

FEDERAL RESERVE BOARD

WASHINGTON

April 26, 1915.

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The Federal Reserve Agent of the Federal Reserve Bank of San Francisco, has transmitted by wire the following inquiry which has been referred to this office for an opinion.

"Please advise whether United States two per cent bonds we now own, and additional amounts we may buy, may be counted as part of our pro rata of twenty-five million annually purchased authorized by the Act."

The provisions of the Act to which he refers are contained in Section 18 and the language to be considered in connection with this inquiry is as follows -

"After two years from the passage of this Act, and at any time during a period of twenty years thereafter, any member bank desiring to retire the whole or any part of its circulating notes, may file with the Treasurer of the United States an application to sell for its account, at par and accrued interest, United States bonds securing circulation to be retired.

The Treasurer shall, at the end of each quarterly period, furnish the Federal Reserve Board with a list of such applications, and the Federal Reserve Board may, in its discretion, require the Federal Reserve banks to purchase such bonds from the banks whose applications have been filed with the Treasurer at least ten days before the end of any quarterly period at which the Federal Reserve Board may direct the purchase to be made. PROVIDED, That reserve banks shall not be permitted to purchase an amount to exceed \$25,000,000 of such bonds in any one year, and which amount shall include bonds acquired under section four of this Act by the Federal reserve bank.

PROVIDED FURTHER, That the Federal Reserve Board shall allot to each Federal reserve bank such proportion of such bonds as the capital and surplus of such bank shall bear to the aggregate capital and surplus of all the Federal reserve banks".

It will be observed from the foregoing that the twelve Federal reserve banks "shall not be permitted to purchase an amount to exceed \$25,000,000 of such bonds in any one year".

The bonds to which limitation applies are those which are offered for sale by member banks through the Treasurer of the United States and against which circulating notes are outstanding which the member bank desires to retire.

Prior to the passage of this Act national banks were permitted to retire circulating notes not to exceed nine million dollars in any one month. This provision furnishes another method by which member banks may retire not to exceed twenty-five million dollars annually of their circulation by sale of bonds through the Treasurer of the United States to the Federal reserve banks.

The power to purchase these bonds from the Treasurer, which purchase may be required by the Federal Reserve Board, should not be confused with the general power of Federal reserve banks to purchase and deal in United States bonds in the open market.

Under the plan devised the Treasurer at the end of each quarterly period reports to the Board all applications which have been filed with him ten days before the end of such period. The Board thereupon allots to each Federal reserve bank its proportion of the bonds which it requires such banks to purchase. When this allotment is made, if any of the Federal reserve banks have purchased in the open market bonds bearing the circulating privilege during the year in which such allotment is made, such Federal reserve bank may claim credit for bonds so purchased and is permitted, under the Federal Reserve Act, to accept only its allotment less the amount of bonds purchased in the open market. Manifestly if this amount exceeds the amount of its allotment it cannot purchase any of such bonds. In order, however, to claim such credit the bonds purchased in the open market must have been purchased during the year in which the allotment is made and bonds acquired prior to the beginning of that year will not entitle the Federal reserve bank to any credit on its allotment.

Inasmuch, therefore, as the first fiscal year during which allotments may be made cannot, under the terms of the Act, begin prior to December 23, 1915, that

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is to say, two years from the date of the passage of the Act, the bonds acquired by Federal reserve banks prior to that date cannot be deducted from the amount allotted to any Federal reserve bank after this date

Respectfully,

(Signed) H. C. ELLIOTT,

Counsel.

Honorable F A. Delano,
Vice Governor.