

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

X-9791
Sec. 5136 R.S.-8

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

January 12, 1937.



Dear Sir:

There is inclosed herewith for your information a copy of a letter dated December 11, 1936, from the Federal Reserve Bank of Richmond requesting a ruling upon the question whether, under the provisions of section 5136 of the Revised Statutes and the Comptroller's regulations governing investment securities, a State member bank may repurchase non-conforming securities which it had lawfully owned prior to February 15, 1936, but which it had sold subsequent to that date in order to establish a loss for income tax purposes.

This question was presented by the Board of Governors to the Comptroller of the Currency for an expression of his views thereon, and a copy of the Comptroller's letter dated December 29, 1936, is inclosed herewith.

Very truly yours,

A handwritten signature in dark ink, appearing to read "L. P. Bethea". The signature is fluid and cursive, with a long horizontal stroke extending to the right.

L. P. Bethea,
Assistant Secretary.

Inclosures.

TO PRESIDENTS OF ALL FEDERAL RESERVE BANKS

X-9791-a

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FEDERAL RESERVE BANK
OF RICHMOND

December 11, 1936.

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

Gentlemen:

Reference is made to report of examination of _____ Bank, _____, _____, as of October 13, 1936, in which criticism is made of purchases of certain securities that do not conform to the provisions of Section 5136 of the Revised Statutes and the regulation of the Comptroller of the Currency issued pursuant thereto.

The transactions are set forth on the attached memorandum copies from supplemental sheet 12-15 of the report. It is to be noted that these securities in like denominations were lawfully held by the bank prior to February 15, 1936, the date of the Comptroller's regulation, but were sold subsequent to that date. When repurchased, the securities were entered on the books in the same amounts at which they were carried at the dates of sales.

We are in receipt of a report submitted to the President and Board of Directors of the bank by a committee appointed to review and study the report of examination. Concerning the criticism with respect to the purchases of non-conforming securities, the committee had the following to say:

"Relative to the violation of Paragraph 19, Section 9 of the Federal Reserve Act, we find that the bank sold the securities in question for but one purpose only, namely to establish a loss for income tax purposes; that it repurchased a like amount of exactly the same securities, and put them on the bank's books at exactly the same price that they were formerly carried; that the Committee does not feel that this action is in any way a violation of the Act. The bank's reason for repurchasing these securities after establishing a loss was due to the fact that they did not desire to have them taken out of their portfolio, believing that these securities would appreciate in the future."

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Mr. _____, Vice President, visited us recently for the purpose of discussing some of the affairs of his bank, among which was the subject referred to above. He requested that we obtain a ruling on this question from the Board of Governors of the Federal Reserve System.

The matter has been referred to our Counsel and he is definitely of the opinion that the purchases of the securities referred to in the report constituted violations of Section 5136 of the Revised Statutes. We shall appreciate an expression from the Board as to whether or not it concurs in our Counsel's opinion.

Yours very truly,

/s/ J. G. Fry

J. G. Fry,
Vice President.

Inclosure

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The following bonds purchased after February 15, 1936 appeared to be 'distinctly or predominantly speculative' and, therefore, lacking the quality of 'investment securities' are non-conforming. The purchase of securities, which are in default either as to principal or interest, is also prohibited.

5 M Lehigh Valley R. R. 4-1/2's - 2003	Purchased 8-10-36
5 M Chic. Mil. St. Paul & Pac. Rwy. 5's - 1975	Purchased 9-9-36
20 M Chic. Mil. St. Paul & Pac. Rwy. Conv. Adj. 5's - 2000	Purchased 9-10-36
5 M Norfolk-Southern R.R. 5's - 1961	2 M purchased 8-5-36 3 M " 8-10-36
25 M S. A. L. Rwy. Stamped 4's - 1950	Purchased 8-25-36
4 M Baltimore Transit A 5's - 1975	Purchased 8-14-36
17 500 Consolidation Coal Co. 5's - 1960	Purchased 8-26-36 thru 9-14-36

Stocks acquired contrary to the provisions of Section 9 of the Federal Reserve Act.

40 shares Baltimore Transit Co. pfd	Purchased 8-14-36
315 shares Consolidation Coal Co.	Purchased 8-26-36
105 shares Consolidation Coal Co. pfd	Purchased 8-26-36

Like amounts of the above securities were held by the bank prior to February 15, 1936, but were sold subsequently to this date.

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TREASURY DEPARTMENT
COMPTROLLER OF THE CURRENCY
WASHINGTON

December 29, 1936

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

Gentlemen:

This acknowledges your letter of December 21, 1936, with enclosure from the Federal Reserve Bank of Richmond, requesting a ruling upon the question whether under the provisions of Section 5136 of the Revised Statutes and the Comptroller's Regulations regarding investment securities, a State member bank may repurchase non-conforming securities which it had lawfully owned prior to February 15, 1936, but which it had sold subsequent to that date in order to establish a loss for income tax purposes.

This office would consider such repurchase of non-conforming securities a prohibited purchase of securities in violation of the regulations of this office issued under date of February 15, 1936, pursuant to the provisions of Section 5136 of the Revised Statutes.

Very truly yours,
(Signed) J. F. T. O'Connor
J. F. T. O'CONNOR
Comptroller