participations in the System Account among the Federal Reserve banks provides first for allocating a sufficient amount of securities to each Federal Reserve bank to cover its expenses not taken care of by other earnings, and second to allocate the remaining securities in the System Account among the Federal Reserve banks on the basis of their dividend requirements. The relationship between the expenses of individual Federal Reserve banks and total expenses of the System is quite different from the relationship between dividend payments by individual Federal Reserve banks and total dividend payments by the System. Since profits on sales of securities are now taken into earnings and thus reduce the amount of securities needed by the Federal Reserve banks to produce sufficient income to cover expenses, it is apparent that as profits increase the amount of securities allocated to the Federal Reserve banks to cover their expenses decreases, and the amount of securities allocated to the Federal Reserve banks on the basis of dividend requirements increases. When these profits are substantial there is a substantial fluctuation in participations in the System Account on quarterly reallocation dates. These fluctuations could be materially reduced if our formula for allocating securities

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To: Federal Open Market Committee - 7 -

among the Federal Reserve banks were expanded to embrace three steps instead of the present two. These steps might be as follows: (1) allocate sufficient securities to each Federal Reserve bank to cover expenses not taken care of by other income, (2) allocate to each Federal Reserve bank a sufficient amount of securities to cover dividend requirements, and (3) allocate the remaining securities among the Federal Reserve banks in proportion to their combined expense and dividend requirements.

If the Federal Open Market Committee desires, we shall be prepared to make recommendations with respect to each of the points discussed above.

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To: Federal Open Market Committee - 2 -

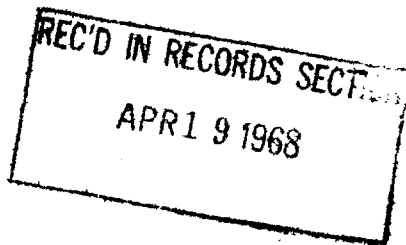
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With respect to the first suggestion, i.e., that securities be shown in the weekly statement at book value, the following comments are offered. It has been the practice since early in the history of the System to show securities in published statements at their par value, principally, we understand, in order to obviate any possibility of the public's gaining the impression that there has been a change in the System's holdings, when, as a matter of fact, no change has taken place. Should securities be shown at book value in published statements, reported holdings would fluctuate as a result of the following, as well as through purchases and sales: (1) amortization of premium, which would reduce book value, (2) accumulation of discount, which would increase book value, and (3) valuation reserves and charge-offs. If United States Government securities were shown among assets in press statements at book value, they would normally be shown likewise in the maturity classification, but if thought desirable they could continue to be shown in the maturity classification at par value.

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To: Federal Open Market Committee - 4 -

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Should profits on sales of securities, either on so-called switches or on outright sales, be used to write down the book value of the System Account it would be necessary to distribute profits among the Federal Reserve banks on the basis of their current participations in the System Account. It would not be practicable to distribute them among the Federal Reserve banks on the basis of average participations in the System Account since June 30, 1936.

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With respect to the second alternative, i.e., the use of profits on sales of securities to establish valuation reserves which would be deducted from the premium account, it may be pointed out that if this were done, and a substantial portion of our present contingent reserves were also allocated for that purpose, the time would presumably come in the course of the next few years when the valuation reserve would equal the amount of the premium account. In such case the amortization of premium would have to be discontinued unless a portion of the valuation reserve were either returned to profit and loss or used as a reserve to reduce the book value of the System Account below par value. The purpose sought to be accomplished by this method, i.e., reduction in the premium account, could be achieved equally as well and more simply by using profits to write off premium as

Handwritten notes:
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To: Federal Open Market Committee - 7 -

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If the Federal Open Market Committee desires, we shall be prepared to make recommendations with respect to each of the points discussed above.

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 - MAY 6 - 1940
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 April 30, 1940

Mr. Smead

Allocation of the *Carded*

Mr. Van Fossen

System Account
*x System Open Market Account
 formula for Allocation*

In connection with the memorandum which you and Mr. Rouse are to submit in regard to profits on sale of Government securities, the method of reporting security holdings in the weekly statement, and the method of allocating the System Account, I have the following suggestions:

In accordance with long established custom, the Federal Reserve banks will undoubtedly continue to pay the regular dividend even though not earned so long as they have sizable surplus accounts. Accordingly, it is suggested that in allocating the System Open Market Account, the first step be to allocate a sufficient amount of securities to cover estimated expenses and dividends after making allowance for earnings from other sources. Under the present formula any remaining securities would be allocated in proportion to capital or to its equivalent, dividends. In support of this procedure it may be pointed out that if earnings over a period of years averaged just about sufficient to cover expenses and dividends, this method of allocating the System Account would result in the accumulation by each Federal Reserve bank of excess earnings in proportion to their respective capital accounts and the drain on such accumulated earnings in years when earnings were insufficient to cover dividends would likewise be in proportion to capital. Accordingly, over the entire period the effect would be virtually the same as we would have if earnings in each year were just sufficient to cover earnings and dividends.

In further support of this method of allocating securities in excess of amounts needed to cover expenses and dividends is the fact that earnings of the Federal Reserve banks are applied first to cover expenses, losses, etc., and only such earnings as remain are available for dividends. Inasmuch as it is likely that the Federal Reserve banks will ordinarily have at least sufficient earnings to cover expenses, there does not appear to be any reason for allocating securities remaining after expenses and dividends have been provided for on the basis of combined expenses and dividends as has been suggested. In this connection it should also be borne in mind that one of the criticisms of our present formula is that a bank which reduces its expenses gets very little benefit therefrom and a bank which spends money freely gets an allocation sufficient to cover its expenses so that so far as the allocation of the System Account is concerned there is no inducement for a bank to keep down its expenses. To allocate securities remaining, after expenses and dividends have been

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 J. D. Smith

To: Mr. Smead

- 2 -

provided for, in proportion to expenses and dividends combined would in addition give a larger share of excess earnings to the bank that does not hold down its expenses.

While in normal circumstances the only drain upon surplus is likely to be to pay a portion of dividends in years when earnings are low, it is possible, of course, for the Federal Reserve banks to sustain heavy losses on investments which might necessitate a substantial charge to surplus or to reserves for contingencies. Accordingly, there is something to be said in favor of allocating securities remaining, after expenses and dividends have been provided for, in such a way as to equalize the position of the various Federal Reserve banks in respect to surplus and reserves for contingencies. I am in fact inclined to favor a formula which will accomplish this objective. If such a formula is to be adopted the first consideration would be to decide upon a basis of comparison. For this purpose, I would suggest total deposits of member banks in each Federal Reserve district on the theory that this represents as good a measure as we can find of the potential relative risk to each Federal Reserve bank of granting discount accommodation to its member banks. My suggestion would be that after allocating a sufficient amount of securities to cover expenses and dividends, the remaining securities be divided equally among the Federal Reserve banks that have a ratio of surplus (Section 7) plus other capital accounts to total deposits of its member banks less than the similar ratio for the System as a whole, with the provision that this special allocation shall not exceed \$50,000,000 for any bank. I would then allocate any securities still remaining in proportion to capital.

Following is a table showing the amount of surplus (Section 7) plus other capital accounts of each Federal Reserve bank, total member bank deposits, the ratio of the former to the latter, and the ratio of dividends of each bank to the System total and of expenses and dividends of each bank to the System:

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To: Mr. Smead

- 3 -

(In thousands)

Federal Reserve Bank	Surplus (Sec. 7) plus "other capital" accounts		Total member bank deposits	Ratio of Col. 1 to Col. 3 (percent)	Ratio of dividends to total	Ratio of expenses and dividends to total
	Amount	Multiples of one year's dividends				
Boston	12,231	21.8	2,767,556	.442	6.87	7.25
New York	63,946	20.9	18,011,692	.355	37.56	27.95
Philadelphia	16,494	23.1	3,256,029	.507	8.76	8.19
Cleveland	18,153	21.6	3,882,686	.468	10.29	10.05
Richmond	6,808	21.5	1,958,959	.348	3.87	5.45
Atlanta	7,474	26.9	1,749,278	.427	3.40	4.37
Chicago	29,866	36.6	6,977,445	.428	9.98	11.23
St. Louis	6,250	21.2	1,732,025	.361	3.02	4.76
Minneapolis	5,215	29.5	1,134,644	.460	2.17	3.20
Kansas City	4,909	18.7	1,858,726	.264	3.21	5.26
Dallas	5,864	23.8	1,582,112	.371	3.01	3.95
San Francisco	12,490	19.5	4,928,038	.253	7.86	8.34
Total	189,700	23.2	49,340,152	.384	100.00	100.00

It will be noted that surplus (Section 7) plus other capital accounts for the System as a whole is sufficient to cover dividends at the present rate for slightly over twenty-three years and that in the case of the Chicago, Minneapolis, Atlanta, and Dallas banks the ratio is higher than for the twelve banks combined. It will also be noted that for the System as a whole surplus (Section 7) plus other capital accounts is equal to .384 of one percent of total member bank deposits and that this percentage is higher than for the System at the Federal Reserve banks of Philadelphia, Cleveland, Minneapolis, Boston, Chicago, and Atlanta. Allocation of the System Account in accordance with the proposed plan would, of course, tend to reduce the percentage for these six banks and increase that of the other six.

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To: Mr. Sneed

- 4 -

Below is a comparison using January 1, 1940, figures of the distribution of the \$162,973,000 of securities remaining after expenses and dividends have been provided for:

(In thousands)

Federal Reserve Bank	Allocation of remainder of account		
	Under present formula, i.e., in proportion to dividends	In proportion to dividends and expenses	On basis of equalizing surplus and other capital accounts
Boston	32,057	33,349	11,284
New York	174,061	133,055	111,273
Philadelphia	41,396	37,194	14,571
Cleveland	47,259	47,211	16,636
Richmond	17,651	24,783	56,213
Atlanta	15,658	19,473	5,512
Chicago	16,008	50,782	16,195
St. Louis	13,893	22,311	54,891
Minneapolis	10,021	14,530	3,528
Kansas City	14,747	23,226	55,191
Dallas	13,894	18,479	54,891
San Francisco	36,328	38,580	62,788
Total	162,973	162,973	162,973

In column 1 is the distribution under the present formula, as actually made on January 1. In column 2 is the distribution that would have been made if these securities had been allocated in proportion to dividends and expenses, and in column 3 is the distribution that would have been made if the Federal Reserve banks of New York, Richmond, St. Louis, Kansas City, Dallas, and San Francisco had each been allocated \$50,000,000 and the remaining \$162,973,000 had then been allocated to the twelve banks in proportion to capital.

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To: Mr. Smead

- 5 -

The following observations appear to be in order:

Boston, Philadelphia, Cleveland, Atlanta, Chicago, and Minneapolis:

According to the above mentioned standard, the surplus plus the reserve for contingencies at each of these banks is too large and the proposed formula would substantially reduce its participation.

New York:

Surplus is too small. Proposed formula would tend to build it up but not as rapidly as present formula.

Richmond, St. Louis, Kansas City, Dallas, and San Francisco:

Surplus too small. Proposed formula would substantially increase participation.

Attention is called to the fact that if the plan of allocating excess securities in proportion to dividends and expenses were adopted, the effect on the allocation of the System Account would be in the wrong direction in the case of the ~~Richmond~~, Atlanta, Chicago, ~~St. Louis~~, and Minneapolis Banks and in all the other cases the change in the banks' participation, while in the right direction, would be much less substantial than it would be under the other proposal.

In order not to take away on one allocation what is granted in the preceding allocation, it is recommended that each quarterly allocation be made as if it were for a 12 month period, just as the January 1 allocation now is, or that the allocation be made but once a year hereafter. Instead of estimates based on figures for 5 months, I believe it would be preferable to use actual figures for the preceding 12 months both in the case of expenses and of earnings other than on Government securities.

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REC'D IN FILES SECTION
MAR 30 1940
333-343

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FEDERAL RESERVE BANK
OF NEW YORK

March 29, 1940

Ref

Dear Mr. Smead:

We received your letter of March 28 and have today sent to the Reserve banks a copy of the computation showing the adjustments to be made in participations in the System Open Market Account on April 1, 1940, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on November 30, 1937.

Enclosed herewith is copy of the letter of transmittal together with three copies of the computation, also copy of the telegram which was sent to each of the Federal Reserve banks today.

Yours faithfully,

Robert G. Rouse
Robert G. Rouse,
Manager, System Open
Market Account.

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

Encls. (5)

For Files
S. E. Helmer

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MISC. 140-B-15M-10 38

March 29, 1940

Dear Mr. Sinclair:

In accordance with my telegram of today, I enclose herewith computation of the readjustments to be made on April 1, 1940, of the participations of the Federal Reserve banks in the System Open Market portfolio.

Yours faithfully,

Robert G. Rouse,
Manager, System Open
Market Account.

Mr. John S. Sinclair, President,
Federal Reserve Bank of Philadelphia,
Philadelphia, Pa.

Encl.

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MISC 140A 15M 2-35

FEDERAL RESERVE BANK OF NEW YORK
SECURITIES DEPT. - MAH/JW

March 29, 1940

Please send following telegram to the President of each Federal Reserve bank as indicated below:

Under the plan for reallocation of Government securities adopted by the Federal Open Market Committee November 30, 1937, a readjustment of participations in Government securities held in the System Account is called for April 1, 1940. The computations showing adjustments to be made in participations of the several Federal Reserve banks is being sent to all Reserve banks today. These computations indicate an increase of _____ or a decrease of _____ in your participation on April 1. We shall wire you on April 1 the detailed entries to be made on that date.

		<u>Increase</u>	<u>Decrease</u>
Young	Boston	\$3,428,000	\$ -
Sinclair	Philadelphia	-	5,255,000
Fleming	Cleveland	674,000	-
Leach	Richmond	695,000	-
Parker	Atlanta	4,114,000	-
Schaller	Chicago	4,006,000	-
Martin	St. Louis	2,328,000	-
Peyton	Minneapolis	1,195,000	-
Hamilton	Kansas City	-	1,729,000
Gilbert	Dallas	967,000	-
Day	San Francisco	-	1,550,000

HOUSE

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON APRIL 1, 1940

(In thousands of dollars)

	System	Boston	New York	Philadelphia	Cleveland	Richmond	Atlanta	Chicago	St. Louis	Minneapolis	Kansas City	Dallas	San Francisco
A - Expenses													
1. Estimated current expenses, 1940	28,822	2,119	7,270	2,316	2,879	1,700	1,338	3,337	1,513	1,007	1,682	1,217	2,444
B - Earnings													
1. Estimated current earnings, 1940 (exclusive of earnings on Govts.)	1,590	79	305	241	108	112	73	217	21	55	187	36	156
2. Estimated earnings on Govt. securities to March 31	10,763	770	3,268	883	1,098	546	436	1,160	483	318	504	410	887
3. Net profits on sales of Govt. securities to March 28	571	42	165	48	57	30	24	63	26	18	28	22	48
4. Total	12,924	891	3,738	1,172	1,263	688	533	1,440	530	391	719	468	1,091
C - Excess of "A-1" over "B-4"	15,898	1,228	3,532	1,144	1,616	1,012	805	1,897	983	616	963	749	1,353
D - Allocation required (on basis of 1.73156% earnings rate on Govts.) to produce earnings April-December equal to "C"	1,218,611	94,128	270,731	87,690	123,869	77,572	61,705	145,408	75,349	47,218	73,816	57,412	103,710
E - Estimated dividends	8,166	561	3,067	715	840	316	278	815	247	177	262	246	642
F - Allocation of remainder of System holdings (\$2,475,270,000 less \$1,218,611,000) on basis of "E"	1,256,659	86,332	471,978	110,031	129,267	48,629	42,781	125,420	38,010	27,238	40,319	37,857	98,797
G - Total allocation of Government securities ("D" plus "F")	2,475,270	180,460	742,712	197,721	253,136	126,201	104,486	270,828	113,359	74,456	114,135	95,269	202,507
H - Present allocations	2,475,270	177,032	751,585	202,976	252,462	125,506	100,372	266,822	111,031	73,261	115,864	94,302	204,057
I - Change in allocations	--	+3,428	-8,873	-5,255	+674	+695	+4,114	+4,006	+2,328	+1,195	-1,729	+967	-1,550

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REC'D IN FILES SECTION
MAR 29 1940
333-343

March 28, 1940.

Mr. R. G. Rouse, Vice President,
Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Rouse:

There is enclosed a copy of the table showing changes necessary in holdings of United States Government securities of the various Federal Reserve banks on April 1, 1940, under the formula for reallocations of the System Open Market Account.

Current expenses and current earnings (exclusive of earnings on Government securities) were estimated by multiplying the amounts for October, 1939, through February, 1940, by 2.4, except that adjustments were made in the figures for New York and St. Louis as described below.

In computing the estimates of earnings and expenses for the New York Bank earnings and expenses of the Annex Building were excluded from the figures for the base period and to the result thus obtained budget amounts for earnings and expenses of the Annex Building for 1940 were added. The estimate of expenses for the St. Louis Bank obtained in accordance with the regular formula was increased by \$150,000, as was done at the time of the January 1 reallocation. I have discussed these adjustments over the telephone with Mr. Behrens.

Very truly yours,

J.R.V.

J. R. Van Fossen, Asst. Chief,
Division of Bank Operations.

Enclosure 1.

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For Files
S. E. Hagan

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MAR 29 1940

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON APRIL 1, 1940

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A - Expenses													
1. Estimated current expenses, 1940 ^{1/}	28,822	2,119	7,270	2,316	2,879	1,700	1,338	3,337	1,513	1,007	1,682	1,217	2,444
B - Earnings													
1. Estimated current earnings, 1940 (exclusive of earnings on Govts.) ^{1/}	1,590	79	305	241	108	112	73	217	21	55	187	36	156
2. Estimated earnings on Govt. securities to March 31	10,763	770	3,268	883	1,098	546	436	1,160	483	318	504	410	887
3. Net profits on sales of Govt. securities to March 28	571	42	165	48	57	30	24	63	26	18	28	22	48
4. Total	12,924	891	3,738	1,172	1,263	688	533	1,440	530	391	719	468	1,091
C - Excess of "A-1" over "B-4"	15,898	1,228	3,532	1,144	1,616	1,012	805	1,897	983	616	963	749	1,353
D - Allocation required (on basis of 1.73156% earnings rate on Govts.) to produce earnings April-December equal to "C"^{2/}	1,218,611	94,128	270,734	87,690	123,869	77,572	61,705	145,408	75,349	47,218	73,816	57,412	103,710
E - Estimated dividends^{3/}	8,166	561	3,067	715	810	316	278	815	247	177	262	246	612
F - Allocation of remainder of System holdings (\$2,475,270,000 less \$1,218,611,000) on basis of "E"	1,256,659	86,332	471,978	110,031	129,267	48,629	42,781	125,420	38,010	27,238	40,319	37,857	98,797
G - Total allocation of Government securities ("D" plus "F")	2,475,270	180,460	742,712	197,721	253,136	126,201	104,486	270,828	113,359	74,456	114,135	95,269	202,507
H - Present allocations	2,475,270	177,032	751,585	202,976	252,462	125,506	100,372	266,822	111,031	73,261	115,864	94,302	204,057
I - Change in allocations	—	+3,428	-8,873	-5,255	+674	+695	+4,114	+4,006	+2,328	+1,195	-1,729	+967	-1,550

^{1/} See letter to Mr. Rouse

^{2/} Actual rate used - .013046 (275/365 x 1.73156%)

^{3/} Dividends accrued, February 29, plus 5% of paid-in capital stock on March 20

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S. E. Hainer

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Mr. Smead

April 1 reallocation

Mr. Van Fossen

In connection with the forthcoming reallocation in the System Open Market Account, the question arises as to how we should arrive at the New York estimated earnings and expenses for 1940 in view of the fact that earnings and expenses in connection with the Annex Building will be reported as such currently instead of being included for the year as a whole in the December figures as was done in 1939.

New York's functional expense report shows that expenses in connection with the Annex Building during 1939 totaled \$93,726.92 and earnings \$62,118.19. These amounts, as indicated above, were included in the December earnings and expense statements. Following is a table showing various estimates of 1940 earnings and expenses as well as the actual figures for 1939 which, of course, include figures connected with the Annex Building. You will note that my suggestion is that the figures of both earnings and expenses obtained according to the usual formula be reduced by \$125,000. It may be that this slightly over estimates the amount of the expenses, but it is believed that it definitely over states the earnings and, accordingly, it is believed that the net result is satisfactory and incidentally pretty closely in line with the 1939 actual figures.

FEDERAL RESERVE BANK OF NEW YORK

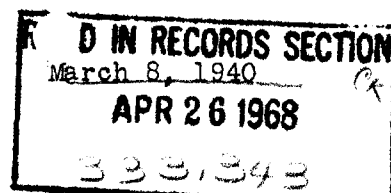
	<u>Expenses</u>	<u>Earnings other than on Govts.</u>
(In thousands of dollars)		
1939 - Actual	7,312	323
1940 - Jan. 1 estimate*	7,346	229
April 1 estimate**	7,441	425
Six times Jan. & Feb.	7,303	266
April 1 estimate adjusted	7,254	299
Proposed adjusted estimate	7,316	300

*Based on July to November according to formula
 **Based on October to February according to formula

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PROFITS ON SWITCHES IN SYSTEM ACCOUNT

A question has been raised as to whether the present accounting procedure used in the System Account may at times be a deterrent to the proper administration of the Account. The procedure in question is that by which profits on switches in the Account are added to current profits and the securities purchased taken up at cost. The alternative under consideration is to use the profits to write down the premium account on the System's books. 3/9/40

In carrying out the policies of the Federal Open Market Committee seeking to maintain orderly market conditions, it is frequently desirable to make shifts in the System Account by selling individual issues that are in considerable demand and buying issues in considerable supply, particularly if the shift would be advantageous to the Account. These shifts can properly be made at times when the market as a whole does not need outright purchases or sales by the System Account. At times like the present when the market is above book value, each shift (1) increases the book value of the System Account, although the par value remains unchanged, (2) reduces future income from the Account, and (3) increases current profits.

The suggestion has been made that the accounting practice should be reconsidered, because there is a possibility that it may militate against the execution of transactions that are desirable from the point of view of both the market and the Account. At times when the market is above book value there may be some hesitancy to undertake otherwise desirable transactions, because (1) to the extent that the book value is written up and immediate profits are taken the possibility of incurring losses in the future is increased and (2) to the extent that current income is reduced the possibility of failing to meet System expenses in the future is increased. At times when the market is below book value there may also be hesitancy to undertake otherwise desirable transactions, because of an unwillingness to take losses.

An alternate procedure would be to use the profit on the issue sold in a switch to write down the cost price of the issue purchased, either directly or after this profit has been carried through the profit and loss account. If this principle were applied when securities are sold at a loss, it would be necessary to add the loss to the cost of the issue purchased. From the accounting point of view a switch may be considered in either of two lights. The present accounting practice considers the purchase and the sale in a switch as two separate transactions. From another point of view a switch is somewhat in the nature of an exchange, because in most routine switches both sides of the transaction are completed simultaneously and the total par value of the System's investment in Government securities is not altered. From this point of view the difference between book value and selling price is not the same kind of a profit or loss that results from outright sales. The existing practice amounts in effect under present market conditions to a write-up of the System's portfolio whenever a switch is made in the Account and results in a decrease in the current rate of earnings on the Account.

Director #1

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- 2 -

It is recognized that the ultimate return to the System Account on its investment in Government securities will not be known unless and until the entire Account is liquidated. The ultimate return at that time would be the same, regardless of the accounting practices that are followed in the interim. The question for consideration is whether better current results are provided by the existing procedure or by the use of profits either on switches or on outright sales as well to write down the cost of the issues purchased. Incidentally, if profits on sales of securities were used to write down premiums, changes in the holdings of the several banks in the Account on quarterly reallocation dates would be substantially less than under the present procedure.

It may be noted in this connection that profits and losses are distributed among individual Reserve banks on the basis of average holdings in the Account since June 30, 1936. The premium account and current earnings, however, are distributed on the basis of the current participation. Should it be decided to use profits to write off premiums paid, the simplest procedure would be to make the entries on the basis of current holdings rather than to continue to distribute profits on the basis of average holdings since June 30, 1936. This is a question, however, that would need to have the consideration of the committee.

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON JANUARY 1, 1940

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A. Expenses (1) Estimated current expenses, 1940	28,772	2,079	7,346	2,335	2,891	1,689	1,265	3,286	1,486	998	1,711	1,210	2,476
B. Earnings (1) Estimated current earnings, 1940 (exclusive of earnings on Gov'ts)	1,502	92	229	216	111	104	51	211	24	63	194	41	164
C. Excess of A-1 over B-1	27,270	1,987	7,117	2,117	2,780	1,585	1,214	3,075	1,462	935	1,517	1,169	2,312
D. Allocation required (on basis of 1.751% earning rate on Gov'ts to produce earnings equal to "C")	1,557,040	113,452	406,360	120,875	158,730	90,499	69,316	175,574	83,476	53,386	86,616	66,747	132,009
E. Estimated dividends, 1940	8,131	563	3,057	727	830	310	275	608	244	176	259	244	638
F. Allocation of remainder of System holdings (\$2,481,270,000 less \$1,557,040,000) on basis of "E"	927,230	64,203	348,609	82,905	94,650	35,351	31,360	92,112	27,825	20,070	29,535	27,825	72,755
G. Total allocation of Gov'ts ("D" plus "F")	2,481,270	177,655	754,969	203,780	253,380	125,850	100,676	267,716	111,301	73,456	116,151	94,572	204,764
H. Present allocations	2,481,270	180,381	771,537	212,644	259,222	128,855	100,391	273,116	84,222	67,441	112,205	90,045	204,131
I. Change in allocations	--	-2,726	-16,568	-8,914	-5,842	-3,005	+285	-5,430	+27,079	+6,015	+3,946	+4,527	+633

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FEDERAL RESERVE BANK
OF NEW YORK

December 29, 1939

Dear Mr. Smead:

We received your letter of December 28 (and have today sent to the Reserve banks a copy of the computation showing the adjustments to be made in participations in the System Open Market Account on January 2, 1940, as of January 1, 1940, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on November 30, 1937.

Enclosed herewith is copy of the letter of transmittal together with three copies of the computation, also copy of the telegram which was sent to each of the Federal Reserve banks today.

Yours faithfully,

Robert G. Rouse
Robert G. Rouse,
Manager, System Open
Market Account.

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

Encls. (5)

Directive #1

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Similar letter sent to President of each Federal Reserve Bank except New York

December 29, 1939.

Dear Mr. Young:

In accordance with my telegram of today, I enclose herewith computation of the readjustments to be made on January 2, 1940, as of January 1, 1940, of the participations of the Federal Reserve banks in the System Open Market portfolio.

Yours faithfully,

Robert G. Rouse,
Manager, System Open
Market Account

Honorable Roy A. Young, President,
Federal Reserve Bank of Boston,
Boston, Mass.

RHR/JW

Encl.

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Securities Dept.
RHR/JW

December 29, 1939.

Please send following telegram to each President of the Federal Reserve Banks as indicated below:

Under the plan for reallocation of Government securities adopted by the Federal Open Market Committee November 30, 1937, a readjustment of participations in Government securities held in the System Account is called for January 1, 1940. The computations showing adjustments to be made in participations of the several Federal Reserve banks is being sent to all Reserve banks today. These computations indicate an increase of _____ in your participation decrease on January 1. We shall wire you on January 2 the detailed entries to be made on that date as of January 1.

ROUSE

		<u>Increase</u>	<u>Decrease</u>
Young	Boston	\$ -0-	\$ 2,726,000
Sinclair	Philadelphia	-0-	8,914,000
Fleming	Cleveland	-0-	5,842,000
Leach	Richmond	-0-	3,005,000
Parker	Atlanta	285,000	-0-
Schaller	Chicago	-0-	5,430,000
Martin	St. Louis	27,079,000	-0-
Peyton	Minneapolis	6,015,000	-0-
Hamilton	Kansas City	5,946,000	-0-
Gilbert	Dallas	4,527,000	-0-
Day	San Francisco	635,000	-0-

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON JANUARY 1, 1940

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A. Expenses													
(1) Estimated current expenses, 1940	28,772	2,079	7,346	2,335	2,891	1,689	1,265	3,286	1,486	998	1,711	1,210	2,476
B. Earnings													
(1) Estimated current earnings, 1940 (exclusive of earnings on Gov'ts)	1,502	92	229	216	111	104	51	211	24	63	194	41	164
C. Excess of A-1 over B-1	27,270	1,987	7,117	2,117	2,780	1,585	1,214	3,075	1,462	935	1,517	1,169	2,312
D. Allocation required (on basis of 1.7511% earning rate on Gov'ts) to produce earnings equal to "C"	1,557,040	113,452	406,360	120,875	158,730	90,499	69,316	175,574	83,476	53,386	86,616	66,747	132,009
E. Estimated dividends, 1940	8,131	563	3,057	727	830	310	275	108	244	176	259	244	638
F. Allocation of remainder of System holdings (\$2,481,270,000 less \$1,557,040,000) on basis of "E"	927,230	61,203	348,609	82,905	94,650	35,351	31,360	92,112	27,825	20,070	20,535	27,825	72,755
G. Total allocation of Gov'ts ("D" plus "F")	2,484,270	177,655	754,969	203,780	253,380	125,850	100,676	267,716	111,301	73,456	116,151	94,572	204,764
H. Present allocations	2,484,270	180,381	771,537	212,644	259,222	128,855	100,391	273,416	84,222	67,441	112,205	90,045	204,131
I. Change in allocations	--	-2,726	-16,568	-8,914	-5,842	-3,005	+285	-5,430	+27,079	+6,015	+3,946	+4,527	+633

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December 28, 1939.

Carded

Mr. R. G. Rouse, Vice President,
Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Rouse:

There is enclosed a copy of the table showing the changes necessary in holdings of United States Government securities, direct and guaranteed, by the various Federal Reserve banks on January 1, 1940, under the formula for re-allocations of the System Open Market Account.

Current expenses and current earnings (exclusive of earnings on Governments) have been estimated by multiplying the actual amounts thereof for July through November 1939 by 2.4. We have deducted from the estimate of current expenses for Chicago obtained on this basis \$44,000 in view of an adjustment in annual depreciation charges on the Chicago and Detroit buildings. We have added \$150,000 to the estimate of current expenses for St. Louis because of the prospective increase in depreciation of fixed machinery and equipment due to the installation of air conditioning at the head office and branches.

Very truly yours,

E. L. Smead, Chief,
Division of Bank Operations.

FILE COPY

FOR FILES
J. B. Smith

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON JANUARY 1, 1940

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Hugh- mond	Atlanta	Chicago	St. Louis	Min- neapolis	Kansas City	Dallas	San Francisco
A. Expenses													
(1) Estimated current expenses, 1940	28,772 ✓	2,079	7,346	2,335	2,891	1,689	1,265	3,286	1,486	998	1,711	1,210	2,476
B. Earnings													
(1) Estimated current earnings, 1940 (exclusive of earnings on Gov'ts)	1,502 ✓	92	229	218	111	104	51	211	24	63	194	41	164
C. Excess of A-1 over B-1	27,270 ✓	1,987	7,117	2,117	2,780	1,585	1,214	3,075	1,462	935	1,517	1,169	2,312
D. Allocation required (on basis of 1.7511% earning rate on Gov'ts) to produce earnings equal to "C"	1,557,040 ✓	113,452	406,360	120,875	198,730	90,499	69,316	173,574	83,476	53,386	86,616	66,747	132,009
E. Estimated dividends, 1940	8,131 ✓	563	3,057	727	830	310	275	808	244	176	299	244	638
F. Allocation of remainder of System holdings (\$2,481,270,000 less \$1,557,040,000) on basis of "E"	927,230 ✓	61,203	318,609	82,905	94,650	35,351	31,360	92,142	27,825	20,070	29,535	27,825	72,795
G. Total allocation of Gov'ts ("D" plus "F")	2,481,270 ✓	177,655	724,969	203,780	293,380	125,850	100,676	265,716	111,301	73,456	116,151	94,572	204,764
H. Present allocations	2,481,270 ✓	180,381	771,537	212,644	299,222	128,855	100,391	273,116	84,222	67,141	112,205	90,045	204,131
I. Change in allocations	—	-2,726	-16,568	-8,914	-5,842	-3,005	+285	-3,430	+27,079	+6,015	+3,946	+4,527	+633

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DEC 29 1939

EXPLANATION OF COMPUTATION OF ITEMS INDICATED
(Reallocation of Government Securities January 1, 1940)

- A-1 2.4 times current expenses, July-November, adjusted as follows:
1. \$44,000 deducted from Chicago in view of adjustment in depreciation charges on Chicago and Detroit buildings to 2 per cent of gross book value.
 2. \$150,000 added to St. Louis in view of prospective increase in depreciation on fixed machinery and equipment (installation of air conditioning).
- B-1 2.4 times current earnings, July-December.
- D Rate as of December 28, 1939, from Mr. Miller by telephone.
- E 6 per cent of paid-in capital on December 27, 1939.
- H As of December 28, 1939, from Mr. Miller by telephone.

DEC 29 1939
J. B. L. 224

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December 22, 1939

Mr. F. Guy Hitt,
First Vice President,
Federal Reserve Bank of St. Louis,
St. Louis, Missouri.

Dear Mr. Hitt:

Reference is made to your letter of December 18, 1939, in regard to the prospective increases in expenses of your Bank in 1940 incident to the installation of air conditioning equipment in the head office and branch buildings.

A number of the other Federal Reserve banks which have installed air conditioning equipment in recent years have set aside a special reserve at the end of the year in which the installation was completed equal to the entire cost of the installation and have charged such cost to profit and loss rather than current expenses. It would seem that whenever a Federal Reserve bank wishes to depreciate new equipment over a period of ten years the charge should be made to current expenses, but when it wishes to write off substantial amounts within the course of one or two years that it is preferable to make the charge to profit and loss, as otherwise current expenses are unduly inflated during such years. It is suggested, therefore, that if you wish to charge the cost of the air conditioning off within a two-year period that you make the charge direct to profit and loss. In order to allow for approximately half of this cost's being written off in 1940, we shall include \$150,000 for this purpose in our estimate of expenses of your Bank in the January 1, 1940, reallocation of securities in the System Open Market Account.

Very truly yours,

E. L. Smead, Chief,
Division of Bank Operations.

Supplies
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Mr. Paul Johnson

323 5-1939 (2)

FEDERAL RESERVE BANK
OF NEW YORK

*Reserves for losses on Industrial
Stocks*

December 15, 1959.

*Samuel P. Dawson & Co., Inc.
Wm. J. Palmer, Inc.*

Sirs:

The board of directors of this bank, at its regular meeting on December 14, 1959 at which a quorum was present, adopted the following resolution:

"VOTED to declare a dividend for the six months' period ending December 31, 1959, at the rate of six per centum per annum on the paid-in capital stock of the bank, payable on the 30th day of December, 1959, to stockholders as shown by the books of the bank at the close of business on that date."

There are enclosed two copies of a statement of estimated income and expenses for the year 1959 in comparison with actual income and expenses for the year 1958. This statement was presented to the directors in connection with their consideration of the above-mentioned dividend and the deductions from net earnings shown in such statement have been considered by the directors and officers and are deemed appropriate.

Among the adjustments upon the books of the bank reflected in the enclosed statement is the transfer to "Reserves for Contingencies" of the amount of the profit on sales of United States Government securities, shown in the statement as \$948,000. The directors authorized the transfer to this account of the total profit during the year 1959 on sales of Government securities so that the figure of \$948,000 may not be the final figure when the books are closed for this year. Before authorizing this transfer, the directors considered the possibility of applying the amount of the profit on sales of Government securities in reduction of the book value of this bank's participation in the System Open Market Account, but they felt that such an application of this amount would be less desirable because of the bookkeeping problems involved in connection with future reallocations of this bank's participation in the System Open Market Account and because it probably would be less revealing of the actual results of our participation in the Account than the course adopted.

We should appreciate receiving the Board's approval of the payment of the above-mentioned dividend and the making of the adjustments indicated in the statement. The final adjustments would be made, of course, on the basis of the actual year-end figures.

Respectfully,

Herbert H. Kimball

Herbert H. Kimball,
Secretary.

Board of Governors of the
Federal Reserve System,
Washington, D. C.

FOR FILES
J. B. Smith

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OCT 31 1939
October 24, 1939

Mr. Smead

Mr. Van Fossen

Formula for reallocation
of System account.

Following is a statement showing the changes in participations in the System account on April 1, July 1, and October 1, and for purposes of comparison the corresponding changes that would have occurred if (A) securities not needed to cover expenses and dividend requirements had been allocated in proportion to total expenses and dividends combined, and (B) if the reallocations on April 1, July 1, and October 1 had been made on the same basis as the January 1 allocation, i.e., if accrued earnings and expenses and profits during the current year had been disregarded and the allocation made to cover a twelve month period rather than the period to the end of the current calendar year.

1939 REALLOCATIONS OF SYSTEM ACCOUNT
CHANGES IN PARTICIPATIONS

Federal Reserve Bank	Actual			Revised on basis of distributing securities not needed to cover expenses and dividends in proportion to expenses and dividends combined			Revised on basis of a 12 month estimate, disregarding earnings, expenses, and profits to date		
	April 1	July 1	Oct. 1	April 1	July 1	Oct. 1	April 1	July 1	Oct. 1
Boston	+3	-3	-2	+3	-3	+3	+2	-1	-2
New York	-3	+36	+43	-3	+36	-69	-4	+9	+28
Philadelphia	+1	+11	+2	+1	+11	-4	+1	+5	+3
Cleveland	-5	+4	+10	-5	+4	+9	-4	+2	+6
Richmond	+1	+7	-10	+1	+7	+10	+1	+5	-8
Atlanta	-2	-9	-5	-2	-9	+7	-1	-3	-8
Chicago	+6	-10	+5	+6	-10	+17	+5	-4	+2
St. Louis	+4	-8	-30	+4	-8	-13	+4	-2	-11
Minneapolis	-3	-6	-3	-3	-6	+8	-2	-2	-3
Kansas City	-	-7	-10	-	-7	+16	-	-2	-6
Dallas	-4	-5	-4	-4	-5	+7	-3	-2	-4
San Francisco	-	-10	+4	-	-10	+11	-	-4	+3

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Mr. Smead

- 2 -

It will be noted that the reallocation on April 1 and July 1 would not have been affected by adoption of Plan A above mentioned, but that on the October 1 reallocation results would have been affected quite materially, and that in the case of six banks the change in participations would have been greater than at any quarter date as actually made. It will also be noted that under Plan B referred to above changes in participations would have been much less pronounced than under the existing formula or under Plan A. It is also reasonable to assume that changes on the forthcoming January 1 reallocation would be reduced if Plan B had been used for the October 1 reallocation.

You will recall that in my discussion of this matter with Messrs. Rouse and Miller at New York they expressed the opinion that the present formula is satisfactory, as evidenced by the fact that it has been in use for a considerable period of time and no criticisms have been received for at least a year from any of the Federal Reserve banks. Mr. Rouse also stated that he would dislike to make any change in the present formula until he has had further opportunity to study the matter.

Under the circumstances and particularly since results on the January 1 reallocation would not be likely to differ greatly under either of the proposed new formulae from those under the existing formula, it is suggested that no change be made in the formula until after the January 1 reallocation, and that steps be taken to obtain accurate information as to what the results would have been in 1939 under Plans A and B referred to above if they had been used during the current calendar year. I have not discussed this matter with Mr. Miller, but the Federal Reserve Bank of New York is in position to compile such figures and I do not believe that the undertaking would require an excessive amount of work.

The foregoing does not contemplate, of course, any change in the present objective of distributing the System account on the basis fundamentally of expense and dividend requirements in excess of earnings from other sources. It may be desired, however, to give consideration again to the possibility of distributing the System account in such a manner as to tend to equalize the position of the Federal Reserve banks as regards their capital accounts, either as a whole or exclusive of capital paid in and surplus (Section 13b). In this connection it is well to bear in mind that to accomplish this latter objective it is necessary to establish some standard for determining what the capital account of one bank should be as compared with another. I think the fact

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Mr. Smead

- 3 -

that the Federal Reserve Bank of Philadelphia has a paid in capital of \$12,116,000, Cleveland \$13,790,000, and Chicago \$13,803,000, is sufficient to show that capital paid in would not be a satisfactory basis. In my opinion the most equitable basis would be to relate capital account to total deposits of member banks in each Federal Reserve district, and a somewhat less satisfactory basis would be to relate capital account to required reserves of the banks in each Federal Reserve district. The first mentioned plan is based on the theory that total deposits of member banks is a pretty good measure of the relative importance of the various Federal Reserve districts and of the possible risk involved in granting discount accommodation. Of course expense and dividend requirements would be provided for before any distribution of the System account was made with a view to equalizing the capital account. What has been said above, I believe, is sufficient to demonstrate that the problem of deciding upon a satisfactory standard for comparing the capital set-up of the various Federal Reserve banks is a very difficult one and that it would be very optimistic to anticipate that the twelve Federal Reserve banks could be brought into agreement on this subject. A second problem already suggested by implication is as to whether we should be concerned in this connection with the total of paid in capital, surplus, and reserve for contingencies or only with Section 7 surplus and reserve for contingencies. This in itself would probably prove to be a difficult problem to solve inasmuch as it is likely that there would be considerable disagreement on the part of the Federal Reserve banks in the matter.

Assuming that agreement had been reached as regards these two subjects, there would remain the problem of deciding how securities not needed to cover expenses and dividends should be allocated with a view to equalizing the capital position. There are any number of ways, of course, in which this could be done and I should imagine that getting agreement on this point would not be the least of our troubles. My own suggestion would be that after providing for estimated expenses and dividends with some little margin for error any securities remaining should be divided equally among the Federal Reserve banks that were below the System average as regards capital, for example, if at this stage \$200,000,000 of securities remained and eight Federal Reserve banks had a ratio of capital, surplus and reserve for contingencies to total deposits of member banks less than the System ratio, each of these Federal Reserve banks would be given \$25,000,000 in the final allocation. An additional allocation of \$25,000,000 which would, of course, be subject to change at the end of three months would represent earnings of something like \$100,000 during a three months period. In the course of time, if the Federal Reserve System had substantial excess earnings, it is obvious that one by one the banks that were originally below the System average would be brought up to the System average, and in the meantime the System average would itself be rising so that ultimately all Federal Reserve banks would be brought up to the level of the highest.

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CONFIDENTIAL

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON OCTOBER 1, 1939

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A - Expenses													
1. Estimated current expenses, 1939	28,489	2,133	7,236	2,348	2,834	1,673	1,335	3,267	1,354	942	1,718	1,191	2,458
B - Earnings													
1. Estimated current earnings, 1939 (exclusive of earnings on Govts.)	1,502	110	258	175	115	78	56	208	25	65	197	46	169
2. Estimated earnings on Govts. to Sept. 30	26,041	1,920	7,172	2,137	2,601	1,387	1,158	2,858	1,220	778	1,317	1,033	2,160
3. Net profits on Govts. to Sept. 27	2,337	170	670	197	230	122	101	260	107	75	116	90	199
4. Total	29,880	2,200	8,100	2,509	2,946	1,587	1,315	3,326	1,352	918	1,630	1,169	2,528
C. Estimated dividends	8,110	564	3,054	725	822	305	272	823	239	175	256	241	634
D. Excess of A-1 plus "C" over B-4	6,719	197	1,890	564	710	391	292	764	241	199	344	263	564
E. Allocation required (on basis of 1.5490% earnings rate on Govts.) to produce earnings October-December equal to "D"	1,720,923	127,295	484,082	144,456	181,851	100,146	74,789	195,682	61,727	50,969	88,108	67,362	144,456
F. Allocation of remainder of System holdings (\$2,803,809,000 less \$1,720,923,000) on basis of "C"	1,082,886	75,308	1,07,785	96,805	109,757	10,725	36,319	109,891	31,912	23,367	34,182	32,180	84,655
G. Total allocation of Govts. ("E" plus "F")	2,803,809	202,603	891,867	241,261	291,608	110,871	111,108	305,573	93,639	74,336	122,290	99,542	229,111
H. Present allocations	2,803,809	204,714	848,441	239,252	281,203	150,611	115,901	300,903	123,689	77,215	132,709	103,988	224,983
I. Change in allocation	--	-2,111	+43,226	+2,009	+10,405	-9,740	-4,793	+4,670	-30,050	-2,879	-10,419	-4,446	+4,128

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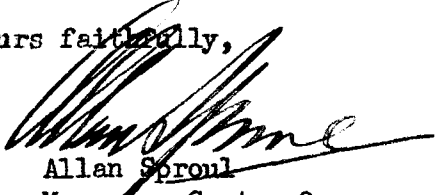
FEDERAL RESERVE BANK
OF NEW YORK

September 29, 1939.

Dear Mr. Smead:

We received your letter of September 28 and have today sent to the Reserve banks a copy of the computation showing the adjustments to be made in participations in the System Open Market Account on October 2, as of October 1, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on November 30, 1937.

Enclosed herewith is copy of the letter of transmittal together with three copies of the computation, also copy of the telegram which was sent to each of the Federal Reserve banks today.

Yours faithfully,

Allan Sproul
Manager, System Open
Market Account

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

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Directive #1

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MISC. 140A 15M 8-37

FEDERAL RESERVE BANK OF NEW YORK

SECURITIES DEPT.
RHB/JN

September 29, 1939.

Please send following telegram to each Federal Reserve bank as indicated below:

Under the plan for reallocation of Government securities adopted by the Federal Open Market Committee November 30, 1937, a readjustment of participations in Government securities held in the System Account is called for October 1. The computations showing adjustments to be made in participations of the several Federal Reserve banks is being sent to all Reserve banks today. These computations indicate an increase of _____ in your participation on October 1. We shall decrease _____ wire you on October 2 the detailed entries to be made on that date as of October 1.

SPROUL

		<u>INCREASE</u>	<u>DECREASE</u>
Young	Boston	\$ -	\$ 2,111,000
Sinclair	Philadelphia	2,009,000	-
Fleming	Cleveland	10,405,000	-
Leach	Richmond	-	9,740,000
Parker	Atlanta	-	4,793,000
Schaller	Chicago	4,670,000	-
Martin	St. Louis	-	30,050,000
Peyton	Minneapolis	-	2,879,000
Hamilton	Kansas City	-	10,419,000
Gilbert	Dallas	-	4,446,000
Day	San Francisco	4,128,000	-

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MISC. 140A 15M 8-37

FEDERAL RESERVE BANK OF NEW YORK

Similar letter sent to President of each Federal Reserve bank.

September 29, 1959.

Dear Mr. Young:

In accordance with my telegram of today, I enclose herewith computation of the readjustments to be made on October 2, as of October 1, of the participations of the Federal Reserve banks in the System Open Market portfolio.

Yours faithfully,

Allen Sproul
First Vice President

Honorable Roy A. Young, President,
Federal Reserve Bank of Boston,
Boston, Mass.

Encl.

RHB/JW

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON OCTOBER 1, 1939

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A - Expenses													
1. Estimated current expenses, 1939	28,489	2,133	7,236	2,348	2,834	1,673	1,335	3,267	1,354	942	1,718	1,191	2,458
B - Earnings													
1. Estimated current earnings, 1939 (exclusive of earnings on Govts.)	1,502	110	258	175	115	78	56	208	25	65	197	46	169
2. Estimated earnings on Govts. to Sept. 30	26,041	1,920	7,472	2,137	2,601	1,387	1,158	2,858	1,220	778	1,317	1,033	2,160
3. Net profits on Govts. to Sept. 27	2,337	170	670	197	230	122	101	260	107	75	116	90	199
4. Total	29,880	2,200	8,400	2,509	2,946	1,587	1,315	3,326	1,352	918	1,630	1,169	2,528
C. Estimated dividends	8,110	564	3,054	725	822	305	272	823	239	175	256	241	634
D. Excess of A-1 plus "C" over B-4	6,719	197	1,890	564	710	391	292	764	241	199	344	263	564
E. Allocation required (on basis of 1.5490% earnings rate on Govts.) to produce earnings October-December equal to "D"	1,720,923	127,295	484,082	144,456	181,851	100,146	74,789	195,682	61,727	50,969	88,108	67,362	144,456
F. Allocation of remainder of System holdings (\$2,803,809,000 less \$1,720,923,000) on basis of "C"	1,082,886	75,308	407,785	96,805	109,757	40,725	36,319	109,891	31,912	23,367	34,182	32,180	84,655
G. Total allocation of Govts. ("E" plus "F")	2,803,809	202,603	891,867	241,261	291,608	140,871	111,108	305,573	93,639	74,336	122,290	99,542	229,111
H. Present allocations	2,803,809	204,714	848,641	239,252	281,203	150,611	115,901	300,903	123,689	77,215	132,709	103,988	224,983
I. Change in allocation	--	-2,111	+43,226	+2,009	+10,405	-9,740	-4,793	+4,670	-30,050	-2,879	-10,419	-4,446	+4,128

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September 28, 1939.
J.N.

Mr. Allan Sproul,
First Vice President,
Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Sproul:

There is enclosed a copy of the table showing the changes necessary in holdings of United States Government securities by the various Federal Reserve banks on October 1, 1939, under the formula for reallocations of the System Open Market Account.

Current expenses have been estimated by multiplying the amounts for January through August by 1.5, and in the case of Atlanta adding \$70,000, as was done at the time of the July 1 reallocation. I have received a letter from St. Louis stating its installation of air-conditioning and ventilating equipment will not be completed this year, and accordingly we have made no adjustment of estimated expenses for St. Louis.

Estimated current earnings (exclusive of earnings on Governments) were computed by multiplying such earnings for January through August by 1.5. We have adjusted the estimate for Richmond obtained on this basis by deducting \$25,000 in view of the recent falling off in earnings on industrial advances.

Very truly yours,

✓
E. L. Smead, Chief,
Division of Bank Operations.

W M S
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For Files
S. E. Hainer

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**EXPLANATION OF COMPUTATION OF ITEMS INDICATED
 (Reallocation of Government Securities October 1, 1939)**

A-1 1.5 times current expenses January-August, adjusted as follows:

Atlanta—\$70,000 added to cover unusual chargeoffs and depreciation on account of air conditioning and general improvements of branch bank buildings to be completed this year.

B-1 1.5 times earnings (excluding earnings on Governments) January-August, adjusted as follows:

Richmond—\$25,000 deducted in view of recent falling off in earnings on industrial advances.

B-2)
 B-3)

Obtained or confirmed by telephone from New York, September 27.

C Dividends paid and accrued through August 31 plus 2% of paid-in capital stock on August 31.

E Actual rate used $\frac{39013}{100}$ ($\frac{92}{365} \times 1.5490\%$). Rate obtained from New York by telephone September 27.

For Files
 S. E. Hainer

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON OCTOBER 1, 1939

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A - Expenses													
1. Estimated current expenses, 1939	28,489	2,133	7,236	2,348	2,834	1,673	1,335	3,267	1,354	942	1,718	1,191	2,458
B - Earnings													
1. Estimated current earnings, 1939 (exclusive of earnings on Govts.)	1,502	110	258	175	115	78	56	208	25	65	197	46	169
2. Estimated earnings on Govts. to Sept. 30	26,041	1,920	7,472	2,137	2,601	1,387	1,158	2,858	1,220	778	1,317	1,033	2,160
3. Net profits on Govts. to Sept. 27	2,337	170	670	197	230	122	101	260	107	75	116	90	199
L. Total	29,880	2,200	8,400	2,509	2,946	1,587	1,315	3,326	1,352	918	1,630	1,169	2,528
C. Estimated dividends	8,110	544	3,054	725	822	305	272	823	239	175	256	241	634
D. Excess of A-1 plus "C" over B-4	6,719	197	1,890	544	710	391	292	764	211	199	344	263	564
E. Allocation required (on basis of 1.5490% earnings rate on Govts.) to produce earnings October-December equal to "D"	1,720,923	127,295	484,082	144,456	181,851	100,446	74,789	195,682	61,727	50,969	88,108	67,362	144,456
F. Allocation of remainder of System holdings (\$2,803,809,000 less \$1,720,923,000) on basis of "C"	1,082,886	75,308	407,785	96,805	109,757	40,725	36,319	109,891	31,912	23,367	34,182	32,180	84,655
G. Total allocation of Govts. ("E" plus "F")	2,803,809	202,603	891,867	241,261	291,608	141,171	111,108	305,573	93,639	74,336	122,290	99,542	229,111
H. Present allocations	2,803,809	201,714	848,641	239,252	281,203	150,611	115,901	300,903	123,689	77,215	132,709	103,988	224,983
I. Change in allocation	—	-2,111	+43,226	+2,009	+10,405	-9,740	-4,793	+4,670	-30,050	-2,879	-10,419	-4,446	+4,128

added

[Signature]

For Files
S. E. Hainer

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FOUND IN FILES SECTION
JUN 30 1939
333-343

Ref

June 29, 1939
SAH

Mr. Allan Sproul,
First Vice President,
Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Sproul:

Referring to my letter of June 26, there is enclosed a copy of the revised statement showing the changes under the formula in holdings of United States Government securities by the various Federal Reserve banks on July 1, 1939, based upon the amount of United States Government securities in the System Open Market account as of June 28.

Very truly yours,

✓

E. L. Smead, Chief,
Division of Bank Operations.

Enclosure - 1

SAH
VF:seh

FILE COPY

For Files
S. E. Hainer

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON JULY 1, 1939

(In thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Min- neapolis	Kansas City	Dallas	San Francisco
A - Expenses													
(1) Estimated current expenses, 1939	28,196	2,137	7,257	2,315	2,797	1,698	1,333	3,232	1,130	936	1,711	1,190	2,132
B - Earnings													
(1) Estimated current earnings, 1939 (exclusive of earnings on Governments)	1,537	117	251	171	116	108	58	209	25	67	194	48	170
(2) Estimated earnings on Govern- ments to June 30	16,909	1,251	4,770	1,361	1,686	883	774	1,873	805	522	871	688	1,125
(3) Net profits on Governments to June 30	1,675	122	480	111	165	87	72	186	77	54	83	65	113
(4) Total	20,121	1,490	5,501	1,673	1,967	1,078	904	2,268	907	643	1,118	801	1,738
C - Excess of A-1 over B-4	8,377	647	1,753	672	830	620	429	964	523	293	563	389	694
D - Allocation required (on basis of 1.33622% per annum earnings rate on Gov'ts) to provide earnings July-December equal to "C"	1,213,611	96,051	280,213	99,762	123,218	92,013	63,688	113,111	77,612	43,198	83,581	57,719	103,028
E - Estimated dividends, 1939	8,098	564	3,054	721	820	304	271	819	239	175	255	210	633
F - Allocation of remainder of System holdings (\$2,550,637,000, less \$1,213,611,000) on basis of "E"	1,307,023	91,030	162,918	116,854	132,318	19,066	43,710	132,187	38,575	28,215	41,157	38,736	102,167
G - Total allocations	2,550,637	187,081	753,161	216,616	255,566	111,109	107,128	275,298	116,217	71,713	121,738	96,485	205,195
H - Present allocations	2,550,637	190,390	716,898	205,712	252,011	133,725	115,974	285,779	123,780	77,557	131,720	101,890	215,171
I - Change in allocations	—	-3,309	+36,263	+10,904	+3,555	+7,384	-8,516	-10,181	-7,563	-5,811	-6,982	-5,105	-9,976

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*Mr Smead ✓
now read ✓*

REC'D IN RECORDS SECTION
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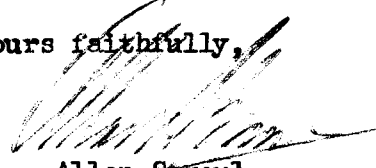
FEDERAL RESERVE BANK
OF NEW YORK

June 29, 1939.

Dear Mr. Smead:

We received your letter of June 26 and have today sent to the Reserve banks a copy of the computation showing the adjustments to be made in participations in the System Open Market Account on July 3, as of July 1, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on November 30, 1937.

Enclosed herewith is a copy of the letter of transmittal and three copies of the computation which was revised in accordance with telephone conversation.

Yours faithfully,

Allan Sproul
Manager, System Open
Market Account

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

Encls.

Directive #1

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SECURITIES DEPT.
RHB/JW

June 29, 1959.

Please send following telegram to each Federal Reserve Bank as indicated below:

Under the plan for reallocation of Government securities adopted by the Federal Open Market Committee November 30, 1957, a readjustment of participations in Government securities held in the System Account is called for July 1. The computations showing adjustments to be made in participations of the several Federal Reserve Banks is being sent to all Reserve Banks today. These computations indicate an increase of _____ in your participation on July 1. We shall decrease _____ wire you on July 3 the detailed entries to be made on that date as of July 1.

SPROUL

		<u>INCREASE</u>	<u>DECREASE</u>
Young	Boston	-0-	\$3,509,000
Sinclair	Philadelphia	\$10,904,000	-0-
Fleming	Cleveland	5,525,000	-0-
Leach	Richmond	7,384,000	-0-
Parker	Atlanta	-0-	8,548,000
Schaller	Chicago	-0-	10,481,000
Martin	St. Louis	-0-	7,563,000
Peyton	Minneapolis	-0-	5,814,000
Hamilton	Kansas City	-0-	6,982,000
Gilbert	Dallas	-0-	5,405,000
Day	San Francisco	-0-	9,976,000

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MISC. 140A 15M 8-37

FEDERAL RESERVE BANK OF NEW YORK

Similar letter sent to President of each Federal Reserve bank

June 28, 1959

Dear Mr. Young:

In accordance with my telegram of today, I enclose herewith computation of the readjustments to be made on July 3 as of July 1 of the participations of the Federal Reserve banks in the System Open Market portfolio.

Yours faithfully,

Allan Sproul
Manager, System Open
Market Account

Honorable Roy A. Young, President,
Federal Reserve Bank of Boston,
Boston, Mass.

Enc.

FD

CONFIDENTIAL

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON JULY 1, 1939

(In thousands of dollars)

	System	Boston	New York	Philadelphia	Cleveland	Richmond	Atlanta	Chicago	St. Louis	Minneapolis	Kansas City	Dallas	San Francisco
A - Expenses													
(1) Estimated current expenses, 1939	28,498	2,137	7,257	2,345	2,797	1,698	1,323	3,232	1,430	936	1,711	1,190	2,432
- Earnings													
(1) Estimated current earnings, 1939 (exclusive of earnings on Governments)	1,537	117	254	171	116	108	58	209	25	67	194	48	170
(2) Estimated earnings on Governments to June 30	16,909	1,251	4,770	1,361	1,686	883	774	1,873	805	522	871	688	1,425
(3) Net profits on Governments to June 24	<u>1,675</u>	<u>122</u>	<u>480</u>	<u>141</u>	<u>165</u>	<u>87</u>	<u>72</u>	<u>186</u>	<u>77</u>	<u>54</u>	<u>83</u>	<u>65</u>	<u>143</u>
(4) Total	20,121	1,490	5,504	1,673	1,967	1,078	904	2,268	907	643	1,148	801	1,738
C - Excess of A -1 over B -4	8,377	647	1,753	672	830	620	429	964	523	293	563	389	694
D - Allocation required (on basis of 1.33622% per annum earning rate on Gov'ts.) to provide earnings July - December equal to "C"	1,243,614	96,051	260,243	99,762	123,218	92,043	63,628	143,111	77,642	43,498	83,581	57,749	103,028
E - Estimated dividends, 1939	8,098	564	3,054	724	820	304	271	819	239	175	255	240	633
F - Allocation of remainder of System holdings (\$2,550,637 less \$1,243,614) on basis of "E"	1,307,023	91,030	492,918	116,854	132,348	49,066	43,740	132,187	38,575	28,245	41,157	38,736	102,167
G - Total allocation of Governments ("D" plus "F")	2,550,637	187,081	753,161	216,616	255,566	141,109	107,428	275,298	116,217	71,743	124,738	96,485	205,195
H - Present allocations	2,550,637	190,390	716,898	205,712	252,041	133,725	115,974	285,779	123,780	77,557	131,720	101,890	215,171
I - Change in allocations	+ 58,076	-3,309	+36,263	+10,904	+ 3,525	+ 7,384	- 8,546	- 10,481	- 7,563	-5,814	- 6,982	- 1,405	- 9,976

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June 26, 1939.
L.H.

Curran

Mr. Allan Sproul,
First Vice President,
Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Sproul:

There is enclosed a copy of the statement we have prepared showing the changes under the formula in holdings of United States Government securities by the various Reserve banks on July 1, 1939, the date of the next quarterly reallocation of securities in the System Open Market Account. I am also enclosing a copy of some notes explaining certain computations. You will note that we have adjusted the estimates of current expenses obtained in the usual way by adding \$70,000 at Atlanta, \$62,000 at St. Louis, and \$4,000 at Kansas City.

Very truly yours,

E. L. Smead, Chief,
Division of Bank Operations.

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Enclosures - 2

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MD:th S. E. Hainer 6/29/39

For Files
S. E. Hainer

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**EXPLANATION OF COMPUTATION OF ITEMS INDICATED
 (Reallocation of Government Securities July 1, 1939)**

- A-1** 2.4 times current expenses January-May (1939),
 adjusted as follows:
- Atlanta—\$70,000 added to cover unusual chargeoffs
 and depreciation on account of air conditioning and
 general improvement of branch bank buildings to be
 completed this year.
- St. Louis—\$62,000 added to cover estimated increase
 in depreciation expense on account of installing air
 conditioning and ventilating equipment at the head
 office and branches.
- Kansas City—\$4,000 added to cover estimated increase in
 depreciation expense on account of installing new
 elevators and a power plant at the head office.
- B-1** 2.4 times earnings (excluding earnings on Governments)
 January-May (1939)
- B-2)**
- B-3)** Obtained or confirmed by New York on telephone, June 26.
- D** Actual rate used, .670087% (184/365 X 1.32925%). Rate ob-
 tained from New York by phone, June 26.
- E** Actual dividends accrued to May 31, plus 3.5% of paid-in
 capital stock on May 31.

For Files
 S. E. Haines *[Signature]*

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON JULY 1, 1939

(In thousands of dollars)

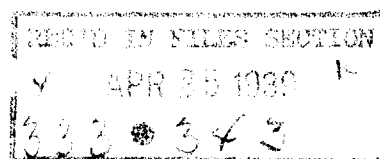
	System	Boston	New York	Phila- delphia	Cleve- land	Richmond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
- Expenses													
(1) Estimated current expenses, 1939	28,498	2,137	7,257	2,345	2,797	1,698	1,333	3,232	1,430	936	1,711	1,190	2,432
- Earnings													
(1) Estimated current earnings, 1939 (exclusive of earnings on Governments)	1,537	117	254	171	116	108	58	209	25	67	194	48	170
(2) Estimated earnings on Govern- ments to June 30	16,909	1,251	4,770	1,361	1,686	883	774	1,873	805	522	871	688	1,425
(3) Net profits on Governments to June 24	1,675	122	480	141	165	87	72	186	77	54	83	65	143
(4) Total	20,121	1,490	5,504	1,673	1,967	1,078	904	2,268	907	613	1,148	801	1,738
- Excess of A-1 over B-1	8,377	647	1,753	672	830	620	429	964	523	293	563	389	694
- Allocation required (on basis of 1.32925% per annum earnings rate on Gov'ts) to provide earnings July-December equal to "C"	1,250,136	96,555	261,608	100,285	123,864	92,525	64,021	143,862	78,050	43,726	84,019	58,052	103,569
- Estimated dividends, 1939	8,098	564	3,054	724	820	304	271	819	239	175	255	240	633
- Allocation of remainder of System holdings (\$2,564,015,000, less \$1,250,136,000) on basis of "E"	1,313,879	91,508	195,503	117,467	133,043	19,323	43,969	132,881	38,778	28,393	41,373	38,939	102,702
- Total allocation of Governments ("D" plus "E")	2,564,015	188,063	757,111	217,752	256,907	141,848	107,990	276,743	116,828	72,119	125,392	96,991	206,271
- Present allocations	2,564,015	191,322	721,957	206,907	253,398	134,227	116,422	287,127	124,174	77,844	132,140	102,282	216,215
- Change in allocations	--	-3,259	+35,154	+10,845	+3,509	+7,621	-8,432	-10,384	-7,346	-5,725	-6,748	-5,291	-9,944

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W *Mad* *added* *Supp.*
For Files
S. E. Hainer

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April 12, 1939.

Mr. Hugh Leach, President,
Federal Reserve Bank of Richmond,
Richmond, Virginia.

Dear Mr. Leach:

Reference is made to your letter of April 7 inquiring as to the method used in estimating current earnings of the Federal Reserve banks for 1939, exclusive of earnings on Governments, as used in the April 1 reallocation of the System holdings of United States Government obligations.

It is our practice to base the estimate of earnings, exclusive of earnings on Governments, on average earnings during the five months (eight months in the case of the October 1 reallocation) preceding the month in which the computation is made. Thus the estimate used in the January 1 reallocation was based on average earnings during the period July to November inclusive, and the estimate for the April 1 reallocation on the period October 1938 to February 1939, inclusive. Had interest received on past-due paper of closed banks been excluded from the figures as a non-recurring item, the estimate for your bank used in the April 1 reallocation would have been reduced by about \$50,000.

According to the above mentioned practice, for the July 1 reallocation the estimates will be based on average monthly earnings from January to May inclusive, and for the October 1 reallocation on average monthly earnings from January to August inclusive. Obviously the estimates for the July 1 and October 1 reallocations are likely to be more closely in line with actual figures for the year, and the reallocations on July 1 and October 1 will thus take into account any departure of actual earnings and expenses from the estimates used in the previous allocations for the year.

Very truly yours,

E. L. Smead, Chief,
Division of Bank Operations.

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FEDERAL RESERVE BANK
 OF RICHMOND

April 7, 1939

Mr. E. L. Smead, Chief,
 Division of Bank Operations,
 Board of Governors
 of the Federal Reserve System,
 Washington, D. C.

Dear Mr. Smead:

In the computation of readjustments as of April 1, 1939 of the participations of the Federal reserve banks in the System Open Market portfolio the estimated current earnings for 1939 (exclusive of earnings on Governments) were shown for this bank as \$170,000. We have endeavored to verify the estimate, but even on a rather liberal basis have been unable to estimate earnings of more than \$107,000. I am enclosing a statement showing the earnings of this bank (exclusive of earnings on Governments) for the first quarter of 1938, the year 1938, the first quarter of 1939, and an estimate for the year 1939.

You will note that our earnings for 1938 were only \$153,280, which included larger earnings on industrial advances and commitments than can be expected for the year 1939 and a non-recurring item "Interest received on past due paper of closed banks" of \$22,135. You will also note that the earnings of this bank for 1938 were \$17,000 less than the estimate which was used as a basis for the reallocation of Government securities as of April 1, 1939.

It is my understanding that the computation referred to is prepared in your office, and if you will let me know how you arrived at the estimated figure of \$170,000 it will be very much appreciated.

Very truly yours,

Hugh Leach
 Hugh Leach,
 President.

Enclosure

See ams 4/12/39

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EARNINGS FROM SOURCES OTHER THAN GOVERNMENT SECURITIES

(Cents omitted)

<u>From</u>	1938		1939	
	Jan.,Feb.,Mch.	Year	Jan.,Feb.,Mch.	Estimated for Year
Discounted bills	\$ 2,237	\$ 9,042	\$ 714	\$ 2,840
Purchased bills	27	112	28	112
Industrial Advances	25,243	82,454	17,920	70,000
Commitments to make industrial advances	3,349	15,074	2,383	10,000
All other (Except Gov'ts.):				
Income from banking house	5,267	20,903	5,234	20,940
Interest received on past- due paper of closed bks.	480	22,135	-	- (a)
Miscellaneous items	1,007	3,560	716	3,560
Totals	\$37,610	\$153,280	\$26,995	\$107,452 (b)

- (a) The receiverships of all suspended banks have been closed, therefore we will not have any earnings to report against the item, "Interest received on past-due paper of closed banks," for 1939.
- (b) The estimated amount of these earnings on which the Committee based its re-allocation of securities on April 1st is \$170,000 - on January 1st was \$186,000.

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RECORDED IN FILES SECTION
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March 30, 1939.

Mr. Allan Sproul, Manager,
System Open Market Account,
Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Sproul:

Thank you for your letter of March 22, advising that Mr. Miller will be glad to come to Washington at some mutually convenient time to discuss possible improvements in the formula now used in allocating securities in the System Open Market Account. We are still experimenting with various suggestions that have been made, and if and when we are able to work out revisions in the formula that we feel would be helpful in reducing the size of quarterly changes in allocations, we shall be glad to get in touch with him.

Sincerely yours,

E. L. Smead, Chief,
Division of Bank Operations.

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FOR FILES
E. L. Smead

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FILED IN FILES SECTION
APR 12 1939
333-343

March 30, 1939

Mr. O. M. Attebery, Vice President,
Federal Reserve Bank of St. Louis,
St. Louis, Missouri

Dear Mr. Attebery:

Referring to your letter of March 20,
enclosing a copy of Mr. Martin's March 13 letter to
Mr. Sproul, in estimating expenses of the Federal
Reserve banks in connection with the April 1 realloca-
tion of the System Open Market Account, an allowance
of \$70,000 was made in the estimate for your bank to
cover the anticipated increase in depreciation on
fixed machinery and equipment.

Very truly yours,

E. L. Smead, Chief,
Division of Bank Operations.

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APR 12 1939

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FEDERAL RESERVE BANK
OF NEW YORK

March 27, 1939.

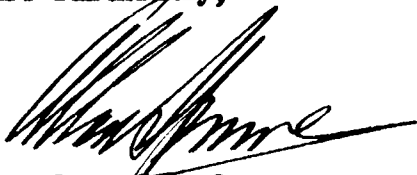
Dear Mr. Smead:

3/24/39

We received your letter on March 25 and have today sent to the Reserve banks a copy of the computation showing the adjustments to be made in participations in the System Open Market Account as of April 1, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on November 30, 1937.

A copy of the letter of transmittal and two copies of the computation are enclosed herewith.

Yours faithfully,



Allan Sproul,
Manager, System Open
Market Account.

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

Encs.

Director

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J.B-15M-10-38

Similar letter sent to President of each Federal Reserve bank.

March 27, 1939.

Dear Mr. Young:

In accordance with my telegram of today, I enclose herewith computation of the readjustments to be made on April 1 of the participations of the Federal Reserve banks in the System Open Market portfolio.

Yours faithfully,

Allan Sproul
Manager, System Open
Market Account

Honorable Roy A. Young, President,
Federal Reserve Bank of Boston,
Boston, Mass.

Encl.

SAM:JN

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FEDERAL RESERVE BANK OF NEW YORK

SECURITIES DEPT.
RHB/JN

March 27, 1939.

Please send following telegram to each Federal Reserve Bank as indicated below:

Under the plan for reallocation of government securities adopted by the Federal Open Market Committee November 30, 1937, a readjustment of participations in government securities held in the System Account is called for April 1. The computations showing adjustments to be made in participations of the several Federal Reserve Banks is being sent to all Reserve Banks today. These computations indicate an ^{increase} ~~decrease~~ of _____ in your participation on April 1. We shall advise you on April 1 the detailed entries to be made on that date.

SPROUL

		<u>INCREASE</u>	<u>DECREASE</u>
Young	Boston	\$ 3,516,000	\$ -0-
Sinclair	Philadelphia	1,048,000	-0-
Fleming	Cleveland	-0-	4,526,000
Leach	Richmond	703,000	-0-
Parker	Atlanta	-0-	1,981,000
Schaller	Chicago	6,527,000	-0-
Martin	St. Louis	4,351,000	-0-
Peyton	Minneapolis	-0-	2,610,000
Hamilton	Kansas City	42,000	-0-
McKinney	Dallas	-0-	4,136,000
Day	San Francisco	172,000	-0-

REALLOCATION OF GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON APRIL 1, 1939
(Amounts in thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	At- lanta	Chicago	St. Louis	Minne- apolis	Kansas City	Dallas	San Francisco
- Expenses													
(1) Estimated current expenses, 1939	29,003	2,171	7,318	2,342	2,820	1,703	1,382	3,317	1,469	977	1,741	1,230	2,533
- Earnings													
(1) Estimated current earnings, 1939 (exclusive of earnings on Governments)	1,748	113	337	208	131	170	52	204	25	76	190	53	189
(2) Estimated earnings on Govern- ments to March 31	8,363	613	2,364	671	841	436	386	916	391	262	431	347	705
(3) Net profits on Governments to March 22	307	22	89	26	30	16	13	34	14	10	15	12	26
(4) Total	10,418	748	2,790	905	1,002	622	451	1,154	430	348	636	412	920
- Excess of A-1 over B-4	18,585	1,423	4,528	1,437	1,813	1,081	931	2,163	1,039	629	1,105	818	1,613
- Allocation required on basis of 1.3399% per annum earnings rate on Governments) to provide earnings April-December equal to "C"	1,840,987	140,959	448,533	142,346	180,087	107,081	92,223	214,262	102,921	62,307	109,459	81,029	159,780
- Estimated dividends, 1939	8,097	564	3,062	723	821	304	271	816	238	174	254	238	632
- Allocation of remainder of System holdings (\$2,564,015,000, less \$1,840,987,000) on basis of "F"	723,028	50,363	273,424	64,561	73,311	27,146	24,199	72,865	21,253	15,537	22,681	21,253	56,435
- Total allocation of Governments ("D" plus "F")	2,564,015	191,322	721,957	206,907	253,398	134,227	116,422	287,127	124,174	77,844	132,140	102,282	216,215
- Present allocations	2,564,015	188,006	724,463	205,859	257,924	133,524	118,403	280,800	119,823	80,454	132,098	106,418	216,043
- Change in allocations	--	+3,316	-2,706	+1,048	-4,526	+703	-1,981	+6,327	+4,351	-2,610	+42	-4,136	+172

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IN THE FEDERAL RESERVE SYSTEM
MAR 24 1934
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Mar. 24, 1934

Mr. Allan Sproul,
First Vice President,
Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Sproul:

There is enclosed the statement of changes in allocations of the System Open Market Account necessary on April 1 on the basis of the estimates of earnings, expenses, and dividends shown.

In estimating current expenses and current earnings, exclusive of earnings on Governments, amounts for the five months ending February 28 have been multiplied by 2-4/10 as a basis. These estimates of current expenses have been adjusted by adding \$70,000 at St. Louis and \$90,000 at Kansas City and deducting \$180,000 at Atlanta and \$70,000 at Chicago. The additional amounts at St. Louis and Kansas City are in view of expected increases in depreciation on fixed machinery and equipment for the year. The adjustments at Atlanta and Chicago were made in view of unusually large amounts reported for furniture and equipment in November and December.

Very truly yours,

by MTD
K
Enclosure

FILE

COPY
E. L. Sneed, Chief,
Division of Bank Operations.

FOR FILES
J. B. Smith

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Explanation of Computation of Items Indicated
 Reallocation of System Open Market Account
 April 1, 1939

A-1 2.4 times current expenses October-February, adjusted as follows:

Atlanta--\$180,000 deducted on account of unusual charges for "Furniture and equipment" and "Repairs and alterations" in November and December 1938.

Chicago--\$70,000 deducted on account of unusual charges for "Furniture and equipment" and "Depreciation" in December 1938.

St. Louis--\$70,000 added to cover estimated increase in "Depreciation" (see correspondence with Mr. Martin).

Kansas City--\$90,000 added to cover estimated increase in "Depreciation" due to installation of new elevators and power plant.

B-2 Actual earnings to March 22.

Estimates obtained from New York by phone, March 22.

B-3 Obtained from New York by phone, March 22.

D- Actual rate used 1.009513% ($275/365 \times 1.3399\%$)

E- Dividends accrued on February 28 plus 5% of paid-in capital stock at February 28.

FEDERAL RESERVE BANK
 ST. LOUIS

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FEDERAL RESERVE BANK
OF NEW YORK

March 22, 1939.

Mr. E. L. Smead,
Chief, Division of Bank Operations,
Board of Governors of the Federal
Reserve System,
Washington, D. C.

Dear Mr. Smead:

Handwritten initials

Referring to your letter of September 28, 1938, and to our subsequent conversations, Mr. S. A. Miller, Manager, Securities Department, has been studying the quarterly adjustments of participations of the Federal reserve banks in the System Open Market Account. He is not very optimistic about reducing the size of these adjustments so long as the present principle governing participations in the Account is maintained, but he is ready to talk to you about the whole matter. If and when you want to have a conference, I am sure that he can arrange to go to Washington at some mutually convenient time.

Personally, I do not think the question is one of prime importance and I assume that you feel the same way about it, but, of course, if a better system than the one we now have can be devised, we should want to adopt it.

Yours faithfully,

Allan Sproul,
Manager, System Open
Market Account.

See memo 3/30/39

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FEDERAL RESERVE BANK
OF
ST. LOUIS

March 20, 1939.

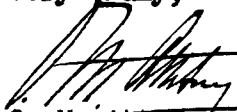
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Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

Dear Mr. Smead:

For your information, I enclose copy
of letter Mr. Martin addressed to Mr. Sproul,
Manager, System Open Market Account, under date
of March 13, 1939.

Yours very truly,


O. M. Attebery,
Vice President.

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J. B. Smith

See ans 3/30/39

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C O P Y.

March 13, 1939.

Mr. Allan Sproul, Manager,
System Open Market Account,
Federal Reserve Bank of New York,
New York, N. Y.

Dear Mr. Sproul:

The Board of Governors of the Federal Reserve System has approved the recommendation of our Board of Directors that we be authorized to spend not more than \$175,000.00 for air conditioning the four buildings occupied by this bank and its branches. We have employed an engineer who is working on the plans and specifications and the installations, we understand, will be completed about July 1.

In keeping with the accounting instructions from the Board of Governors of the Federal Reserve System, the expenditure will be capitalized and depreciated monthly, which will result in added operating expense for the latter part of the year of approximately \$75,000.00.

We are bringing this information to your attention in advance of the reallocation of securities which will take place on April 1.

Very truly yours,

(Signed) WM. McC. MARTIN

President.

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**FEDERAL RESERVE BANK
OF NEW YORK**

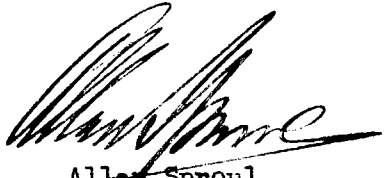
March 17, 1939.

Dear Mr. Smead:

In a letter dated March 13, Mr. Wm. McC. Martin advised me, in advance of the quarterly reallocation of securities in the System Open Market Account, on April 1, of an additional expense of approximately \$75,000 to be incurred by the Federal Reserve Bank of St. Louis during the latter part of the year, in connection with an expenditure of not more than \$175,000 for air conditioning the buildings occupied by the bank and its branches.

In case you have not been fully informed in this regard, I am enclosing a copy of the above-mentioned letter, together with a copy of my reply, dated March 16.

Yours faithfully,



Allen Sproul,
Manager, System Open
Market Account.

Mr. E. L. Smead,
Chief, Division of Bank Operations,
Board of Governors of the Federal
Reserve System,
Washington, D.C.

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I. B. Smith

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COPY

FEDERAL RESERVE BANK
OF ST. LOUIS

March 13, 1939.

Mr. Allen Sproul, Manager,
System Open Market Account,
Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Sproul:

The Board of Governors of the Federal Reserve System has approved the recommendation of our Board of Directors that we be authorized to spend not more than \$175,000 for air conditioning the four buildings occupied by this bank and its branches. We have employed an engineer who is working on the plans and specifications and the installations, we understand, will be completed about July 1.

In keeping with the accounting instructions from the Board of Governors of the Federal Reserve System, the expenditure will be capitalized and depreciated monthly, which will result in added operating expense for the latter part of the year of approximately \$75,000.00.

We are bringing this information to your attention in advance of the reallocation of securities which will take place on April 1.

Very truly yours,

(Signed) Wm. McC. Martin,

President

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FEDERAL RESERVE BANK OF NEW YORK

March 16, 1939.

Mr. Wm. McC. Martin,
President, Federal Reserve
Bank of St. Louis,
St. Louis, Mo.

Dear Mr. Martin:

This will acknowledge receipt of your letter of March 13, advising me, in advance of the quarterly reallocation of securities in the System Open Market Account, on April 1, of an additional expense of approximately \$75,000 to be incurred by your bank during the latter part of the year, in connection with an expenditure of not more than \$175,000 for air conditioning the buildings occupied by your bank and branches.

Under the present procedure for quarterly reallocation of participations in the System Open Market Account, the figures covering estimated and actual earnings, expenses, dividends, and charges or additions to net earnings of the Reserve banks, are assembled for the Committee by the office of the Board of Governors of the Federal Reserve System. Owing to the fact that you have received instructions from the Board with respect to the accounting procedure covering the expenditure, I assume that the matter should automatically be taken into consideration at the time the next reallocation of participations is effected.

However, in order to be certain that Mr. Saeed, at Washington, is fully informed concerning the proposed special expenditure of your bank, we have called the matter to his attention.

Yours faithfully,

Allan Sproul,
Manager, System Open
Market Account.

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FOR FILE
J. B. Saeed

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FEDERAL RESERVE BANK
OF NEW YORK

December 29, 1938.

Dear Mr. Smead:

We have your letter of December 27 and have today sent to the Reserve banks a copy of the computation showing the adjustments to be made in participations in the System Open Market Account as of January 1, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on November 30, 1937.

A copy of the letter of transmittal and two copies of the computation are enclosed herewith.

Yours faithfully,



Allan Sproul
Manager, System Open
Market Account

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

Encl.

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Copy of similar letter sent to President of each Federal Reserve bank.

December 29, 1938.

Dear Mr. Young:

In accordance with my telegram of today, I enclose herewith computation of the readjustments to be made on January 3 as of January 1 of the participations of the Federal Reserve banks in the System Open Market portfolio.

Yours faithfully,

Allan Sproul
Manager, System Open
Market Account

Honorable Roy A. Young, President,
Federal Reserve Bank of Boston,
Boston, Mass.

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REALLOCATION OF U. S. SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON JANUARY 1, 1939
(Earnings on securities estimated at 1.313 per cent per annum)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A - Expenses													
(1) Estimated current expenses, 1939	28,803	2,124	7,342	2,305	2,857	1,692	1,375	3,216	1,406	995	1,720	1,263	2,508
B.- Earnings													
(1) Estimated current earnings, 1939 (exclusive of earnings on Gov'ts)	1,784	121	350	206	137	186	42	194	28	82	194	61	183
C - Excess of A-1 over B-1	27,019	2,003	6,992	2,099	2,720	1,506	1,333	3,022	1,378	913	1,526	1,202	2,325
D - Allocation required (on basis of 1.313% earnings rate on Gov'ts) to produce earnings equal to "C"	2,057,807	152,552	532,521	159,863	207,159	114,699	101,523	230,160	104,951	69,536	116,222	91,546	177,075
E - Estimated dividends 1939	8,067	565	3,062	733	809	300	269	807	237	174	253	237	621
- Allocation of remainder of System holdings (\$2,564,015,000 less \$2,057,807,000) on basis of "E"	506,208	35,454	192,142	45,996	50,765	18,825	16,880	50,640	14,872	10,918	15,876	14,872	38,968
G.-Total allocation of Gov'ts ("D" plus "E")	2,564,015	188,006	724,663	205,859	257,924	133,524	118,403	280,800	119,823	80,454	132,098	106,418	216,043
H.-Present allocations	2,564,015	192,971	815,422	222,761	257,820	120,321	104,521	276,389	106,791	56,815	113,249	94,258	202,697
I -Change in allocations	--	-4,965	-90,759	-16,902	+104	+13,203	+13,882	+4,411	+13,032	+23,639	+18,849	+12,160	+13,346

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December 27, 1938

Mr. Allan Sproul,
First Vice President,
Federal Reserve Bank of New York,
New York, New York

Dear Mr. Sproul:

There is inclosed a statement prepared from available information showing estimated expenses of each Federal Reserve bank for 1939 and changes in allocations necessary in the System account as of January 1, 1939, on the basis of these estimates.

The omission from the computation of the item prior service contributions to Retirement System has, of course, materially affected the result. In estimating 1939 expenses, figures for the five months July through November of the current year have been used as a basis with an addition of \$60,000 in expenses at the Federal Reserve Bank of Kansas City to cover an anticipated increase in depreciation reserves.

Very truly yours,

E. L. Smead, Chief,
Division of Bank Operations.

Inclosure

by [handwritten initials] and 12/29/38

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J. B. Smith

REALLOCATION OF U. S. SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON JANUARY 1, 1939
 (Earnings on securities estimated at 1.313 per cent per annum)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A - Expenses													
(1) Estimated current expenses, 1939	28,803 ✓	2,124	7,342	2,305	2,857	1,692	1,375	3,216	1,406	995	1,780	1,263	2,508
B. - Earnings													
(1) Estimated current earnings, 1939 (exclusive of earnings on Gov'ts)	1,784 ✓	121	350	206	137	186	42	194	28	82	194	61	183
C - Excess of A-1 over B-1	27,019 ✓	2,003	6,992	2,099	2,720	1,506	1,333	3,022	1,378	913	1,586	1,202	2,325
D - Allocation required (on basis of 1.313% earnings rate on Gov'ts) to produce earnings equal to "C"	2,057,807 ✓	152,552	532,521	199,863	207,159	114,699	101,523	230,160	104,951	69,536	116,222	91,546	177,075
E - Estimated dividends 1939	8,067 ✓	565	3,062	733	809	300	269	807	237	174	253	237	621
F - Allocation of remainder of System holdings (\$2,564,015,000 less \$2,057,807,000) on basis of "E"	506,208 ✓	35,454	192,142	45,996	50,765	18,825	16,880	50,640	14,872	10,918	15,876	14,872	38,968
G. - Total allocation of Gov'ts ("D" plus "F")	2,564,015 ✓	188,006	724,663	205,859	257,924	133,524	118,403	280,800	119,823	80,454	132,098	106,418	216,043
H. - Present allocations	2,564,015 ✓	192,971	815,422	222,761	257,820	120,321	104,521	276,389	106,791	56,815	113,249	94,258	202,697
I - Change in allocations	—	-4,965	-90,759	-16,902	+104	+13,203	+13,882	+4,411	+13,032	+23,639	+18,849	+12,160	+13,346

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EXPLANATION OF THE BASIS FOR COMPUTING ITEMS INDICATED

- A-1 2.4 of current expenses July-November 1938
plus \$60,000 at Kansas City for expected increase in
normal depreciation (fixed machinery and equipment)
- B-1 2.4 of current earnings, exclusive of earnings on
Government securities, July-November 1938.
- D Rate used obtained by telephone from Mr. Miller
December 27, 1938.
- E 6 percent of paid-in capital stock on December 21, 1938.

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FEDERAL RESERVE BANK
OF
KANSAS CITY

December 5, 1938.

AIR MAIL

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D.C.

Dear Mr. Smead:

Under date of November 29 I wrote to Mr. Allan Sproul, as Manager of the System Open Market Account, requesting that consideration be given to some unusual expenditures we are about to make when figuring reallocations of participations as of January 1, 1939. I am this morning in receipt of his reply in which he states that under the present procedure for quarterly reallocations of participations, the figures covering estimated and actual earnings, expenses, dividends, and charges or additions to net earnings of the reserve banks, are assembled by the Board of Governors of the Federal Reserve System for the Committee. He suggests, therefore, that I ascertain whether you have been fully informed concerning the proposed special expenditures of this bank.

Our directors and the Board of Governors have approved an expenditure of approximately \$175,000 to cover the installation of eight new automatic elevators in our building, contracts for which have been signed. In addition, we have under consideration the installation of a power plant for the manufacture of our own electricity at a cost of from \$65,000 to \$75,000. It is probable that large payments will be made on these contracts early next year and we understand that under the accounting manual instructions we would be privileged to charge off approximately \$90,000 on the new elevators during the year. As to the power plant, we understand the entire expenditure could be capitalized since this is an addition rather than a replacement.

It is hoped that you will give consideration to these expenditures when assembling figures for use of the Open Market Committee in making the next reallocation of open market participations.

It will be appreciated also if you will let me have your views as to the accounting procedure we should follow in connection with these expenditures. We have given consideration to the setting up of a liability item as to the elevators and making provisions for reserves before the close of this year. The only reason I can see why this might not be appropriate is that after making provision for the proposed prepayment of prior service liability to the Retirement System, about which I wired you today, our net earnings will probably be exhausted and any such charge as we are now discussing would have to be made against surplus. It is possible that we may not have sufficient earnings after payment of dividends and setting aside

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FEDERAL RESERVE BANK OF KANSAS CITY

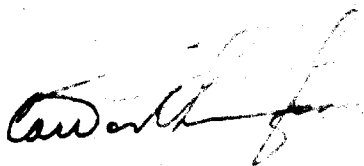
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the usual reserves to make the prepayment of prior service liability in full without a charge to surplus.

Any help you may be able to give us on these problems will be appreciated.

Since these questions will come up for discussion at our directors' meeting on Thursday, December 8, I will appreciate a telegraphic reply.

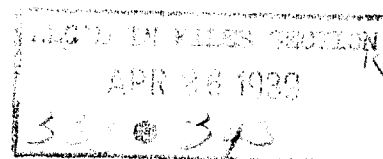
Yours very truly,



C. A. Worthington,
First Vice President.

CAW:L

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October 4, 1938

Mr. Smead
 Mr. Van Fossen

Quarterly allocation of
 System account.

The procedure and formula adopted effective January 1, 1938, for the quarterly allocation of the System account provides for the allocation in two steps, first, in an amount sufficient to cover the excess of expenses for the year over estimated earnings and profits on the sale of Government securities to the date of allocation plus estimated earnings, other than on Government securities, for the remainder of the year; and second, in proportion to dividend requirements.

Inasmuch as the relative share which the various Federal Reserve banks receive in the first and the second steps of the allocation differ considerably, anything that materially changes the amount of Government securities allocated in the first step, as compared with the previous quarterly allocation, will result in disproportionately large changes in individual allocations.

Estimates of expenses and of earnings other than on Governments can be made with sufficient accuracy as not to cause any marked changes for the quarter in the amount of securities allocated in the first step. Profits on the sale of Government securities and changes in the annual earning rate on the System account, however, are two factors, for which no allowance can be made, and which are likely to cause marked fluctuations in participations. Obviously profits realized on the sale of securities and an increased rate of earnings both would have the effect of decreasing the amount of securities allocated in the first step and accordingly would result in an increase in the participation of the New York and other banks that have a relatively large

See attached notes (3)

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Mr. Smead - 2

paid-in capital. Conversely, losses on the sale of Government securities or a reduction in the earning rate would increase the amount of securities required to be allocated in the first step and would reduce the participation of the New York bank and other banks with a relatively high paid-in capital.

8 During the current year profits on Government securities have amounted to approximately \$8,000,000 and the earning rate on allocation dates has varied from a maximum of 1.57 percent to a minimum of 1.2632 percent. The unforeseen profit of about \$8,000,000 on sales of Government securities is equivalent in its effect to an error of about 37 percent in the January 1 estimate of the amount of securities needed to cover the excess of expenses over earnings. The corresponding error on April 1 was about 24 percent and on July 1 about 7 percent. As regards the earning rate, which now is 1.29 percent, an increase in the rate to 1.39 percent per annum would have the same effect on the allocation as an error of over 8 percent in the estimated net excess of expenses over earnings, and a reduction of the rate to 1.19 percent would have an approximately similar effect.

If the amount of securities in System account were increased, additional securities would be allocated to the Federal Reserve banks in accordance with the second step in the previous allocation, i.e., in accordance with dividend requirements. Accordingly, an increase in earnings due to an increase in the System account would increase all participations uniformly in proportion to dividend requirements and would have no effect on the next reallocation. Profits on the sales of Government securities, however, are distributed not in proportion to dividend requirements but in proportion to average participations since July 1, 1936. Under the formula now in use the first step in the allocation automatically offsets the effect of not distributing profits during the preceding quarter in

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Mr. Smead - 3

accordance with dividend requirements. Where, as during the first and second quarters of 1938, profits are substantial this results not only in reducing greatly the amount of securities allocated in the first step but also changes greatly the proportion thereof allocated to individual banks. Differences in total allocations may therefore be due as much to these differences in step one as to those in step two previously referred to.

A number of possible modifications of the formula have been considered with a view to obtaining a formula that would not produce such marked changes in participations. The simplest and most effective means of avoiding substantial changes in participations due to profits would be to disregard profits in the allocation and in effect to make each quarterly allocation on essentially the same basis as the January 1 allocation is made. This procedure would be somewhat undesirable, however, in that it would fall far short of attaining the objective of equalizing dividend coverage. It would not, furthermore, eliminate fluctuations in participations due to changes in the annual earning rate.

A more satisfactory procedure, I believe, would be to combine steps one and two of the present formula so as to make the first allocation in such amount, if possible, as to cover the excess of expenses and dividends over earnings (other than those on Governments after the allocation date) and profits. By so doing the effect of a change in the earning rate would be largely eliminated, inasmuch as in the absence of such disturbing factors as profits the percentage of the securities allocated in this stage allocated to each bank would not vary greatly from quarter to quarter. Any excess earnings could, of course, be allocated as at present in proportion to dividends, and if this

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Mr. Smead - 4

were done results would be identical with those under the present formula whenever the earning rate was high enough to make an allocation under the second step necessary. It does not appear, however, that distribution of earnings in excess of expenses and dividends in proportion to dividend requirements has anything to commend it. A more desirable procedure, of course, would be one that would tend to equalize the position of the Federal Reserve banks in respect to capital, surplus and reserves for contingencies. There is room for a great deal of difference of opinion as to what this should mean in actual practice and as to how the objective could best be achieved. It seems to me that the logical thing to do would be to equalize insofar as possible the position of the various Federal Reserve banks as regards the ratio of total deposits of member banks to the sum of the Federal Reserve banks' own paid-in capital, surplus and reserves for contingencies. This is preferred because differences in paid-in capital of the Federal Reserve banks reflect differences merely in capital and surplus of member banks and the capitalization of member banks in some Federal Reserve districts is much greater in proportion to deposit liabilities than in other Federal Reserve districts. I would recommend that after expenses and dividends have been covered any securities remaining be so allocated as to give each Federal Reserve bank an amount equal to five percent of its dividend requirements merely as an insurance against shortcomings in the estimates resulting in the unexpected failure of earnings to equal expenses and dividends, and then to distribute any remainder equally among a specified number, six perhaps, of the Federal Reserve banks having the highest ratio of total deposits of member banks to the Federal Reserve banks' own paid-in capital, surplus, and reserves for contingencies.

Attached is a revised formula in accordance with the above recommendation.

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Attachment

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A. Expenses and dividends:

- (1) Estimated current expenses during year
- (2) Prior service contribution
- (3) Estimated annual dividends
- (4) Total

B. Earnings:

- (1) Current earnings to latest available data
- (2) Estimated for remainder of year
(exclusive of earnings on Governments
after date of allocation)
- (3) Net profit on Governments sold to date
- (4) Total

C. Excess of A(4) over B(4)

D. Allocation required (on basis of current annual rate of earnings on Governments) to furnish earnings equal to "C".

E. Allocation of remainder of System account.*

F. Total allocation (D + E).

* Allocate to each bank an amount, if available, sufficient to give additional earnings equal to 5 percent of estimated dividends and divide any remainder equally among the six banks having the highest ratio of total deposits of member banks to the sum of its own paid-in capital, surplus and reserves for contingencies.

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ALLOCATIONS OF SYSTEM OPEN MARKET ACCOUNT

APR 25 1968

(In thousands of dollars)

	April 1, 1938	July 1, 1938	Oct. 1, 1938	Jan. 1, 1939	Net change Jan. 1, 1938 to Jan. 1, 1939
A. CHANGES UNDER PRESENT FORMULA					
Boston	-3,300	+11,200	-3,200	-700	+4,100
New York	+6,300	+34,300	+35,300	-114,900	-39,000
Philadelphia	-1,100	+20,200	-8,000	-8,900	+2,300
Cleveland	-7,200	-5,600	+17,600	-12,400	-7,600
Richmond	+3,700	-12,800	-6,900	+22,400	+6,500
Atlanta	+4,000	-200	-6,700	+7,400	+4,500
Chicago	-5,200	+1,600	-2,400	+13,000	+7,000
St. Louis	+4,700	-4,800	-7,600	+19,600	+11,900
Minneapolis	+5,100	-14,900	-16,600	+27,600	+1,200
Kansas City	-7,500	-6,000	-5,400	+23,100	+4,200
Dallas	-2,500	-12,300	+9,300	+7,100	+1,600
San Francisco	+2,800	-10,700	-5,200	+16,500	+3,400
B. ESTIMATED CHANGES IF, ON APRIL 1, JULY 1, and OCTOBER 1, SECURITIES REMAINING AFTER EXPENSES AND DIVIDENDS ARE COVERED ARE DISTRIBUTED IN PROPORTION TO ESTIMATED EXPENSES AND DIVIDENDS.					
Boston	-3,000	+13,000	-1,500	-4,400	+4,100
New York	-7,800	-700	-7,400	-23,000	-39,000
Philadelphia	-2,000	+18,700	-11,300	-3,200	+2,300
Cleveland	-7,700	-7,500	+17,600	-10,200	-7,600
Richmond	+6,300	-7,100	+500	+6,700	+6,500
Atlanta	+5,300	+3,300	-2,800	-1,300	+4,500
Chicago	-3,200	+6,300	+1,800	+2,100	+7,000
St. Louis	+7,000	+900	-300	+4,300	+11,900
Minneapolis	+6,800	-11,300	-12,500	+18,200	+1,200
Kansas City	-4,500	+1,900	+3,800	+3,100	+4,200
Dallas	-1,200	-10,000	+14,200	-1,400	+1,600
San Francisco	+3,900	-7,700	-2,100	+9,100	+3,400

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-2-

April 1, 1938	July 1, 1938	Oct. 1, 1938	Jan. 1, 1939	Net change Jan. 1, 1938 to Jan. 1, 1939
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**C. ESTIMATED CHANGES IF PROFITS ON SALES OF U.S. GOVERNMENT
SECURITIES ARE DISREGARDED (AS IS DONE ON JAN. 1
REALLOCATIONS) AND PRESENT FORMULA OTHERWISE FOLLOWED.**

Boston	-3,000	+12,100	-2,200	-2,800	+4,100
New York	-21,600	-30,600	-1,700	+15,000	-39,000
Philadelphia	-3,200	+15,300	-10,500	+700	+2,300
Cleveland	-7,200	-6,600	+17,200	-11,000	-7,600
Richmond	+7,900	-2,700	-800	+1,900	+6,500
Atlanta	+6,500	+6,200	-3,200	-5,000	+4,500
Chicago	-800	+10,500	+1,600	-4,300	+7,000
St. Louis	+9,400	+6,300	-1,100	-2,600	+11,900
Minneapolis	+8,400	-7,000	-11,800	+11,600	+1,200
Kansas City	-2,300	+6,500	+1,400	-1,300	+4,200
Dallas	+200	-6,200	+13,200	-5,500	+1,600
San Francisco	+5,800	-3,900	-2,000	+3,500	+3,400

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Relative position
of books as regards
prepared on last
page of memo.

- d J. ①
- H C 2
- d J. 3
- liri 4
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- ary 6
- Mem 7
- at 8
- Put 9
- Share 10
- Put 11
- alpha 12

REC'D IN RECORDS SECTION
APR 25 1968

My records
mandates are
incorporated in the
attached Oct. 4 memo
beginning with the
last A on page 3.

44

REC'D IN RECORDS SECTION
APR 25 1968

Van

I think we
should draft
a brief memo
setting forth the
changes we should
like to see made
in formulas.

CH

REC'D IN FILES SECTION
OCT - 1 1938

WJ

CHANGES IN PARTICIPATIONS OF FEDERAL RESERVE BANKS
IN SYSTEM OPEN MARKET ACCOUNT

FOR FILES
A. M. Stone

Federal Reserve Bank	Reallocations required by present approved procedure		Estimated changes on January 1, 1939, if no reallocation is made on October 1, 1938*
	Approximate changes October 1, 1938	Estimated changes January 1, 1939	
Boston	-\$3,000,000	-\$1,000,000	-\$4,000,000
New York	+ 29,000,000	-112,000,000	-83,000,000
Philadelphia	-9,000,000	-8,000,000	-17,000,000
Cleveland	+18,000,000	-12,000,000	+5,000,000
Richmond	-6,000,000	+22,000,000	+16,000,000
Atlanta	-6,000,000	+7,000,000	+1,000,000
Chicago	-2,000,000	+13,000,000	+11,000,000
St. Louis	-6,000,000	+19,000,000	+13,000,000
Minneapolis	-16,000,000	+27,000,000	+11,000,000
Kansas City	-4,000,000	+22,000,000	+18,000,000
Dallas	+10,000,000	+ 7,000,000	+17,000,000
San Francisco	-5,000,000	+16,000,000	+12,000,000

*Changes on October 1, 1938, if made, combined with subsequent changes on January 1, 1939, would equal the changes necessary on January 1, 1939, as shown below, in the event that no reallocation was made on October 1, 1938.

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LES SECTION
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H. J. Lab
10/1/38

REALLOCATION OF UNITED STATES SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON OCTOBER 1, 1938
Earnings on Securities estimated at 1.29% per annum

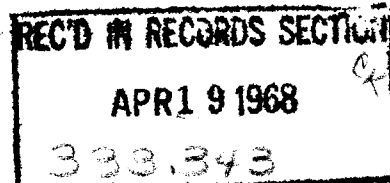
(Amounts in thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A. Expenses													
(1) Estimated current expenses, 1938	28,695	2,175	7,336	2,438	2,763	1,677	1,317	3,240	1,415	1,007	1,665	1,154	2,508
(2) Prior service contributions	2,521	179	639	193	220	157	94	333	145	83	171	109	198
(3) Total	<u>31,216</u>	<u>2,354</u>	<u>7,975</u>	<u>2,631</u>	<u>2,983</u>	<u>1,834</u>	<u>1,411</u>	<u>3,573</u>	<u>1,560</u>	<u>1,090</u>	<u>1,836</u>	<u>1,263</u>	<u>2,706</u>
B. Earnings													
(1) Estimated current earnings, 1938 (exclusive of earnings on Gov'ts)	1,819	139	379	218	144	133	43	212	40	83	195	66	167
(2) Estimated earnings on Gov'ts to Sept. 30	26,114	1,931	7,682	2,212	2,512	1,372	1,120	2,847	1,182	834	1,278	961	2,183
(3) Net profits on Gov'ts to Sept. 28	7,973	573	2,230	671	787	422	342	899	371	271	401	313	693
(4) Total	<u>35,906</u>	<u>2,643</u>	<u>10,291</u>	<u>3,101</u>	<u>3,443</u>	<u>1,927</u>	<u>1,505</u>	<u>3,958</u>	<u>1,593</u>	<u>1,188</u>	<u>1,874</u>	<u>1,340</u>	<u>3,043</u>
C. Excess of B-4 over A-3	4,690	289	2,316	470	460	93	94	385	33	98	38	77	337
D. Estimated dividends, 1938	8,017	564	3,057	735	799	298	267	790	234	174	250	236	613
E. Allocation required (on basis of 1.29% earnings rate on Gov'ts) to produce earnings Oct.-Dec. equal to "D" minus "C"	1,023,222	84,576	227,895	81,501	104,260	63,048	53,206	124,558	61,818	23,374	65,201	48,901	84,884
F. Allocation of remainder of System holdings (\$2,564,015,000 less \$1,023,222,000) on basis of "D"	1,540,793	108,395	587,527	141,260	153,560	57,273	51,315	151,831	44,973	33,441	48,048	45,357	117,813
G. Total allocation of Gov'ts ("E" plus "F")	2,564,015	192,971	815,422	222,761	257,820	120,321	104,521	276,389	106,791	56,815	113,249	94,258	202,697
H. Present allocations	2,564,015	196,203	780,147	230,771	240,262	127,224	111,196	278,831	114,411	73,430	118,631	84,963	207,946
I. Change in allocations	--	-3,232	+35,275	-8,010	+17,558	-6,903	-6,675	-2,442	-7,620	-16,615	-5,382	+9,295	-5,249

FOR FILE
J. E. SMITH

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Authority E.O. 12958

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DECLASSIFIED
Authority E.O. 12958FEDERAL RESERVE BANK
OF NEW YORK

September 29, 1938.

Dear Mr. Smead:

Receipt is acknowledged of your letter of September 28, enclosing computation showing adjustments to be made in the participations in the System Open Market Account on October 1, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on November 30, 1937.

Two copies of the computation showing the adjustments to be made are enclosed herewith together with a copy of telegram which was sent to each of the banks today and a copy of the letter of transmittal which was sent with the computation.

I note that you have been studying, without reaching any conclusions, the matter of large fluctuations in allocations on quarterly dates. When I have had a chance to become familiar with this problem I shall be glad to discuss the subject with you.

Very truly yours,

A handwritten signature in dark ink, appearing to read "Allan Sproul".

Allan Sproul
Manager, System Open
Market Account

Encls. (4)

Directive #1

DECLASSIFIED Authority <u>E.O. 12958</u>
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Following telegram sent to each Federal Reserve Bank as indicated below:

Under the plan for reallocation of government securities adopted by the Federal Open Market Committee November 30, 1937, a readjustment of participations in government securities held in the System Account is called for on October 1. The computations showing adjustments to be made in participations of the several Federal Reserve banks is being sent to all Reserve Banks today. These computations indicate an ^{increase} decrease of _____ in your participation on October 1. We shall advise you on October 1 the detailed entries to be made on that date.

SPROUL

		<u>INCREASE</u>	<u>DECREASE</u>
Young	Boston	-0-	\$3,232,000
Sinclair	Philadelphia	-0-	3,010,000
Fleming	Cleveland	\$17,558,000	-0-
Leach	Richmond	-0-	6,903,000
Newton	Atlanta	-0-	6,675,000
Schaller	Chicago	-0-	2,442,000
Martin	St. Louis	-0-	7,620,000
Peyton	Minneapolis	-0-	16,615,000
Hamilton	Kansas City	-0-	5,382,000
McKirmey	Dallas	9,295,000	-0-
Day	San Francisco	-0-	5,249,000

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Similar letter sent to president of each Federal Reserve Bank except New York

September 29, 1958.

Dear Mr. Young:

In accordance with my telegram of today, I enclose herewith computation of the readjustments to be made, on October 1, of the participations of the Federal Reserve banks in the System Open Market Account.

Very truly yours,

Allan Sproul
Manager, System Open
Market Account

Honorable Roy A. Young, President,
Federal Reserve Bank of Boston,
Boston, Mass.

Encl.

RHB/JH

REALLOCATION OF UNITED STATES SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON OCTOBER 1, 1938
Earnings on Securities estimated at 1.29% per annum

(Amounts in thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A. Expenses													
(1) Estimated current expenses, 1938	28,695	2,175	7,336	2,438	2,763	1,677	1,317	3,240	1,415	1,007	1,665	1,154	2,508
(2) Prior service contributions	2,521	179	639	193	220	157	94	333	145	83	171	109	198
(3) Total	<u>31,216</u>	<u>2,354</u>	<u>7,975</u>	<u>2,631</u>	<u>2,983</u>	<u>1,834</u>	<u>1,411</u>	<u>3,573</u>	<u>1,560</u>	<u>1,090</u>	<u>1,836</u>	<u>1,263</u>	<u>2,706</u>
B. Earnings													
(1) Estimated current earnings, 1938 (exclusive of earnings on Gov'ts)	1,819	139	379	218	144	133	43	212	40	83	195	66	167
(2) Estimated earnings on Gov'ts to Sept. 30	26,114	1,931	7,682	2,212	2,512	1,372	1,120	2,847	1,182	834	1,278	961	2,183
(3) Net profits on Gov'ts to Sept. 28	7,973	573	2,230	671	787	422	342	899	371	271	401	313	693
(4) Total	<u>35,906</u>	<u>2,643</u>	<u>10,291</u>	<u>3,101</u>	<u>3,443</u>	<u>1,927</u>	<u>1,505</u>	<u>3,958</u>	<u>1,593</u>	<u>1,188</u>	<u>1,874</u>	<u>1,340</u>	<u>3,043</u>
C. Excess of B-4 over A-3	4,690	289	2,316	470	460	93	94	385	33	98	38	77	337
D. Estimated dividends, 1938	8,017	564	3,057	735	799	298	267	790	234	174	250	236	613
E. Allocation required (on basis of 1.29% earnings rate on Gov'ts) to produce earnings Oct.-Dec. equal to "D" minus "C"	1,023,222	84,576	227,895	81,501	104,260	63,048	53,206	124,558	61,818	23,374	65,201	48,901	84,884
F. Allocation of remainder of System holdings (\$2,564,015,000 less \$1,023,222,000) on basis of "D"	1,540,793	108,395	587,527	141,260	133,560	57,273	51,315	151,831	44,973	33,441	48,048	45,357	117,813
G. Total allocation of Gov'ts ("E" plus "F")	2,564,015	192,971	815,422	222,761	257,820	120,321	104,521	276,389	106,791	56,815	113,249	94,258	202,697
H. Present allocations	2,564,015	196,203	780,147	230,771	240,262	127,224	111,196	278,831	114,411	73,430	118,631	84,963	207,946
I. Change in allocations	--	-3,232	+35,275	-8,010	+17,558	-6,903	-6,675	-2,442	-7,620	-16,615	-5,382	+9,295	-5,249

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REC'D IN FILES SECTION
SEP 29 1938
333-343

E Carded *OB*

September 28, 1938.

*x Sys O in account
x Reallocation of Sec.*

Mr. Allan Sproul,
First Vice President,
Federal Reserve Bank of New York,
New York, N. Y.

Dear Mr. Sproul:

There is inclosed a statement prepared from available information showing estimated earnings and expenses of each Federal Reserve bank for 1938, and changes in allocations as of October 1 necessary in the System Account on the basis of these estimates.

In my letter to Mr. Matteson, dated June 25, 1938, I stated that I hoped to have Mr. Van Fossen do some work on the formula now in use during the coming months with the object, if possible, of finding a way to reduce somewhat the marked fluctuations in allocations on quarterly dates. We have not reached any conclusions with respect to this matter as yet, but I should like to discuss the subject with you at an early date.

Very truly yours,

E. L. Smead, Chief,
Division of Bank Operations.

Inclosure

Waf

ELS/jbc

FILE COPY

see letter 3/22/39

FOR FILES
I. B. Smith

REALLOCATION OF UNITED STATES SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON OCTOBER 1, 1938

Earnings on Securities estimated at 1.29% per annum

(Amounts in thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A. Expenses													
(1) Estimated current expenses, 1938	28,695	2,175	7,336	2,438	2,763	1,677	1,317	3,240	1,415	1,007	1,665	1,154	2,508
(2) Prior service contributions	2,521	179	639	193	220	157	94	333	145	83	171	109	198
(3) Total	31,216	2,354	7,975	2,631	2,983	1,834	1,411	3,573	1,560	1,090	1,836	1,263	2,706
Earnings													
(1) Estimated current earnings, 1938 (exclusive of earnings on Gov'ts)	1,819	139	379	218	114	133	43	212	40	83	195	66	167
(2) Estimated earnings on Gov'ts to Sept. 30	26,114	1,931	7,682	2,212	2,512	1,372	1,120	2,847	1,182	834	1,278	961	2,183
(3) Net profits on Gov'ts to Sept. 28	7,973	573	2,230	571	787	422	312	899	371	271	401	313	693
(4) Total	35,906	2,643	10,291	3,101	3,413	1,927	1,505	3,958	1,593	1,188	1,874	1,340	3,043
C. Excess of B-4 over A-3	4,690	289	2,316	470	460	93	94	385	33	98	38	77	337
D. Estimated dividends, 1938	8,017	564	3,057	735	799	298	267	790	234	174	250	236	613
Allocation required (on basis of 1.29% earnings rate on Gov'ts) to produce earnings Oct.-Dec. equal to "D" minus "C"	1,023,222	84,576	227,895	81,501	104,260	63,048	53,206	124,558	61,818	23,374	65,201	48,901	84,884
F. Allocation of remainder of System holdings (\$2,564,015,000 less \$1,023,222,000) on basis of "D"	1,540,793	108,395	587,527	141,260	153,560	57,273	51,315	151,831	44,973	33,441	48,048	45,357	117,813
G. Total allocation of Gov'ts ("E" plus "F")	2,564,015	192,971	815,422	222,761	257,820	120,321	104,521	276,389	106,791	56,815	113,249	94,258	202,697
H. Present allocations	2,564,015	196,203	780,147	230,771	240,262	127,224	111,196	278,831	114,411	73,430	118,631	84,963	207,946
I. Change in allocations	—	-3,232	+35,275	-8,010	+17,558	-6,903	-6,675	-2,442	-7,620	-16,615	-5,382	+9,295	-5,249

FOR FILES
checked
11/15/38
[Signature]

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PARTICIPATION OF FEDERAL RESERVE
 BANKS IN SYSTEM OPEN MARKET ACCOUNT

FD IN RECORDS SECTION
 APR 9 1968
 333,343

9/22/38

CK

The procedure followed in allocating participations in the System Open Market Account provides for reallocations as of January, April, July, and October 1st of each year.

The formula now used for allocating participations in the System Open Market Account among the twelve Federal Reserve banks provides, among other things, that each Federal Reserve bank shall be allotted sufficient securities to produce earnings equal to its expenses and other fixed charges, and that any securities then remaining undistributed be allocated to the Federal Reserve banks on the basis of dividend requirements.

Since profits on securities since January 1, 1938, have been exceptionally large, approximately \$7,800,000, earnings to date have been sufficient to cover all of the expenses of the Federal Reserve banks for the calendar year 1938 and part of accrued dividends. Accordingly, under the existing formula the securities in the System Account would be reallocated among the Federal Reserve banks as of October 1 in the proportion of dividend requirements only. At the beginning of the year the securities in the Account were allocated, as stated above, on the basis of expenses and then dividends, and since for the last quarter of the year they would, under the formula, be allocated on the basis of dividend requirements only, it is apparent that if the expenses of a given bank bear a higher ratio to the total expenses of the System than its dividend requirements bear to the total dividend requirements of the System, it would get a substantial decrease in its participation in the Account for the last quarter of the present year.

Beginning January 1, 1939, the securities in the Account will again be reallocated among the Federal Reserve banks on the basis of expense and

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- 2 -

dividend requirements, and presumably as in the past, without making allowance at that time for possible profits during the year. The attached statement shows the approximate changes which, on the basis of the existing approved formula, should be made as of October 1, 1938, in the participations of the twelve Federal Reserve banks in the System Account, and estimated changes in allocations as of January 1, 1939, (a) if the reallocation is made as of October 1, and (b) if the reallocation is not made as of October 1.

It is apparent from the attached statement that if the reallocation is made as of October 1 the changes in participations as of January 1, 1939, will be much larger than they would be at that time if no reallocation is made on October 1. In the circumstances, and since there is no particular point in allocating securities among the Federal Reserve banks on the basis of dividend requirements only, as would be the case if the October 1, 1938, reallocation is made, it may be well to consider whether any further reallocation of securities in the System Account should be deferred until January 1, 1939.

If it is thought advisable not to make any reallocation as of October 1, 1938, it presumably will be necessary for the Federal Open Market Committee to take the matter up with each Federal Reserve bank.

Attachment
9/22/38.

CHANGES IN PARTICIPATIONS OF FEDERAL RESERVE BANKS
IN SYSTEM OPEN MARKET ACCOUNT

Federal Reserve Bank	Reallocations required by present approved procedure		Estimated changes on January 1, 1939, if no reallocation is made on October 1, 1938*
	Approximate changes October 1, 1938	Estimated changes January 1, 1939	
Boston	-\$3,000,000	-\$1,000,000	-\$4,000,000
New York	+29,000,000	-112,000,000	-83,000,000
Philadelphia	-9,000,000	-8,000,000	-17,000,000
Cleveland	+18,000,000	-12,000,000	+5,000,000
Richmond	-6,000,000	+22,000,000	+16,000,000
Atlanta	-6,000,000	+7,000,000	+1,000,000
Chicago	-2,000,000	+13,000,000	+11,000,000
St. Louis	-6,000,000	+19,000,000	+13,000,000
Minneapolis	-16,000,000	+27,000,000	+11,000,000
Kansas City	-4,000,000	+22,000,000	+18,000,000
Dallas	+10,000,000	+7,000,000	+17,000,000
San Francisco	-5,000,000	+16,000,000	+12,000,000

*Changes on October 1, 1938, if made, combined with subsequent changes on January 1, 1939, would equal the changes necessary on January 1, 1939, as shown below, in the event that no reallocation was made on October 1, 1938.

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RATIO OF EACH FEDERAL RESERVE BANK'S REQUIREMENTS
FOR EXPENSES AND PRIOR SERVICE CONTRIBUTIONS AND
FOR DIVIDENDS TO SUCH REQUIREMENTS FOR THE SYSTEM AS A WHOLE

Federal Reserve Bank	<u>Percent to System Total</u>	
	<u>Expenses and Prior Service Contributions</u>	<u>Dividend Requirements</u>
Boston	7.5	7.0
New York	25.5	38.1
Philadelphia	8.4	9.2
Cleveland	9.6	10.0
Richmond	5.9	3.7
Atlanta	4.5	3.3
Chicago	11.4	9.9
St. Louis	5.0	2.9
Minneapolis	3.5	2.2
Kansas City	5.9	3.1
Dallas	4.1	2.9
San Francisco	<u>8.7</u>	<u>7.7</u>
TOTAL	100.0	100.0

CHANGES IN PARTICIPATIONS IN SYSTEM OPEN MARKET ACCOUNT RESULTING FROM RE-
 ALLOCATION OF SECURITIES ON DATES INDICATED
 (In thousands of dollars)

FILE IN FILES SECTION
 JAN 14 1939
 3330 B43

9/1/38

Federal Reserve Bank	October 1, 1936	January 1, 1937	April 1, 1937	January 1, 1938	April 1, 1938	July 1, 1938
Boston	+ 12,477	+ 1,488	+ 1,617	+ 1,445	- 3,277	+ 11,241
New York	- 15,318	+ 7,017	+35,535	- 150	+ 6,301	+ 34,292
Philadelphia	- 2,191	-14,213	+ 9,635	- 5,243	- 1,082	+ 20,243
Cleveland	+ 9,975	+ 4,458	-13,613	+ 3,447	- 7,161	- 5,616
Richmond	- 2,501	+ 7,907	- 3,837	+ 1,901	+ 3,682	- 12,755
Atlanta	+ 832	+10,753	- 2,117	- 4,778	+ 3,955	- 219
Chicago	- 5,174	- 7,523	- 7,128	+ 399	- 5,151	+ 1,592
St. Louis	- 14,118	+ 245	- 7,451	+ 1,995	+ 4,742	- 4,809
Minneapolis	+ 4,110	- 5,279	- 5,366	+ 237	+ 5,130	- 14,945
Kansas City	+ 2,928	+ 746	- 5,352	+ 6,841	- 7,477	- 5,996
Dallas	+ 7,067	- 5,671	+ 884	+ 36	- 2,484	- 12,320
San Francisco	+ 1,913	+ 72	- 2,807	- 6,130	+ 2,822	- 10,708

Prepared for Mr. Smead September 1938.

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 Authority E.O. 12958

SEP 14 1938

CHANGES IN PARTICIPATIONS IN SYSTEM OPEN MARKET ACCOUNT RESULTING FROM RE-
ALLOCATION OF SECURITIES ON DATES INDICATED
(In thousands of dollars)

Federal Reserve Bank	October 1, 1936	January 1, 1937	April 1, 1937	January 1, 1938	April 1, 1938	July 1, 1938
Boston	+ 12,477	+ 1,488	+ 1,617	+ 1,445	- 3,277	+ 11,241
New York	- 15,318	+ 7,017	+35,535	- 150	+ 6,301	+ 34,292
Philadelphia	- 2,191	-14,213	+ 9,635	- 5,243	- 1,082	+ 20,243
Cleveland	+ 9,975	+ 4,458	-13,613	+ 3,447	- 7,161	- 5,616
Richmond	- 2,501	+ 7,907	- 3,837	+ 1,901	+ 3,682	- 12,755
Atlanta	+ 832	+10,753	- 2,117	- 4,778	+ 3,955	- 219
Chicago	- 5,174	- 7,523	- 7,128	+ 399	- 5,151	+ 1,592
St. Louis	- 14,118	+ 245	- 7,451	+ 1,995	+ 1,742	- 4,809
Minneapolis	+ 4,110	- 5,279	- 5,366	+ 237	+ 5,130	- 14,945
Kansas City	+ 2,928	+ 746	- 5,352	+ 6,841	- 7,477	- 5,996
Dallas	+ 7,067	- 5,671	+ 884	+ 36	- 2,484	- 12,320
San Francisco	+ 1,913	+ 72	- 2,907	- 6,130	+ 2,822	- 10,708

Prepared for Mr. Smead September 1938.

MP

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REC'D IN FILES SECTION

W JAN 14 1939

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COMPARISON OF ESTIMATED CURRENT EXPENSES (MADE IN CONNECTION WITH REALLOCATION OF SYSTEM OPEN MARKET ACCOUNT AS OF DATES INDICATED) WITH ACTUAL CURRENT EXPENSES

Federal Reserve Bank	Percent to actual for 1936 estimated as of		Percent to actual for 1937 estimated as of			Percent to actual for 1938** estimated as of		
	June 30, 1936	Oct. 1, 1936	Jan. 1, 1937	April 1, 1937	July 1, 1937*	Jan. 1, 1938	April 1, 1938	July 1, 1938
Boston	92.3	98.8	98.6	97.7	97.8	100.9	98.0	99.1
New York	106.3	101.0	97.1	97.0	98.1	101.4	102.4	100.0
Philadelphia	104.6	100.8	99.8	100.7	99.1	100.2	99.8	100.0
Cleveland	97.3	101.7	108.7	102.0	97.5	105.8	102.6	100.0
Richmond	100.1	98.7	100.8	100.0	98.0	105.5	105.6	100.0
Atlanta	97.3	98.2	109.0	107.8	97.4	103.9	105.6	103.9
Chicago	103.4	100.6	106.8	102.6	97.5	102.2	99.9	100.0
St. Louis	113.4	101.3	105.4	101.5	95.1	98.8	101.1	100.0
Minneapolis	98.1	103.4	105.1	99.5	95.3	105.9	109.5	101.5
Kansas City	95.2	99.8	99.9	97.9	98.4	106.9	100.6	100.0
Dallas	92.6	101.1	99.3	100.8	94.2	112.5	107.1	100.0
San Francisco	99.3	100.7	103.9	102.4	101.6	101.6	101.6	100.0
Total	101.3	100.6	101.9	100.1	97.9	102.9	102.1	100.2

* Date of proposed reallocation

** On five months' basis.

Prepared for Mr. Smead September 1938.

FOR FILES
H. B. Daniels

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REC'D IN FILES SECTION
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COMPARISON OF ESTIMATED CURRENT EXPENSES (MADE IN CONNECTION WITH REALLOCATION OF SYSTEM OPEN MARKET ACCOUNT AS OF DATES INDICATED) WITH ACTUAL CURRENT EXPENSES

Federal Reserve Bank	Percent to actual for 1936 estimated as of		Percent to actual for 1937 estimated as of			Percent to actual for 1938** estimated as of		
	June 30, 1936	Oct. 1, 1936	Jan. 1, 1937	April 1, 1937	July 1, 1937*	Jan. 1, 1938	April 1, 1938	July 1, 1938
Boston	92.3	98.8	98.6	97.7	97.8	100.9	98.0	99.1
New York	106.3	101.0	97.1	97.0	98.1	101.4	102.4	100.0
Philadelphia	104.6	100.8	99.8	100.7	99.1	100.2	99.8	100.0
Cleveland	97.3	101.7	108.7	102.0	97.5	105.8	102.6	100.0
Richmond	100.1	98.7	100.8	100.0	98.0	105.5	105.6	100.0
Atlanta	97.3	98.2	109.0	107.8	97.4	103.9	105.6	103.9
Chicago	103.4	100.6	106.8	102.6	97.5	102.2	99.9	100.0
St. Louis	113.4	101.3	105.4	101.5	95.1	98.8	101.1	100.0
Minneapolis	98.1	103.4	105.1	99.5	95.3	105.9	109.5	101.5
Kansas City	95.2	99.8	99.9	97.9	98.4	106.9	100.6	100.0
Dallas	92.6	101.1	99.3	100.8	94.2	112.5	107.1	100.0
San Francisco	99.3	100.7	103.9	102.4	101.6	101.6	101.6	100.0
Total	101.3	100.6	101.9	100.1	97.9	102.9	102.1	100.2

* Date of proposed reallocation
 ** On five months' basis.

Prepared for Mr. Smead September 1938.

FOR FILES
 H. B. Daniels

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 Authority E.O. 12958

COMPARISON OF ESTIMATED CURRENT EXPENSES (MADE IN CONNECTION WITH REALLOCATION OF SYSTEM OPEN MARKET ACCOUNT AS OF DATES INDICATED) WITH ACTUAL CURRENT EXPENSES

Federal Reserve Bank	Percent to actual for 1936 estimated as of		Percent to actual for 1937 estimated as of			Percent to actual for 1938 ^o estimated as of		
	June 30, 1936	Oct. 1, 1936	Jan. 1, 1937	April 1, 1937	July 1, 1937 ^o	Jan. 1, 1938	April 1, 1938	July 1, 1938
Boston	92.3	98.8	98.6	97.7	97.8	100.9	98.0	99.1
New York	106.3	101.0	97.1	97.0	98.1	101.4	102.4	100.0
Philadelphia	104.6	100.8	99.8	100.7	99.1	100.2	99.8	100.0
Cleveland	97.3	101.7	108.7	102.0	97.5	105.8	102.6	100.0
Richmond	100.1	98.7	100.8	100.0	98.0	105.5	105.6	100.0
Atlanta	97.3	98.2	109.0	107.8	97.4	103.9	105.6	103.9
Chicago	103.4	100.6	106.8	102.6	97.5	102.2	99.9	100.0
St. Louis	113.4	101.3	105.4	101.5	95.1	98.8	101.1	100.0
Minneapolis	98.1	103.4	105.1	99.5	95.3	105.9	109.5	101.5
Kansas City	95.2	99.8	99.9	97.9	98.4	106.9	100.6	100.0
Dallas	92.6	101.1	99.3	100.8	94.2	112.5	107.1	100.0
San Francisco	99.3	100.7	103.9	102.4	101.6	101.6	101.6	100.0
Total	101.3	100.6	101.9	100.1	97.9	102.9	102.1	100.2

^o Date of proposed reallocation
^{oo} On five months' basis.

Prepared for Mr. Smead September 1938.

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*Mr. Mead
The Board
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FEDERAL RESERVE BANK
OF NEW YORK

DIVISION OF
BANK OPERATIONS

June 27, 1938.

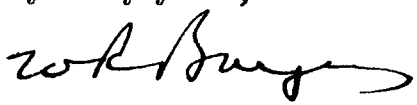
Dear Mr. Smead:

We have your letter of June 25 and have today sent to the Reserve banks a copy of the computation showing the adjustments to be made in participations in the System Open Market Account as of July 1, 1938, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on November 30, 1937.

A copy of the letter of transmittal is enclosed herewith.

We note that you will make a further study of the formula now used.

Very truly yours,



W. R. Burgess
Manager, System Open
Market Account

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

Encl.

JN

Directive #1

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Similar letter sent to President of each Federal Reserve Bank as follows:

Boston	\$11,241,000+	Chicago	\$ 1,592,000 +
Philadelphia	20,243,000+	St. Louis	4,809,000 -
Cleveland	5,616,000-	Minneapolis	14,945,000 -
Richmond	12,755,000-	Kansas City	5,996,000 -
Atlanta	219,000-	Dallas	12,520,000 -
San Francisco			\$10,708,000 -

June 27, 1938.

Dear Mr. Harrison:

In connection with the plan for reallocation of government securities adopted by the Federal Open Market Committee at its meeting on November 30, 1937, a copy of the computation showing the adjustments to be made in participations as of July 1, 1938 is being sent to all Reserve banks.

A copy of this statement is enclosed herewith, which indicates that your participation in the System Open Market Account will be increased \$34,292,000.

Changes in allocations are somewhat more marked than usual and are due in no small part to the size of profits which the System has received on governments since January 1. To the extent that earnings exceed expenses they are allocated in accordance with dividend requirements which are somewhat differently distributed among the reserve banks than the requirements for earnings.

We shall advise you on July 1 the detailed entries to be made on that date.

Very truly yours,

W. R. Burgess
Manager, System Open
Market Account

Mr. George L. Harrison, President,
Federal Reserve Bank of New York,
New York, N. Y.

Encl.

REALLOCATION OF UNITED STATES GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON JULY 1, 1938

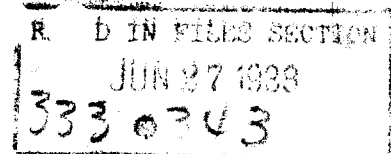
Earnings on securities computed at 1.2632 percent per annum

(Amounts in thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
A. Expenses													
(1) Estimated current expenses, 1938	28,662	2,178	7,350	2,481	2,708	1,675	1,321	3,251	1,410	1,015	1,654	1,111	2,508
(2) Prior service contributions	2,521	179	639	193	220	157	94	333	145	83	171	109	198
(3) Total	31,183	2,357	7,989	2,674	2,928	1,832	1,415	3,584	1,555	1,098	1,825	1,220	2,706
B. Earnings													
(1) Estimated current earnings, 1938 (exclusive of earnings on Gov'ts)	1,789	137	376	227	144	131	39	227	35	54	191	68	160
(2) Estimated earnings on Gov'ts to June 30	17,987	1,309	5,209	1,481	1,751	968	767	1,966	819	601	902	691	1,523
(3) Net profits on Gov'ts to June 24	6,674	479	1,864	562	659	353	287	754	311	227	336	262	580
(4) Total	26,450	1,925	7,449	2,270	2,554	1,452	1,093	2,947	1,165	882	1,429	1,021	2,263
C. Excess of A-3 over B-4	4,733	432	540	404	374	380	322	637	390	216	396	199	443
D. Allocation required (on basis of 1.2632% per annum earnings rate on Gov'ts) to produce earnings July-December equal to "C"	743,259	67,840	84,800	63,443	58,732	59,674	50,566	100,033	61,245	33,920	62,187	31,251	69,568
E. Ratio of estimated dividend requirements for year to system total	100.00	7.05	38.19	9.19	9.97	3.71	3.33	9.82	2.92	2.17	3.10	2.95	7.60
F. Allocation of remainder of System holdings (\$2,564,015 less \$743,259,000) on basis of "E"	1,820,756	128,363	695,347	167,328	181,529	67,550	60,631	178,798	53,166	39,510	56,444	53,712	138,378
G. Total allocation of Gov'ts ("D" + "F")	2,564,015	196,203	780,147	230,771	240,261	127,224	111,197	278,831	114,411	73,430	118,631	84,963	207,946
H. Present allocations	2,564,015	184,962	745,855	210,528	245,877	139,979	111,416	277,239	119,220	88,375	124,627	97,283	218,654
I. Change in allocations	--	+11,241	+34,292	+20,243	-5,616	-12,755	-219	+1,592	-4,809	-14,945	-5,996	-12,320	-10,708

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June 25, 1938.

Mr. W. B. Matteson, Asst. Vice President,
 Federal Reserve Bank of New York,
 New York, N. Y.

Dear Mr. Matteson:

In accordance with our understanding over the telephone this morning, there is enclosed a copy of our calculation on the "Reallocation of United States Government Securities in System Open Market Account on July 1, 1938".

Changes in allocations are somewhat more marked than usual and Mr. Van Fossen advises me that they are due in no small part to the larger profits which the System has received on Governments since January 1. For example, the expenses of your bank are about 25 percent of the expenses for the System as a whole, whereas the dividend requirements for your bank amount to about 38 percent of the requirements for the System as a whole. Consequently, under the present formula the more earnings exceed expenses the larger your relative participation in the System account. I hope to have Mr. Van Fossen do some work on the formula during the coming months and if he is able to develop anything which would reduce somewhat the marked fluctuations in allocations on quarterly dates, we shall take the matter up with Dr. Burgess.

Very truly yours,

[Handwritten signature]

E. L. Smead, Chief,
 Division of Bank Operations

ELS/jbs

REALLOCATION OF UNITED STATES GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON JULY 1, 1938

Earnings on securities computed at 1.2632 percent per annum

(Amounts in thousands of dollars)

	System	Boston	New York	Phila-delphia	Cleve-land	Rich-mond	Atlanta	Chicago	St. Louis	Minn-neapolis	Kansas City	Dallas	San Francisco
A. Expenses													
(1) Estimated current expenses, 1938	28,662	2,178	7,350	2,481	2,708	1,675	1,321	3,251	1,410	1,015	1,654	1,111	2,508
(2) Prior service contributions	2,521	179	639	193	220	157	94	333	145	83	171	109	198
(3) Total	31,183	2,357	7,989	2,674	2,928	1,832	1,415	3,584	1,555	1,098	1,825	1,220	2,706
B. Earnings													
(1) Estimated current earnings, 1938 (exclusive of earnings on Gov'ts)	1,789	137	376	227	144	131	39	227	35	54	191	68	160
(2) Estimated earnings on Gov'ts to June 30	17,987	1,309	5,209	1,481	1,751	968	767	1,966	819	601	902	691	1,523
(3) Net profits on Gov'ts to June 24	6,674	479	1,864	562	659	353	287	754	311	227	336	262	580
(4) Total	26,450	1,925	7,449	2,270	2,554	1,452	1,093	2,947	1,165	882	1,429	1,021	2,263
C. Excess of A-3 over B-4	4,733	432	540	404	374	380	322	637	390	216	396	199	443
D. Allocation required (on basis of 1.2632% per annum earnings rate on Gov'ts) to produce earnings July-December equal to "C"	743,259	67,840	84,800	63,443	58,732	59,674	50,506	100,033	61,245	33,920	62,187	31,251	69,568
E. Ratio of estimated dividend requirements for year to system total	100.00	7.05	38.19	9.19	9.97	3.71	3.33	9.82	2.92	2.17	3.10	2.95	7.60
F. Allocation of remainder of System holdings (\$2,564,015 less \$743,259,000) on basis of "E"	1,820,756	128,363	695,367	167,328	181,529	67,550	60,631	178,798	53,166	39,510	56,444	53,712	138,378
G. Total allocation of Gov'ts ("F" + "D")	2,564,015	196,203	780,147	230,771	240,261	127,224	111,197	278,831	114,411	73,430	118,631	84,963	207,946
H. Present allocations	2,564,015	184,962	745,855	210,528	245,077	139,979	111,416	277,239	119,220	88,375	121,627	97,283	218,654
I. Change in allocations	--	+11,241	+34,292	+20,243	-5,816	-12,755	-219	+1,592	-4,809	-14,945	-5,996	-12,320	-10,708

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Footnotes to statement on reallocation of Govern-
ment securities July 1, 1938.

- A. (1) Estimated current expenses, 1938 a/
- B. (2) Estimated earnings on Gov'ts. to June 30 b/
- D. Allocation required (on basis of 1.2632% per annum earnings rate on Gov'ts.) to produce earnings July-Dec. equal to "C" c/
- E. Ratio of estimated dividend requirements for year to System total d/
- a/ 2.4 of current expenses January-May, less \$19,000 at Boston to adjust for estimate of salaries on monthly basis while payment is made weekly, plus \$50,000 at Atlanta for repairs and alterations to bank building, and plus \$15,000 at Minneapolis for furniture and equipment.
- b/ Actual January 1 - June 26 plus estimated for remainder of June (obtained by phone from Mr. Behrens at New York, June 24).
- c/ Actual rate used .63679% (184/365 of 1.2632%)
- d/ Based on dividends accrued January-May plus 3.5% of paid-in capital stock, May 31.

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FEDERAL RESERVE BANK
OF NEW YORK

RECEIVED
REC'D IN FILES SECTION
MAR 29 1938
333 DIVISION OF
BANK OPERATIONS

March 28, 1938.

Dear Mr. Smead:

In accordance with telephone conversation today, we have sent to the reserve banks a copy of the computation showing the adjustments to be made in participations in the System Open Market Account as of April 1, 1938, pursuant to the plan adopted at the meeting of the Federal Open Market Committee on November 30, 1937.

A copy of the letter of transmittal is enclosed herewith.

Very truly yours,



W. R. Burgess
Manager, System Open
Market Account

Mr. E. L. Smead, Chief,
Division of Bank Operations,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

Encl.

FBI FILES
J. Weeks

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FILED IN FILED SECTION
MAR 24 1938

March 28, 1938.

Dear Mr. Sinclair:

In connection with the plan for reallocation of government securities adopted by the Federal Open Market Committee at its meeting on November 30, 1937, a copy of the computation showing the adjustments to be made in participations as of April 1, 1938 is being sent to all Reserve banks.

A copy of this statement is enclosed herewith, which indicates that your participation in the System Open Market Account will be decreased \$1,082,000.

We shall wire you on April 1 the detailed entries to be made on that date.

Very truly yours,

W. R. Burgess
Manager, System Open
Market Account

Mr. John S. Sinclair, President,
Federal Reserve Bank of Philadelphia,
Philadelphia, Penn.

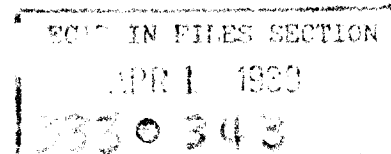
Encl.

REALLOCATION OF UNITED STATES GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON APRIL 1, 1938
 EARNINGS ON UNITED STATES GOVERNMENT SECURITIES COMPUTED AT 1.3987% PER ANNUM.
 (Amounts in thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Richmond	Atlanta	Chicago	St. Louis	Minne- apolis	Kansas City	Dallas	San Francisco
"A" - Expenses													
1. Estimated for 1938	29,215	2,154	7,527	2,475	2,778	1,768	1,342	3,248	1,426	1,095	1,664	1,190	2,548
2. Prior service con- tributions	2,521	179	639	193	220	157	94	333	145	83	171	109	198
3. Total	31,736	2,333	8,166	2,668	2,998	1,925	1,436	3,581	1,571	1,178	1,835	1,299	2,746
B" - Earnings													
1. Estimated January to Dec. (except on Gov'ts)	1,989	162	438	310	139	154	64	233	41	53	191	77	127
2. Earnings on Gov'ts. Jan-Feb.	6,288	462	1,813	519	620	334	264	693	281	204	324	245	529
3. Estimated March earnings on Gov'ts	3,085	226	890	255	304	164	129	340	138	100	159	120	260
4. Profits on Gov'ts. Jan-March 23	2,818	202	785	238	278	149	121	319	131	96	142	111	246
5. Total	14,180	1,052	3,926	1,322	1,341	801	578	1,585	591	453	816	553	1,162
"C" - Excess of "A"(3) over "B"(5)	17,556	1,281	4,240	1,346	1,657	1,124	858	1,996	980	725	1,019	746	1,584
"D" - Gov'ts required (on basis of 1.3987% earnings rate) to produce earnings April - Dec. equal to "C"	1,665,971	121,560	402,353	127,728	157,240	106,662	81,420	189,410	92,997	68,799	96,698	70,791	150,313
"E" - Ratio of dividend require- ments of each bank to System total	100%	7.06%	38.25%	9.22%	9.87%	3.71%	3.34%	9.78%	2.92%	2.18%	3.11%	2.95%	7.61%
"F" - Allocation of remainder of System holdings (\$2,564,015,000 less \$1,665,971,000) on basis of "E"	898,044	63,402	343,502	82,800	88,637	33,317	29,995	87,829	26,223	19,577	27,929	26,492	68,341
"G" - Total allocation of Gov'ts ("D" & "F")	2,564,015	184,962	745,855	210,528	245,877	139,979	111,415	277,239	119,220	88,376	124,627	97,283	218,654
"H" - Present allocations	2,564,015	188,239	739,554	211,610	253,038	136,297	107,460	282,390	114,478	83,246	132,104	99,767	215,832
"I" - Change in allocation	—	-3,277	+6,301	-1,082	-7,161	+3,682	+3,955	-5,151	+4,742	+5,130	-7,477	-2,484	+2,822

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March 25, 1938

Dr. W. R. Burgess, Vice President,
 Federal Reserve Bank of New York,
 New York, N. Y.

Dear Dr. Burgess:

There is inclosed a statement prepared from available information with respect to the estimated earnings and expenses of each Federal Reserve bank for 1938 and the changes in allocations as of April 1 necessary in the System account on the basis of these estimates. In estimating expenses and earnings, other than those on United States Government securities, we have used as a basis figures for the five months, October, 1937, to February, 1938, inclusive.

Since active consideration is being given to possible legislation with respect to making credit available to small industries, it is not believed desirable to make any change at this time with respect to the handling of earnings and expenses on industrial advances and commitments in determining participations in the System Account, reference to which was made in my letter of December 23, 1937.

Very truly yours,

E. L. Smead, Chief,
 Division of Bank Operations.

Inclosure

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*May. photostated
his statement to
send to other 2 eds.
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not after 5/1/38*

REALLOCATION OF UNITED STATES GOVERNMENT SECURITIES IN SYSTEM OPEN MARKET ACCOUNT ON APRIL 1, 1938
EARNINGS ON UNITED STATES GOVERNMENT SECURITIES COMPUTED AT 1.3987% PER ANNUM.
(Amounts in thousands of dollars)

	System	Boston	New York	Phila- delphia	Cleve- land	Richmond	Atlanta	Chicago	St. Louis	Winne- apolis	Kansas City	Dallas	San Francisco
"A" - Expenses													
1. Estimated for 1938	29,215	2,154	7,527	2,475	2,778	1,768	1,342	3,248	1,426	1,095	1,664	1,190	2,548
2. Prior service con- tributions	2,521	179	639	193	220	157	94	333	145	83	171	109	198
3. Total	31,736	2,333	8,166	2,668	2,998	1,925	1,436	3,581	1,571	1,178	1,835	1,299	2,746
"B" - Earnings													
1. Estimated January to Dec. (except on Gov'ts)	1,989	162	438	310	139	154	64	233	41	53	191	77	127
2. Earnings on Gov'ts. Jan-Feb.	6,288	462	1,813	519	620	334	264	693	281	204	324	245	529
3. Estimated March earnings on Gov'ts	3,085	226	890	255	304	164	129	340	138	100	159	120	260
4. Profits on Gov'ts. Jan-March 23	2,818	202	785	238	278	149	121	319	131	96	142	111	246
5. Total	14,180	1,052	3,926	1,322	1,341	801	578	1,585	591	453	816	553	1,162
"C" - Excess of "A"(3) over "B"(5)	17,556	1,281	4,240	1,346	1,657	1,124	858	1,996	980	725	1,019	746	1,584
"D" - Gov'ts required (on basis of 1.3987% earnings rate) to produce earnings April - Dec. equal to "C"	1,665,971	121,560	402,353	127,728	157,240	106,662	81,420	189,410	92,997	68,799	96,698	70,791	150,313
"E" - Ratio of dividend require- ments of each bank to System total	100%	7.06%	38.25%	9.22%	9.87%	3.71%	3.34%	9.78%	2.92%	2.18%	3.11%	2.95%	7.61%
"F" - Allocation of remainder of System holdings (\$2,564,015,000 less \$1,665,971,000) on basis of "E"	898,044	63,402	343,502	82,800	88,637	33,317	29,995	87,829	26,223	19,577	27,929	26,492	68,341
"G" - Total allocation of Gov'ts ("D" & "F")	2,564,015	184,962	745,855	210,528	245,877	139,979	111,415	277,239	119,220	88,376	124,627	97,283	218,654
"H" - Present allocations	2,564,015	188,239	739,554	211,610	253,038	136,297	107,460	282,390	114,478	83,246	132,104	99,767	215,832
"I" - Change in allocation	-	-3,277	+6,301	-1,082	-7,161	+3,682	+3,955	-5,151	+4,742	+5,130	-7,477	-2,484	+2,822

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P. & B.

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Inasmuch
I have not
the figure "5"
is omitted after
under "B"
Cm

Mr. Morris
This is the
letter and
statement I
just spoke to
you about.
LJ

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REC'D IN FILES SECTION
 MAR 31 1938
 333 • 343
 MAR 11, 1938

Mr. Smead

Messrs. Van Fossan and Daniels

Reference is made to your memorandum of January 14, 1938, to Mr. Van Fossan, requesting that we give consideration to questions referred to in letters from Mr. Leach, Mr. Sinclair, and Mr. Peyton on the formula to be used for reallocations of the System Account. The Presidents of the Federal Reserve banks were requested in Mr. Morrill's letter of December 6, 1937, to submit their views regarding the proposed formula to be used in making reallocations. In their replies three of the Federal Reserve banks made suggestions as follows:

Philadelphia

That the amount payable to the Secretary of the Treasury under Section 13b be included in the ordinary charge-offs in arriving at the expenses for formula purposes.

Richmond

- a. That the net debit or credit of profit and loss, except losses on bills and securities and miscellaneous assets, be used in arriving at item "C" in the formula, and
- b. That earnings, expenses and losses on industrial loans be excluded from the formula.

Minneapolis

That the formula include (1) provision for recognized losses or reserves for recognized losses and interest accrued to the Secretary of the Treasury for funds advanced for industrial loans and (2) recoveries on charge-offs, and exclude profits or losses on System Account sales.

The case for excluding earnings and expenses of 13b operations has been covered in Mr. Van Fossan's memorandum of December 15, 1937, and it is recommended that this be done. Aside from suggestions relating to adjustments in the formula because of industrial loan operations there were only two suggestions made -

FOR FILES
 I. B. Smith

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Mr. Smead - 2

1. That all profit and loss items be included in the estimates except year-end losses on bills and securities and miscellaneous assets, and
2. That profits and losses on Government securities be excluded.

Consideration has been given at various times to including estimates of profit and loss items in making the reallocations. The basis used for the reallocation on June 1, 1936, gave consideration to estimated "normal charge-offs and fixed charges" and in arriving at the September 30, 1936, allocations net expense of other real estate was included in the estimates. During 1937 the basis used for the reallocations gave consideration to prior service contributions, net profits on sales of securities and assessments for the Board's building.

Theoretically, the case is clear for considering all profit and loss items, except those relating to 13b operations, in arriving at the estimates of net earnings required by the various Federal Reserve banks. It is believed, however, that as a matter of practice no benefit would result from doing so. In the first place such items are difficult to estimate. Secondly, excluding prior service contributions, net profits on sales of securities, and assessments for the Board's building, profit and loss items have been and will probably continue to be relatively small, and in addition the credit and debit items tend to offset one another. During 1937, excluding the three profit and loss items which were considered in the reallocations, the net debit for the System of profit and loss items was less than 1/2% of current expenses, and the only individual banks having a net debit or net credit greater than 5% of current expenses were Chicago, because of the large credits for releases from prior service contributions and Board building assessment reserves, and Atlanta, because of the large reserve set up at the end of the year for building improvements.

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Mr. Smead - 3

The Minneapolis suggestion that profits or losses on Government securities be excluded from the estimates of net earnings on grounds that they are capital items is believed to have little merit either for the purpose under discussion or as a matter of accounting.

In connection with the consideration which is being given to establishing some limit to the amount of reserves for contingencies which a reserve bank may set up, it may be said that as long as reallocations of the System Account are made to provide earnings sufficient to cover a bank's expenses, the establishment of a limit for reserves for contingencies is perhaps an unnecessary refinement. That is, any bank upon which a relatively large assessment for Board expenses is levied because its reserves for contingencies are low as compared to other banks would, other things being equal, benefit through receiving a larger participation in the System Account. The only measure that can be taken to really solve the problem would have as their objective not the limiting of reserves for contingencies but the distribution of net earnings in excess of dividend requirements so as to tend to equalize the total of Surplus (Sec. 7) plus reserves for contingencies in comparison with paid-in capital.

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Form F. E. 131

Daniels ✓
see memo about this
where from it is
BOARD OF GOVERNORS
THE
FEDERAL RESERVE SYSTEM

Office Correspondence

To Mr. Van Fossan ✓
From Mr. Smead

Subject:

RECORDED IN FILES SECTION
January 14, 1938
MAR 31 1938
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Carded

In connection with letters to Mr. Leach, Mr. Sinclair, and Mr. Peyton regarding allocations of participations in the System Open Market Account, I would appreciate it if you and Mr. Daniels will give the questions referred to in these letters prompt consideration and give me your views thereon.

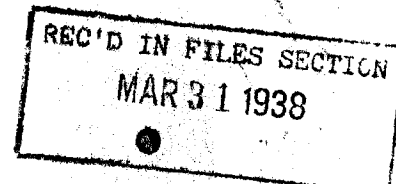
I think it would also be helpful if we prepared a memorandum promptly on relationships between surplus accounts and contingent reserves, as requested by the Board.

FOR FILES
J. B. Smith

see memo 3/11/38

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January 14, 1938

Mr. Hugh Leach, President,
 Federal Reserve Bank of Richmond,
 Richmond, Virginia

Dear Mr. Leach:

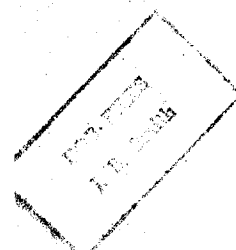
Reference is made to your letter of December 21 in regard to the proposed formula for determining allocations in the System Open Market Account beginning January 1, 1938.

Mr. Smead discussed with you over the telephone the reasons for and against taking into consideration income, expenses, losses, and payments to the Secretary of the Treasury in connection with industrial advances and commitments in determining participations of the various Federal Reserve banks in the System Account. While it was agreed to make no change in the procedure at this time, it is understood that the matter will be thoroughly reviewed and should industrial advances and commitments outstanding continue to decline, it will probably be advisable to disregard all income, expenses, losses, and payments to the Secretary of the Treasury in connection with industrial advances and commitments in determining participations in the System Account as of April 1, 1938.

Your suggestion that it might be desirable to amend the formula so as to take into account the net debit, or net credit, in the current profit and loss account is noted and will receive careful consideration before the next reallocation.

Very truly yours,

Chester Morrill, Secretary,
 Federal Open Market Committee.



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MAR 31 1938

January 14, 1938

Mr. J. S. Sinclair, President,
Federal Reserve Bank of Philadelphia,
Philadelphia, Pennsylvania

Dear Mr. Sinclair:

Reference is made to your letter of December 18 in regard to the proposed formula for determining allocations in the System Open Market Account beginning January 1, 1938.

Mr. Smead discussed with you over the telephone the reasons for and against taking into consideration income, expenses, losses, and payments to the Secretary of the Treasury in connection with industrial advances and commitments in determining participations of the various Federal Reserve banks in the System Account. While it was agreed to make no change in the procedure at this time, it is understood that the matter will be thoroughly reviewed and should industrial advances and commitments outstanding continue to decline, it will probably be advisable to disregard all income, expenses, losses, and payments to the Secretary of the Treasury in connection with industrial advances and commitments in determining participations in the System Account as of April 1, 1938.

Very truly yours,


Chester Morrill, Secretary,
Federal Open Market Committee.

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January 14, 1938

Mr. J. M. Peyton, President,
Federal Reserve Bank of Minneapolis,
Minneapolis, Minnesota

Dear Mr. Peyton:

Reference is made to your letter of December 14 in regard to the proposed procedure for handling transactions in the System Open Market Account beginning January 1, 1938.

It is noted that you suggest that the formula include provision for recognized losses or reserves for recognized losses and interest accrued to the Secretary of the Treasury for funds advanced for industrial loans, and that profits or losses on sales from the System Account be omitted.

In estimating earnings and expenses of the Federal Reserve banks for the purpose of allocating participations in the System Open Market Account it has been the practice to include all known and regularly recurring charges, but no attempt has been made to include special reserves or charge-offs which are made at the end of the year on the basis of the information then existing. Under this procedure all known profits and losses on sales of Government securities which affect all Federal Reserve banks in relatively the same proportion are included in the calculations. Careful consideration has been given from time to time to the desirability of including in the formula provision for losses and reserves for losses which it is customary for the banks to set up at the end of the year, but owing to the difficulties involved in such procedure and particularly in treating all banks alike, the decision has always been against its adoption. In the case of most banks, at least, what additional reserve will be needed is not determined until about the end of the year and, consequently, no provision can be made for such reserves in the figures used in determining participations in the System Account. Account could, of course, be taken of actual losses charged off, and further consideration will be given to your suggestions in this respect.

With respect to including provision for payments to the Secretary of the Treasury under Section 13b in determining participations in the System Account, it is, of course, impossible for us to tell in advance

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Mr. J. N. Peyton - #2

what reserves a Federal Reserve bank is likely to set aside at the end of the year on industrial advances, which largely determines what the payment to the Secretary of the Treasury will be and, accordingly, it would be impossible to make intelligent provision for such payments in our calculations. It is quite probable, however, that approximately the same results as those you have in mind could be obtained by leaving out of the net earnings calculation all income, expenses, losses, and payments to the Secretary of the Treasury in connection with industrial advances and commitments. If industrial advances and commitments continue to decline, it is quite probable that better results will be obtained if such income, expenses, losses, and payments are omitted from the estimates used in determining participations in the System Account. This matter will receive careful consideration and it is expected that a decision with respect thereto will be reached before April 1, 1938, the time of the next reallocation of participations in the System Account.

Very truly yours,



Chester Morrill, Secretary,
Federal Open Market Committee.

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January 4, 1938.
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Dr. W. R. Burgess, Vice President
Federal Reserve Bank of New York
New York, New York

Dear Dr. Burgess:

In connection with our telephone conversation with respect to reallocation of participations in the System Open Market Account, there are inclosed copies of the letters we received from the Federal Reserve Banks of Philadelphia, Richmond, and Minneapolis, and a copy of the letters we have drafted with respect to the suggestions contained therein. It will be appreciated if you will go over these letters and make any changes in them which you think advisable.

Dr. Burgess says the proposed changes are O.K. En

From

No suggestions for changes in the formula were made by any other Federal Reserve banks and, accordingly, it is not necessary for the secretary of the committee to address letters to them at this time.

Sincerely yours,

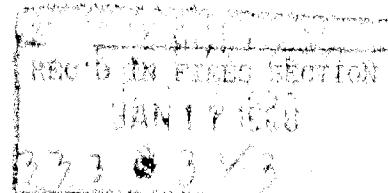
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E. L. Sneed, Chief,
Division of Bank Operations.

Inclosures.

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FEDERAL RESERVE BANK OF PHILADELPHIA

C
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President

December 18, 1937

Dear Mr. Morrill:

I reviewed yesterday with our Board of Directors the proposed procedure for handling transactions in the System Open Market Account beginning January 1, 1938. Our Board has noted its acquiescence in the proposed procedure and reallocation, reserving the right, at a later date, if deemed advisable, to raise such questions as may be deemed necessary or advisable in the premises. It is generally our thought that the plan for allocation is as fair and equitable as can be devised under the present circumstances.

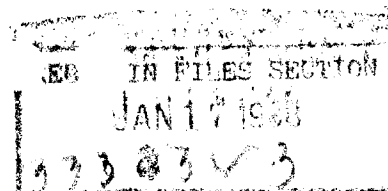
We have noted that the amounts payable to the Secretary of the Treasury under the provisions of Section 13b have not been included in the ordinary charge-offs in arriving at the expenses for formula purposes. It may be that Dr. Burgess and Mr. Smead have considered this question and have determined that it is unwise to include such payments.

Very truly yours,

(Signed) John S. Sinclair

Mr. Chester Morrill, Secretary
Federal Open Market Committee
Board of Governors of the
Federal Reserve System
Washington, D. C.

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FEDERAL RESERVE BANK
 OF RICHMOND

December 21, 1937.

Mr. Chester Morrill, Secretary,
 Federal Open Market Committee,
 Care of Board of Governors
 of the Federal Reserve System,
 Washington, D. C.

Dear Mr. Morrill:

We have read with much interest your letter of December 6, and enclosures, with respect to securities held in the System Open Market Account.

The new procedure for allocating profits and losses on transactions in the account is entirely satisfactory to us and is believed to be an improvement over the old method.

It seems to us that the formula given on page 3 of the proposed accounting procedure might be stated more completely as follows:

A. Expenses and other deductions from earnings --

1. Current expenses to date of allocation.
2. Estimated current expenses for remainder of year.
3. Net debit-Current Profit and Loss account to date of allocation.
4. Prior service contributions for remainder of year.
5. Total.

B. Earnings and additions to earnings --

1. Current earnings to date of allocation.
2. Estimated for remainder of year (exclusive of earnings on Governments).
3. Net credit-Current Profit and Loss account to date of allocation.
4. Total.

The current profit and loss account includes prior service contributions to the date of allocation, as well as profits and losses on sales of securities. It also includes other miscellaneous profits and losses which are not provided for in the Committee's formula. The formula as given above would take into account all earnings, additions to earnings, expenses and charge-offs, except losses on bills and securities (including industrial advances) and miscellaneous assets, which losses are estimated and charged off at the end of the year.

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Mr. Chester Morrill, Secretary,
Federal Open Market Committee,
Washington, D. C.

-2-

December 21, 1937.

The formula which was used in the past included earnings and expenses on industrial loans but did not take into account losses on industrial loans or payments to the Treasury on account of earnings on industrial loans. This was not entirely equitable. The Federal Reserve Bank of Richmond, for instance, had net earnings on industrial loans of \$154,000 for 1936 and \$95,000 for 1937, but also had estimated losses on industrial loans amounting to \$212,000 for 1936 and \$113,000 for 1937.

The new formula is similar to the old formula in so far as industrial loans are concerned. The situation has changed during the last year or two, however, in that the 13b surplus of about half of the Reserve banks now appears to be larger than the combined total of outstanding loans and commitments and the 13b surplus of the remaining banks (with the exception of San Francisco) seems to vary from around 60% to 95% of outstanding loans and commitments. This means, according to the System's interpretation, that most of the funds now invested in industrial loans were received from the Treasury and that future earnings, expenses, and losses on industrial loans will have no effect on the surplus (section 7) accounts of about half of the Reserve banks and little effect on surplus (section 7) accounts of the remaining banks. If this is the proper interpretation of our arrangement with the Treasury, it would seem logical to omit earnings, expenses, and losses on industrial loans from the formula.

On the other hand, we do not know what the final outcome of the System's conferences with the Treasury about losses, earnings, uninvested fund, etc., will be, and have no way of ascertaining from information at our disposal whether the omission from or inclusion in the formula of earnings, expenses, and losses on industrial loans would make any appreciable difference in allotments of Government securities to the various Federal Reserve banks.

Very truly yours,

(Signed) Hugh Leach
President.

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YFEDERAL RESERVE BANK
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December 14, 1937.
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Mr. Chester Morrill, Secretary,
Board of Governors of the
Federal Reserve System,
Washington, D. C.

Dear Mr. Morrill:

Under date of December 6, 1937, you submit "Proposed Accounting Procedure for Handling Transactions in System Open Market Account Beginning January 1, 1938", and request that we review it and advise you of any views we might like to have considered before the procedure recommended in the report is put into effect.

On Page 3 you state that adjustments and participations of the several Federal reserve banks in the System Open Market Account will be made quarterly as of January 1, April 1, July 1, and October 1 of each year, in accordance with the following formula:

"Expenses:

1. Estimated current expenses during the year
2. Prior service contributions
3. Total"

As used by our auditors and as defined by the Board "Estimated current expenses during the year" would include no losses. Would it not be fairer to word this "Estimated current expenses during the year after including provision for recognized losses or reserves for recognized losses and interest accrued to the Secretary of the Treasury for funds advanced for industrial loans", leaving out profits or losses on System Account sales. As an offset, recoveries on charge-offs should be included in the earnings for that year.

On Page 3, under Earnings, "Net profit on governments sold to date" set up as an addition to earnings does not seem to us as sound. We believe that all principal profits or losses accrued from the purchase or sale of System Account bonds should be credited or charged directly to reserve account or surplus account so the yearly earnings of a Federal reserve bank would not be affected by either principal profits or losses. Capital losses of this character should be absorbed by reserves, surplus, or capital. If profits from the System Account are to be considered in figuring the yearly profit, then losses from the sale of assets from the System Account should logically be considered expenses, yet such is not the procedure outlined.

Very truly yours,

(Signed) J. N. Payton

PRESIDENT

JNP:B