

FEDERAL RESERVE BOARD
WASHINGTON

June 25, 1915.

My dear Governor:

The following inquiry submitted by one of the Federal reserve banks has been referred to this office for an opinion.

"If able are we expected to declare a dividend as of June 30th at 6% per annum for the time elapsed between November 16th, 1914 and June 30th, 1915, or are we to understand that Section 7 of the Act requires that the dividend distribution be made only annually or at the close of 1915? If the latter be the case, what action would be appropriate as of the close of June in caring for such entries as usually find their way into Profit & Loss account? Shall we close our books under such instructions as you may give us and continue an "Undivided Profit" account until the close of the year, or would you have us make a dividend, take proper care of expenses, and set aside one-half of remaining earnings and cover the second half into the Treasury of the United States?"

Section 7 provides that -

"After all necessary expenses of a Federal reserve bank have been paid or provided for, the stockholders shall be entitled to receive an annual dividend of six per centum on the paid-in capital stock, which dividend shall be cumulative. After the aforesaid dividend claims have been fully met, all the net earnings shall be paid to the United States as a franchise tax, except that one-half of such net earnings shall be paid into a surplus fund until it shall amount to forty per centum of the paid-in capital stock of such bank".

It appears from this that Congress intended that dividends should be paid annually and not in semi-annual instalments. It is conceivable that a bank might show a surplus as the result of the first six months' operations and a loss for the last six months. If, therefore, a dividend should be declared at the end of six months, an im-

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payment of capital might be shown according to the books at the end of the year which would not have resulted except for the payment of the dividend.

After the dividend has been paid and the required amount has been carried to the surplus account, the balance of earnings resulting from the year's operations is payable to the United States as a franchise tax. The amount of this tax can not be determined until the end of the year. Banks should, therefore, carry all net earnings in the account of Undivided Profits until the end of the fiscal year and should then declare a dividend, and the balance, if any, should be paid half to the United States as a franchise tax and half into the surplus fund, as provided by Section 7.

When the banks have been in operation for a sufficient length of time to enable them to estimate approximately their annual earnings and expenses, the Board might, in case the Undivided Profit Account shows a sufficient amount to cover all contingencies, authorize the payment of the dividend in semi-annual instalments, but until that time the letter of the statute should be followed strictly in order to avoid probable complications.

Respectfully,

M. C. ELLIOTT,

Counsel.

Hon. C. S. Hamlin,
Governor.