

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

X-9607

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD



June 4, 1936.

SUBJECT: Basis of Issuance of Federal
Reserve Bank Stock.

Dear Sir:

There is inclosed for your information and guidance, in the event that cases involving similar circumstances come to your attention, a copy of a letter to the Assistant Federal Reserve Agent at the Federal Reserve Bank of Kansas City regarding the basis of subscriptions to Federal Reserve bank stock.

Very truly yours,

Chester Morrill,
Secretary.

Inclosure.

TO ALL FEDERAL RESERVE AGENTS EXCEPT KANSAS CITY.

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June 4, 1936.

Mr. A. M. McAdams,
Assistant Federal Reserve Agent,
Federal Reserve Bank of Kansas City,
Kansas City, Missouri.

Dear Mr. McAdams:

Reference is made to your letter of April 29, in which you refer to the Board's letter X-9324 of September 20, 1935, and inquire whether, in the circumstances described in your letter, it will be satisfactory to defer adjustments of Federal Reserve bank stock holdings of member banks when it appears that an existing impairment in the book surplus account (by reason of a deficit in the undivided profits account) will be eliminated within a reasonably short period.

It is noted that in the case in question the member bank holds Federal Reserve stock issued on a basis of \$100,000 capital and \$12,500 surplus; that the December 31, 1935, and March 4, 1936, call reports showed net surplus of \$5,234.92 and \$7,737.08, respectively; that the bank has advised you that its net surplus account has been increased to \$9,328.64 and that it anticipates that the book surplus of \$12,500 will show no impairment by June 30, 1936; and that the bank has inquired whether, in view of the circumstances, an immediate adjustment of Federal Reserve bank stock holdings is necessary.

It is also noted that you feel that it would be better from a practical standpoint to base the Federal Reserve bank stock holdings on the amount of book capital and surplus, with a possible exception in cases in which a deficit in the undivided profits account is greater

than the amount of book surplus, on the theory that any impairment in the book surplus account is a purely temporary condition which, unless corrected promptly through the accumulation of earnings, profits, or recoveries, will be corrected by a reduction in the amount of surplus shown by the books. This suggestion is in harmony with the ruling contained in the Board's letter X-7459 of June 19, 1933, that, while any impairment in a member bank's capital stock or surplus should be corrected as soon as possible, its holdings of Federal Reserve bank stock should be based upon the amount of issued and outstanding capital stock and surplus as shown on its books, rather than upon unimpaired capital and surplus. That ruling was somewhat modified by the Board's letter X-9324 primarily to avoid the issuance of any Federal Reserve bank stock against book surplus in cases where the book surplus was less than the deficit in the undivided profits account. To be consistent, letter X-9324 also provided that, if a bank shows a deficit in its undivided profits account not in excess of the amount of surplus shown by its books, the deficit should be deducted from the book surplus in determining the basis for required Federal Reserve bank stock holdings.

The Board feels that, if a bank has a deficit in its undivided profits account, the ruling contained in letter X-9324 should continue to be observed. If, however, the deficit in the undivided profits account is relatively small and the Federal Reserve bank is satisfied that it is likely to be extinguished either by accumulation of earnings

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or by a formal reduction in surplus, there is no objection to deferring the adjustment of Federal Reserve bank stock holdings until the end of the current semi-annual period. As you know, the procedure outlined in paragraph number 6 of the Board's letter X-9371 of November 26, 1935, contemplates that as a general rule semi-annual adjustments in holdings of Federal Reserve bank stock will be sufficient.

Very truly yours,

(Signed) Chester Morrill

Chester Morrill,
Secretary.