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December 1, 1937

Secretary Hull called HM, Jr today and asked him to do nothing on Mexico on silver all of this month because they are having negotiations with Mexico. The Secretary said that he would sit tight and do nothing for this week.

December 1, 1937.
9:04 a.m.

H.M.Jr: Hello.

Operator: Mr. Jones.

H.M.Jr: Hello.
Jesse
Jones: Hello.

H.M.Jr: Good morning, Jesse.

J: Good morning.

H.M.Jr: Are you at home?

J: Yes.

H.M.Jr: Jesse, I want to take a minute or two to explain what I've been working on very quietly, for the President, see.

J: All right.

H.M.Jr: And I asked him - we talked about it, whether somebody couldn't work on cotton with the idea that eighteen million bales of cotton is a good thing, and let's see whether we can't do something to get rid of it.

J: Yes.

H.M.Jr: Rather than just sit around and tell tales of woe, see?

J: Yes.

H.M.Jr: Well, I've been working on this thing quietly for a couple of weeks, and we finally evolved an idea of a national advertising campaign in conjunction with the industry, and we work through the textile industry, and they're tremendously enthusiastic about it and ready to put up some money, see.

J: Who?

H.M.Jr: The textile industry.

J: Yes.

H.M.Jr: Through the cotton institute.

J: Yes.

H.M.Jr: You know. Well, we've got the thing and I first thought we could do the Section 32 money, but Wallace doesn't like it that way, so we looked up and we - Oliphant's given us the opinion we can do it through Commodity Credit.

J: Yes.

H.M.Jr: And yesterday afternoon we put it up before the Comptroller General and he said he'd O.K. it. Now I just walked down with Wallace and he's far enough long that he said he'd like to meet with you and me, and talk this thing over, see.

J: Yes.

H.M.Jr: Now would lunch tomorrow be convenient? And if you'd like - I'd like you to get more details so you can have a chance to think about it. I'd like Wayne Taylor to come over and talk to you at your convenience, he's all full of it.

J: Well, suppose - suppose he do that today, and what time - how early could we have lunch?

H.M.Jr: Well, we'll fix it - are you going to leave town?

J: I was going to leave town. I am - I am going to leave town tomorrow afternoon.

H.M.Jr: Well -

J: I was going today, but Wagner wants me to come up there and get before his committee on the Housing thing in the morning.

H.M.Jr: Well, do you want to make it quarter of one?

J: Yes, well - well that'll be all right, and if we get through - I might take a two o'clock train or at least a three.

H.M.Jr: Oh, yes. Now, supposing I have Wayne contact you, see.

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J: All right.

H.M.Jr: And give you the thing - so as you won't get this thing cold.

J: All right.

H.M.Jr: And - I mean - I'm quite enthusiastic about it.

J: Well, I hope - I hope that I agree with you.

H.M.Jr: Well, I don't know, but -

J: I say I hope I do, and I -

H.M.Jr: I want to give you twenty four hours to think about it.

J: Well, I've got to go to the Hill at ten-thirty to testify on the House side
for the Housing bill.

H.M.Jr: Yes.

J: And so suppose I leave word, and maybe I can get it - I'll call Wayne and maybe I can get a lunch engagement with him today.

H.M.Jr: Yes, well shall I leave it that you'll call Wayne.

J: Yes. I'll call him right now.

H.M.Jr: You'll call him right now.

J: Yes.

H.M.Jr: Wayne doesn't know I called you, because I just got into the office.

J: Well, if you'll tell him -

H.M.Jr: Well, supposing I tell Wayne to call you right away.

J: Tell him to call me, and -

H.M.Jr: And I'll tell him what's it about.

J: Tell him to call me through the office.

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H.M.Jr: Through the office?
J: Yes.
H.M.Jr: Through the office.
J: My office, yes.
H.M.Jr: I'll do that.
J: Thank you.
H.M.Jr: He'll call you in two minutes.
J: All right. Fine.

December 1, 1937

9:15 a. m.

Present:

- Mr. Magill
- Mr. Oliphant
- Mr. Helvering
- Mr. Wenchel
- Mr. Russell
- Mr. Carter

HM, Jr: Who slipped this memorandum to me?

Mr. Magill: That's mine.

HM, Jr: Supposing I read this out loud.

(Read Magill's memorandum in full. It is attached, marked Exhibit I.)

Now, have you (Oliphant) got one?

Mr. Oliphant: Yes.

HM, Jr: (Reading Oliphant's memorandum.) (Exhibit II)

"I have discussed this matter today with Mr. Wenchel and we have examined our calendars. This is what happened:

"Wenchel began work in the Bureau September 22. Eight days later, on September 30 at 10 a.m., he sat in a conference on the Maestri case in Helvering's office with Helvering, Russell, Carter, Regis, May, Pierce and Norman, one of his lawyers. Wenchel did not then know that the Louisiana cases were the subject of special instructions because it had not been possible for me to tell him about all the special situations and unusual problems pending in his office and the Bureau."

May I check? September 30th. Those instructions had not been issued yet.

Mr. Oliphant: Oh, yes! Issued at the time Justice settled the criminal cases.

HM, Jr: Were they? Because the first they were brought to me was October 7th.

Mr. Wenchel: That was the conference in Secretary Magill's office.

HM, Jr: (Resumed reading)

"At this conference in Helvering's office, Wenchel, remembering and mentioning newspaper discussions of the Louisiana cases, asked if there was anything unusual about this Maestri case and was told that what he had in mind was the criminal cases, but that this was a case of settling civil liability. He then agreed that, the evidence on the various issues being what it was, the following proposal to settle was a good one:

Accept the taxpayer's claim as to the \$80,000 from the sale of stock. Cut the alleged gift of \$150,000 in half. Assess \$57,658.14 instead of \$100,000 "nest-egg" since \$42,341.86 had been assessed and taxes paid thereon in the year 1930.

"However, Wenchel did not get the impression that this conference was to conclude the matter because Helvering was insistent that no plan of settlement would be acceptable unless it involved the payment of at least the full tax. Wenchel says he did not know until this morning that the taxpayer's lawyer had been informed that the settlement was satisfactory."

HM, Jr: Same day of what?

Mr. Oliphant: Day of the conference.

Mr. Wenchel: September 30th.

(HM, Jr:) (Completed reading aloud Mr. Oliphant's memorandum of November 30th.)

HM, Jr: This is Oliphant's memorandum to Shafroth. (HM, Jr read aloud this memorandum dated September 1, attached marked Exhibit III.)

Now you have got your time table.

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Mr. Helvering: Do I understand that Mr. Oliphant says that no case shall be settled unless the taxpayer waives the issue? If he does, we might just as well close up shop.

HM, Jr.: Here is a copy of Oliphant's memorandum (to Shafroth.)

(Mr. Helvering read the memorandum.)

Mr. Oliphant: (to Mr. Helvering) Refer to the bottom of the memorandum -- where there is a conflict of evidence, the thing is to go to the Board.

Mr. Helvering: You confine it to the Louisiana cases?

Mr. Oliphant: Yes; that's all.

Mr. Magill: The idea as it developed in the October 7th conference was this: what was meant by horse-trading was whether or not you could arrive at a disposition of the issues either by the taxpayer agreeing he was wrong or the Bureau agreeing that it was wrong, but we were not to trade issues off against each other.

Mr. Helvering: Uh-huh.

HM, Jr.: This (Mr. Russell's memorandum) is not signed.

Mr. Russell: Oh! Glad to sign it. HM, Jr.: Do you mind dating it? Mr. R.: Let's see, today is December 1.

HM, Jr.: (Began reading Russell's memorandum of December 1, 1937. Attached, marked Exhibit IV)

"A thirty-day letter was issued in the above-mentioned case under date of September 16, 1936 covering the years 1925 to 1929, inclusive, disclosing deficiencies in tax of \$144,334.65 and penalties of \$72,167.33, a total of tax and penalty of \$216,501.98. In response to this letter, under date of January 18, 1937 the taxpayer called in person accompanied by Senator Allen J. Ellender and a discussion was had on that date with the following representatives of the Bureau :

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"J. W. Carter, Head Special Adjustment Division
George H. Reges, Jr., Conferee, Special Ad-
justment Division
Paul May, Auditor, Special Adjustment Division
C. O. Pierce, Auditor, Special Adjustment Di-
vision."

HM, Jr: Now, this is the first I knew that Maestri and Ellender called on Mr. Russell.

Mr. Helvering: He came to see me and I sent him up to see them.

HM, Jr: Up to September 9th nothing happened as far as you two gentlemen were concerned (Mr. Magill and Mr. Oliphant)?

Mr. Magill: The first I heard of the case was September 11th.

Mr. Russell: Except we advised Mr. Oliphant we were having a conference and he said that Mr. Wenchel should sit in on it.

Mr. Oliphant: I called Shafroth and told him of the conference and he said he hoped Irey would be present.

HM, Jr: (Resumed reading) "At the conclusion of this conference there was additional information or evidence which Mr. Wentworth desired to submit for consideration of the Bureau representatives. This information was received under date of September 25th. Under date of September 30, 1937 a conference was held in the Commissioner's office attended by Mr. Guy T. Helvering, Commissioner, Mr. Wenchel, Chief Counsel for the Bureau of Internal Revenue, C. T. Russell, Deputy Commissioner, Mr. Harold Norman, Special Attorney, Penal Division, Chief Counsel's Office, Mr. J. W. Carter, Head, Special Adjustment Division, Mr. George H. Reges, Jr., Conferee, Special Adjustment Division, Paul May, Auditor, Special Adjustment Division. At the above conference the following items were discussed:

- "1) The taxpayer's contention as to the \$100,000.00 on hand in 1910,
- (2) The taxpayer's contention as to the \$150,000.00 gift in 1916,
- (3) The taxpayer's contention as to the \$80,000.00, proceeds from the sale of stock in 1923,
- (4) The taxpayer's contention as to the \$103,413.57, proceeds from partition sale in 1927,
- (5) The taxpayer's contention as to the \$1000.00 and \$12,000.00 mortgage notes,
- (6) the taxpayer's contention as to the \$10,000.00 living expenses,
- (7) The taxpayer's contention as to the fraud penalties."

HM, Jr: This took place September 25th?

Mr. Russell: September 30th.

HM, Jr: Now, this is September 30th. (Resumed reading.)

"At this conference it was concluded that the taxpayer's contention on the \$100,000.00 on hand in 1910 should be denied; that the taxpayer's contention as to the \$80,000 proceeds received from the sale of stock in 1923 should be conceded; that the taxpayer's contention as to the \$103,413.57 proceeds from partition sale in 1927 should be conceded; that the taxpayer's contention as to the \$1000.00 and \$12,000.00 mortgage notes should be conceded; that the taxpayer's contention as to the fraud penalty should be denied and the taxpayer's contention as to the \$10,000. living expenses should be denied. This left only one item still in dispute; that is, the taxpayer's contention as to the \$150,000.00 gift in 1916. On this item it was the opinion of the Commissioner and Mr. Wenchel, Chief Counsel, that the full amount of this gift should not be conceded but it was their conclusion, based on the evidence in the case, that if the taxpayer would concede one-half of \$75,000.00 of this item that that would be a fair settlement."

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HM, Jr: Is that right?

Mr. Wenchel: Right.

HM, Jr: (Resumed reading)

"Under date of October 4, 1937 a hearing was held in the Internal Revenue Building, the taxpayer being represented by Mr. Harold G. Wentworth, attorney New York, New York, and the Bureau was represented by:

Chas. T. Russell, Deputy Commissioner
J. W. Carter, Head, Special Adjustment Division
Paul May, auditor, Special Adjustment Division
George H. Reges, Jr., conferee, Special Adjustment Div.

"At this conference Mr. Wentworth was advised as to the Bureau's position on the several items involved in this case and at 2:30 on the same date Mr. Wentworth returned to the office and proposed that his client's case be closed by the disallowance of only one-fourth of the \$150,000.00 gift and by adding \$5000.00 as living expenses for the years 1925 to 1928, inclusive and \$10,000.00 for the year 1929. Mr. Wentworth was advised that his proposal relative to the reduction in living expenses would be recommended but that his proposal to tax only 25% of the \$150,000.00 item would not be recommended."

HM, Jr: Now, this is October 4th?

'Mr. Wentworth was advised that his proposal relative to the reduction in living expenses would be recommended but that his proposal to tax only 25% of the \$150,000.00 item would not be recommended.'

Mr. Cliphant: Was that before or after the long distance telephone call?

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Mr. Russell: This was before.

Mr. Carter: This was before.

Mr. Helvering: This is just a report on their conference with Mr. Wentworth.

Mr. Cliphant: Was that before he telephoned from New York and he had then been told the Government had accepted ...

Mr. Russell: This was before. He had not been told anything.

HM, Jr: (Resumed reading.)

"He finally agreed that he would recommend to his client a settlement of his case by the disallowance of 50% of the \$150,000.00 item or \$75,000.00. Mr. Wentworth was informed that the aforementioned basis of settlement would be presented to the Commissioner for his approval or disapproval, and that he should call Mr. Carter, Head, Special Adjustment Division, the next day to ascertain the Commissioner's decision."

"On October 5, 1937, Mr. Russell conferred with the Commissioner and Mr. Wenchel, Chief Counsel, Bureau of Internal Revenue. Mr. Russell advised Mr. J.W. Carter on the evening of October 5 that the Commissioner had approved the settlement and that Mr. Wenchel, Chief Counsel, had also approved the settlement. On October 6, 1937 Mr. Wentworth called Mr. J.W. Carter on long distance telephone from New York to ascertain the Commissioner's decision and he was advised by Mr. Carter that the proposed basis of settlement had been approved by the Commissioner.

"A letter was prepared addressed to Mr. Wentworth covering the years 1925 to 1929 inclusive, enclosing an agreement Form 870 for these years and stipulation covering the case for the years 1931, 1932 and 1933, which were before the Board pending an appeal. This letter

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"had reached the Acting Commissioner's office for signature when a telephone message was received in the Acting Commissioner's office from Mr. Wenchel calling from the Treasury saying 'Not to take any action on the Maestri case until he sees you'.

HM, Jr: What day was that?

Mr. Magill: The 6th or 7th.

Mr. Russell: That was on the 6th.

HM, Jr: October 5th they telephoned -- October 5th Carter telephoned that the settlement, that it's O. K. October 6th they get ready to prepare a letter to be signed and Wenchel calls up 'not to take any action on the Maestri case until he sees you'.

"On October 7th a conference was held in the office of the Under Secretary of the Treasury, Mr. Magill. The following individuals were present at the conference:

Mr. Roswell Magill, Under Secretary of
the Treasury
Mr. Herman Oliphant, General Counsel,
Treasury Department
Mr. John P. Wenchel, Chief Counsel In-
ternal Revenue
Mr. Elmer L. Irely, Chief, Intelligence Unit
Mr. Chas. T. Russell, Deputy Commissioner
Mr. A. D. Burford, Special Agent in Charge
Mr. J. W. Carter, Head, Special Adjustment
Division
Mr. George H. Reges, Jr., conferee, Special
Adjustment Division

When did you leave town?

Mr. Helvering: The 5th.

5th?

HM, Jr: The last time they spoke to you was the

Mr. Helvering: Yes, the 5th.

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HM, Jr: Who were there?

Mr. Helvering: The three of us, Wenchel, Russell and myself.

Mr. Russell: I think this conference was about two o'clock in the afternoon.

Mr. Helvering: I left on the 4:45 train for Chicago on October 5th.

HM, Jr: (Resumed reading)

"On October 7th a conference was held in the office of the Under Secretary of the Treasury, Mr. Magill. The following individuals were present: * * *

"The aforementioned basis of settlement was rejected and a 90-day letter covering the years 1925 to 1929, inclusive, was issued under date of October 8, 1937."

Well, that's clear, what has happened up to that. That gets down to the conference which took place in your office.

Mr. Magill: The only question I have on this memorandum, most of it I know nothing about, this last sentence is a little ambiguous. I don't know whether your recollection differs from mine or not. As I have said in my memo, I not only don't recall, but I am quite clear that this Maestri settlement of \$134,000 tax and penalty was not discussed at all on October 7th. I am sure nothing was said to me that the Commissioner had accepted it and taxpayer had been notified because as far as I am concerned it would have put an entirely different cast on the whole thing. Does your memorandum coincide with mine that those things were not actually brought out before me?

Mr. Russell: To this extent: remember I told Mr. Oliphant, who was sitting in conference, that settlement was for \$134,000 which included tax, penalty -- penalty for fraud, and that I thought we had won a moral victory to have the taxpayer agree to a fraud and Mr. Oliphant said we were

HM, Jr: I can't hear you.

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Mr. Russell: I say, in this conference I told Mr. Oliphant that we had an agreement from the taxpayer to the tax and fraud penalty and interest and you remember Mr. Oliphant saying we had no concern with moral victories?

Mr. Magill: I don't remember that at all.

Mr. Russell: Do you, Mr. Carter?

Mr. Carter: I do, very distinctly.

Mr. Magill: Do you have any recollection that statement was made that settlement had been reached, the Commissioner had approved it and the Attorney notified? Because my recollection is very clear that nothing of that sort had been said.

Mr. Russell: I don't remember your being told those exact words.

Mr. Magill: No. I don't think it came up at all and one reason I am sure it did not come up is because Mr. Carter discussed various aspects in the case and I remember, for instance, my own pointing out that this \$100,000 and \$150,000 story looked awfully fishy to me and if the facts were put before the Board I thought there was a fair chance we might get away with those issues even though we had his mother testifying that this was a gift, etc., but I am quite sure Mr. Helvering had not agreed.

Mr. Russell: I assumed that was understood because Mr. Wenchel had sat in on the conference.

Mr. Magill: I am only getting my own story straight because that, as I say, would have made all the difference in the world as far as I am concerned if I had known that this case had really been disposed of.

Mr. Cliphant: Disposed of by notifying the taxpayer.

Mr. Magill: I am sure I did not have that information.

Mr. Oliphant: Maybe not exact words were used. My memory was perfect that nobody said or intimated that the taxpayer's lawyer had been notified that this was acceptable because that becomes an entirely different case, because then

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you are dealing with a commitment that has been made and would raise the question if the commitment had been made prior to Magill or myself or anybody else over here being consulted.

HM, Jr: I am just -- Wenchel knew about it?

Mr. Wenchel: No.

HM, Jr: Now, just a minute. Let me bring you in this picture. "On October 5, 1937 Mr. Russell conferred with the Commissioner and Mr. Wenchel. Mr. Russell advised Mr. J. W. Carter on the evening of October 5 that the Commissioner had approved the settlement basis and that Mr. Wenchel, Chief Counsel, had also approved the settlement."

Mr. Russell: That was the afternoon in your (Helvering) office shortly before you left the office.

Mr. Wenchel: I remember that. I was down to see Mr. Russell on something else and the Commissioner happened to come in and there was some further statement with reference to this conference that we had had, but I did not get the impression that any commitment had been made at that time.

Mr. Russell: I remember distinctly at that time

Mr. Wenchel: Pardon me. My calendar does not show anything at all on that and yet it shows all the other Maestri conferences.

Mr. Russell: I remember distinctly asking if it was all right to advise the taxpayer's counsel that it was acceptable.

Mr. Wenchel: The Commissioner came in with his hat and coat on and you said something to him about the Maestri case and I did not pay any attention because I did not think I was in on that. I was there on something else. It was not until it was brought up this morning

Mr. Russell: And in the first conference in the Commissioner's office it was agreed around the table

Mr. Wenchel: ... therefore, when we went into the conference in the Under-Secretary's office, nothing was said

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certainly not by me nor by anyone else, that the taxpayer had been contacted and what Under-Secretary Magill says is absolutely correct and I did not know it until yesterday morning when Mr. Oliphant told me.

HM, Jr: I don't care whether this is Maestri, or Smith, or Jones. I think that's unimportant compared to the fact that there is something that does not fit together here. It's much more important to me to get this picture fitted together. I don't care whether it's Maestri, Smith or Jones, except that it is an important case, but I don't -- let's all be perfectly -- I mean, I wish everybody would hit, and hit hard, because I don't see -- for Heaven's sake, Russell, talk up for yourself.

Mr. Russell: That's what I am doing.

HM, Jr: You are not doing it very well.

Mr. Russell: I am doing my best. Let's see. Put it this way: we did not take a move until we advised the Commissioner and General Counsel what we were doing and, second, at first conference in the Commissioner's office there were approximately eight or ten people there. Everybody agreed that if the taxpayer would submit an offer of one-half of the \$150,000, we would accept it and on the 5th Mr. Wenchel and Mr. Helvering was there. I told them the taxpayer was willing to accept it and it was all right to advise them.

HM, Jr: Where did this meeting take place?

Mr. Russell: In the Commissioner's office.

Mr. Wenchel: That is explained. He was on leave. Russell was Acting Commissioner and he called me up about another matter and we started to discuss it on the telephone and I went downstairs. While we were discussing the matter, the Commissioner came in with his overcoat and hat on and he did not even sit down and Mr. Russell was talking to him and all that I remember was something was said about the Maestri case. I was not consulted. It looked to me like it was carrying on this conversation

Mr. Helvering: Here is all that was said. Russell said to me there that 'while you are here, I am going to

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tell you that Maestri's attorney has agreed to accept the proposition of \$75,000 inclusion in taxes. That is, the income of \$75,000 is taxable.' I said, 'That's what we agreed to the other day. Go ahead and finish it.' I walked out that morning. That morning I asked Mr. Russell to take care of the office because I was leaving.

Mr. Russell: I remember distinctly saying, 'Well, here's the Commissioner out here now. Better talk about the Maestri case before he leaves.'

Mr. Wenchel: No, I don't remember that.

Mr. Russell: We were sitting there talking about something.

Mr. Wenchel: We were sitting there talking. We had some papers in front of us and the Commissioner walked through that door and he was there before I knew he was there. I got up and shook hands. You two talked. I know you were talking about the Maestri case, but what you were saying I don't remember.

Mr. Helvering: I suppose after our previous conference when we had said distinctly if this is conceded and this is conceded then we insist on this and this. Now if that is done and the fraud penalty is added, I will agree to it. But we have to add fraud penalty because the thing is outlawed if we don't.

HM, Jr: Let me ask you this: Here is a case, certainly an important one, which if you had settled on this basis would attract a lot of attention. Going back to Russell, why would you take the responsibility of doing this on verbal assurances. Why wouldn't you get somebody to sign something or write a memorandum, or if you were Acting, why wouldn't something be written saying that this was finally approved by Mr. Helvering and Mr. Wenchel?

Mr. Russell: I did not think it was necessary to have a written memorandum.

HM, Jr: How do you settle other cases?

Mr. Russell: This is the only case with so many people sitting in on so many conferences. We did have to safeguard the Government's interests.

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HM, Jr: You had so many people sitting in on it and no written memorandum?

Mr. Russell: I did not think it was necessary to have a written memorandum of what these gentlemen agreed to.

HM, Jr: The result is it puts you in a very unusual position.

Mr. Russell: It does that. I am willing to take that unusual position if nobody else will go along with it.

HM, Jr: As far as Mr. Helvering is concerned, he's out of the picture. When he stopped out October 5th he said, They have done everything? and you said yes. So he said, All right. So he takes a train and that let's him out. But what I can't get, because I don't know how Wenchel works, but if somebody started talking to me about the Maestri case, I would say, if this is going to be the case let's sit down; I can't give a yes or no.

Mr. Helvering: I am not saying this to be contentious at all, but if you take the conferences just of Bureau officials, in which we were all present, and the agreement was made that certain items would be excluded and certain items be included -- now, that was all formal hearings.

HM, Jr: Right.

Mr. Helvering: Now, the only thing that occurred on October 5 was that Russell stated that Maestri's attorney had agreed to that.

HM, Jr: Right.

Mr. Helvering: So go ahead and settle up.

HM, Jr: If I were in your position -- you go in, or say I go into Magill or Oliphant's office. We have been working on the thing a week. We say if we get this that I will go along. I go in. He says I have got everything we asked for. I say, O. K.; settle.

Mr. Helvering: You wouldn't write a memorandum.

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HM, Jr: On a case like this? Yes, I would. Yes, I do. The answer is that I very definitely do. I not only do, but I have a secretary here taking it. I can't trust my memory. There are too many important things. No, on a thing like this I very definitely do. I still don't see why this thing having been settled, if you don't mind my saying so, if I were in either of you gentlemen's shoes -- I go over to Mr. Magill's office. I say, Mr. Magill, before we even start this thing we think it is our duty to say to Magill and Oliphant that the taxpayer's attorney has been notified that we would settle. Now I can't see how you would walk in Magill's office and discuss this thing for two hours and not tell him that Mr. Wentworth had been advised that this thing would be acceptable.

Mr. Russell: I was under the impression that was why I was up in Magill's office.

Mr. Wenchel: I did not know that he had.

HM, Jr: It all goes back to Russell.

Mr. Russell: All right. I will be the goat. Mr. Secretary, we did not take one step without keeping everybody advised of what we were doing.

Mr. Oliphant: Now, when you notified the taxpayer on October 4th, I was not advised.

Mr. Russell: I remember in the Commissioner's office on the 5th saying that Maestri's lawyer had agreed to accept it and saying I am going to notify him.

HM, Jr: It would be just the same thing if we were sitting here and a month later I find you had accepted Maestri's check. You say, I thought we were discussing the principle and you say, 'Well, you know, Mr. Morgenthau we accepted his check. We already had his check.'

When did you tell him to stop action?

Mr. Wenchel: I don't remember the date of that, but I did call him and told him not to take any action. I remember when it was

Mr. Russell: On the 6th.

Mr. Wenchel: It was. That was the day before this

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conference in Under-secretary Magill's office.

Mr. Oliphant: I was in Indiana.

Mr. Wenchel: I called you up, Russell, and asked you if you had been notified of the conference and then said you had better not take any action.

Mr. Russell: This is the memorandum that I got. (See exhibit V.) Subsequently I was advised about the conference to be held in Mr. Magill's office, but this is the first information I got

HM, Jr: What I am going to do ~~as~~ as to what has taken place in this room and as to your action, I am going to let Mr. Helvering study it. After all, you are responsible to him. I want you to decide whether Mr. Russell has done anything that is improper and after you have had time I would like to talk to you further, but, after all, he is your man and after you have talked it over I would like to talk to you. That takes care of whether Mr. Russell did or didn't.

Now, as to the situation about the Maestri case. After all, we have a lot of things to do. We will start with you, Mr. Helvering. Have you changed your position any since you said that we would take this \$134,000?

Mr. Helvering: No. I am very strongly of the opinion that that is a good settlement.

HM, Jr: You still feel that way?

Mr. Helvering: Yes.

HM, Jr: I am not going to call on these men if that's the way you feel, because they are your subordinates.

Mr. Helvering: May I say a word in that connection? Before we reached any conclusion on this, I called Mr. Burford in and had a talk with him about this case. Burford stated to me, 'Now, Mr. Commissioner, I don't know whether we have a case with Maestri or not.' He says, 'If we can't set up fraud, we haven't,' and he gave me all this detail about the Statute of Limitations. But, he said 'I think he's the biggest crook in the bunch,' or something to that effect. Well, we are confronted

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HM,Jr: Pardon. Did Burford recommend that we take this?

Mr. Helvering: Oh, yes!

HM,Jr: He's on record?

Mr. Carter: He has not signed any report, but he is in accord with this proposed settlement.

Mr. Helvering: He told me in an off-hand conversation in my office that he thought it was a good settlement.

HM,Jr: Will he sign this report?

Mr. Carter: He will. He has not been asked.

HM,Jr: Will Irey and Burford both?

Mr. Helvering: I haven't talked to Irey because Burford was the man working on the case.

I just want to explain the difficulties we have. On this \$150,000 item there are five affidavits on file from Maestri, his two sisters, from his mother and from one outside party, telling they knew about this agreement. I told the boys it taxed my credulity that anybody was handing around \$150,000 cash and I would not concede that that was done, but in face of these affidavits and without any definite evidence on our part to refute them, I thought we would have a hard time to prove that in the Court.

Mr. Cliphant: But we do have a chance of getting Maestri's brother who has an adverse interest and he's fighting his brother over who gets this money from his father and he's coming in and spilling the beans and that would very well wipe out the five affidavits.

HM,Jr: I want to save time. I am going to ask Irey right now. (Telephoned Mr. Irey and transcript of the conversation is attached, marked exhibit VI.)

Mr. Helvering: I want to show you one further step. As a result of this conference in which it was set out what we would do and Mr. Russell's statement to us of that day

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that that had been agreed upon, of course here's the letter prepared to go to the attorney. This was on Mr. Russell's desk when this letter came to me. (See Exhibit VII.)

Mr. Russell: I was just getting ready to sign it.

Mr. Helvering: This is the letter to Wentworth in the Maestri case. Of course that letter never was sent.

Mr. Oliphant and I had a conference in his office one day and we agreed, and Herman and I talked it over, that we ought to have one of his men and one of ours sit in on all the Louisiana cases and I told him I would send him a memorandum on just what the situation was about these cases. September 11th I transmitted this letter to him and he acknowledged it on the 14th and I detailed all of the so-called Louisiana case, those that had been settled and those that had not and those that had been indicted and those who had not and 90-day letters and all that. Later Mr. Magill called me some time later -- I don't remember but I think I have it here though -- and asked me -- here it is, October 25 -- and I sent you, if you remember

Mr. Magill: You sent me another memorandum.

Mr. Helvering: Yes. On just the situation on all the cases. I honestly thought -- I know nothing about the conference over here, of course, but I thought we were handling it just the way we outlined it in your office.

Mr. Oliphant: Well, if this were a case arising in Des Moines, Iowa, involving any individual, I think you would have to say on available evidence this is a fairly good settlement, but if it were a Des Moines case and we did settle, we would be sitting here settling it by deciding disputed questions of fact.

Now, following the settlement of the criminal cases we went into the question pretty carefully. It seemed to us then that regardless of whether we lost or won a little money, it was too serious a matter for us to take the responsibility of resolving these doubtful questions of fact and we ought to put it up to the Board and let the Board decide it in open meeting. The newspapers are not in here. To my mind, it is easier to do it if the newspaper men are here. If it is put up to the Board, everybody hears it.

HM, Jr: We make a perfect jackass out of ourselves

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because I consider that letter they sent out -- I don't have to be even a third-rate lawyer to know that letter would make a perfect jackass out of the Bureau. After they have agreed to this whole business, then they stick that stuff back into a 90-day letter.

Mr. Russell: We agreed to \$75,000 and we had to stick that back.

Mr. Oliphant: Now, that is the desirable thing to do. Have the thing tried by an impartial tribunal in an open court room.

Here's the unfortunate thing. The taxpayer's lawyers have been notified that this thing is agreeable over in the Bureau, so that takes the whole thing over to the Secretary to take the responsibility of saying that, regardless of what my Bureau says, I am going to insist on public trial.

HM, Jr: I had not thought of it in that way. What I was thinking of, if this fellow Wentworth is a good lawyer I would attack the Internal Revenue Bureau and I would attack this whole method and I would just break down this whole business, that they agreed to this thing and who is responsible? The Commissioner? Is he responsible? What is the Secretary's office? Where do they come in when all these people -- is he trying to prosecute this man?

Mr. Oliphant: Is the Secretary personally trying to prosecute this man.

HM, Jr: In view of that, what I was going to, I was going to ask you and Magill, because I would like to settle thing thing now, in view of what has happened -- a lot has been most educational to me in view of this thing -- should we take Mr. Helvering's recommendation in this matter and let him proceed?

Mr. Magill: Well, my reaction is that you should. I think this: you have got an extremely difficult problem. I feel as Mr. Oliphant has expressed himself, particularly in this group of cases, which have had public notoriety, a public trial is highly desirable from our point of view unless the issues can be settled by agreement. On the other hand, the Commissioner having determined that the

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settlement is proper and the taxpayer having been notified, I don't believe either you or I want to be in the position of telling the taxpayer and his attorney that we want to throw the Commissioner down and I am further moved to that by a technical aspect that might not occur to you and that is that this particular type of letter in this particular type of case is exclusively in the Commissioner's jurisdiction. In the ordinary type of case, it does not come over here at all, so if Wentworth is at all shrewd he could bring it out and say to the Senator that this case has been given very unusual attention and that obviously you did this.

HM, Jr: Do you mind giving me a yes or no.

Mr. Magill: I say yes. I think you had better go ahead with the settlement. I don't like it.

Mr. Oliphant: Nothing can be done that I would like less, but I think you had better go ahead with the settlement. One of those unfortunate things.

Mr. Wenchel: I think it is a good settlement, if it were not for what is underneath it.

HM, Jr: Because I feel that the fact that Senator Ellender did not mention that the Bureau had offered settlement was very significant and he's just going to hold that back until he finds out whether the Secretary's office is going to push this and if we were going to push it these people would open up the whole question of how this thing is administered.

In view of what has happened, I say you go ahead from where you were the afternoon of October 5th and the matter is in your hands and everybody here is agreeable that you go ahead.

Mr. Helvering: All right.

Mr. Oliphant: Should this special policy continue in the Louisiana cases, or should we not have special handling.

HM, Jr: Before we take that up, I want Helvering to sit down with his own people and go into this thing first and after he has gone into this whole business -- there is another case pending now.

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Mr. Oliphant: The Shushⁿ.

HM, Jr: Well, I have got the Federal Reserve all waiting outside. But let's do it this way: I would like you, Guy, to sit down with your own people. This question of policy, I will answer that. This question of policy between the Bureau -- I frankly haven't got the time. I have got Oliphant and Magill here. They are both ably trained lawyers and if Senator Ellender had not asked to see me and I said I would see any taxpayer and I have to see a Senator, do I have to sit down with you two people and get into -- should I have to sit on a thing like this?

Mr. Magill: I don't think you should.

HM, Jr: I don't either. If you said to me right now, if you pushed me, I would say a matter like this I would give Helvering all the discretionary power that he wants and let Helvering go ahead. If it comes that Helvering closes some case like this and you gentlemen don't like it, there is always time to sit down and say in the future I wouldn't do it, but my feeling is I would give Helvering all the leeway he wants, but before we do that I would like to sit down with you, Helvering and Magill and Wenchel and Oliphant. I think the five of us should sit down next week, when this financing is over, and let's talk this thing out as to -- not only New Orleans; other things.

Again using this as an example, and I tell you now, Helvering, I would very much like you to settle this question of 90-day letters because I don't think that we should put anything into a 90-day letter which we don't believe.

Mr. Helvering: How are you going to do it?

Mr. Russell: How about Associated Gas cases then?

HM, Jr: All right. I will give you or anybody in this room -- but there is something wrong when the United States Government, if they think a fellow adds \$100,000 and another \$50,000 for trading purposes in the hope that we collect \$100,000 knowing damn well that we won't collect \$150,000. You make up the 90-day letter, but you don't have to defend it before the Board of Tax Appeals?

Mr. Russell: No, sir.

HM, Jr: You do, don't you?

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Mr. Wenchel: Yes, sir.

HM, Jr: Then there is something wrong. But he (Russell) makes up the bill of particulars and this fellow (Wenchel) has to try to prove it. Now I say the United States Government -- we criticise the business man for being phony and I say we stuck this thing in -- it's phony.

Mr. Helvering: Mr. Secretary, if you don't get everything in and make every assessment on every year and every situation that you can, the Board will say it's not in this year; it's in another year. If you don't put the assessment in both years, you are out. This is a very complicated case. You have great confidence in Harold Graves and he has done a great job. I would like to have a study made by him or his men under his supervision, of just exactly the procedure on 90-day letters.

HM, Jr: Anything better than that?

Mr. Magill: It's O. K. I don't know that he's the man to do that particular job, but maybe he's the best man available.

HM, Jr: I will tell you what we will do. Let's do it this way. Will you people move just as fast as you can on this thing and any time you are ready I will set an hour a day until we clean this thing up. I can't do it this week, but I can next.

We know where we are on the Maestri case. I am finished.

oOo-oOo

Ephest I 28

November 30, 1937

TO: Secretary Morgenthau
FROM: Mr. Magill

Re: Maestri Case

My files contain the following information with respect to this case and the other Louisiana cases:

On September 11, 1937, Commissioner Helvering forwarded to Mr. Oliphant a list of the so-called Louisiana cases and a statement of the action taken thereon in the Bureau, the Board of Tax Appeals, and the Courts. In the case of Mr. Robert S. Maestri it appears that the years 1925-1929, inclusive, are "open"; a sixty day letter had been issued for the years 1930 and 1931 and a ninety day letter issued for the years 1932 and 1933. My memorandum to you of the day's activities dated October 7, 1937, contains a paragraph summarizing a conference held on the Louisiana group of cases. The last two sentences of my memorandum to you are as follows:

Oct 7th
"Mr. Oliphant has already directed that in the settlement of cases there should be no 'horse trading'; that is, if there is evidence on both sides of a particular issue the issue is to be submitted to the Board. Compromises are only to be made where the taxpayer concedes the point or where it clearly appears that the Treasury determination was wrong."

On October 27, 1937, Commissioner Helvering sent me another memorandum on the Louisiana cases, from which it appears that a ninety day letter issued on October 8, 1937, to Mr. Robert S. Maestri for the years 1925-1929, inclusive, for each of which years a fraud penalty was asserted. You will note that this deficiency letter was sent out the day after the October 7th conference in my office. Finally, my memorandum to you of the day's activities dated November 6, 1937, summarizes a conference I had with the Commissioner on these cases. Specific reference is made to a telegram from Mr. Robert S. Maestri to the Commissioner asking for a conference regarding settlement of his case; and my recommendation that the Commissioner should tell Mr. Maestri to take up his case for settlement with the Technical Staff in the usual way, with instructions from the Commissioner to the Technical Staff that no settlement should be made except with the approval of the Commissioner and Mr. Oliphant.

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I am positive that no mention was made at the October 7th conference of any definite proposition made by Maestri and approved by the Commissioner to settle the Maestri case; nor that Maestri's attorney had been notified that the Commissioner had agreed to accept an offer in settlement made by Maestri. It is my understanding that both Mr. Oliphant and Mr. Wenchel fully agree with my recollection on this point. If any such specific proposal to settle had been mentioned I would certainly have reported it to you on October 7th as I did report the offer of settlement reported to me by the Commissioner on November 6th. Further I would have instructed the Commissioner or Mr. Russell on October 7th in the same way that I had instructed the Commissioner on November 6th, namely, to make no settlement or agreement to settle without the approval of Mr. Oliphant.

Rm

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

Exhibit II 30

DATE NOV 30 1937

TO Secretary Morgenthau
FROM Herman Oliphant

The Maestri Settlement

I have discussed this matter today with Mr. Wenchel and we have examined our calendars. This is what happened:

Wenchel began work in the Bureau September 22. Eight days later, on September 30 at 10 a.m., he sat in a conference on the Maestri case in Helvering's office with Helvering, Russell, Carter, Regis, May, Pierce and Norman, one of his lawyers. Wenchel did not then know that the Louisiana cases were the subject of special instructions because it had not been possible for me to tell him about all the special situations and unusual problems pending in his office and the Bureau.

At this conference in Helvering's office, Wenchel, remembering and mentioning newspaper discussions of the Louisiana cases, asked if there was anything unusual about this Maestri case and was told that what he had in mind was the criminal cases, but that this was a case of settling civil liability. He then agreed that, the evidence on the various issues being what it was, the following proposal to settle was a good one:

Accept the taxpayer's claim as to the \$80,000 from the sale of stock. Cut the alleged gift of \$150,000 in half. Assess \$57,658.14 instead of \$100,000 "nest-egg" since \$42,341.86 had been assessed and taxes paid thereon in the year 1930.

However, Wenchel did not get the impression that this conference was to conclude the matter because Helvering was insistent that no plan

- 2 -

of settlement would be acceptable unless it involved the payment of at least the full tax. Wenchel says he did not know until this morning that the taxpayer's lawyer had been informed that the settlement was satisfactory.

At noon the same day, Wenchel came over on other matters and told me that settlement of the Maestri case was under discussion in the Bureau, and he gave me the substance of the conference he had attended. I then told him of the special circumstances **surrounding**, and the special instructions covering the Louisiana cases.

As soon as Wenchel told me that settlement of the Maestri case was under discussion, and while he was still sitting with me, I called Magill on the telephone and told him. Magill and I agreed that everybody concerned in the Louisiana cases should be got together and the Department's policy with reference to them made clear.

This conference was held in Magill's office on October 7, I in the meantime having had to go to Indiana because of family illness. Mr. Wenchel says the offer of compromise was mentioned at this conference, but my memory and Wenchel's memory are perfectly clear that no one in this conference said or intimated that settlement of the Maestri case had been agreed upon and his attorney notified.

I attach photostatic copy of a memorandum I dictated for my files on September 7, 1937, and a copy of my memorandum of September 1 to Morrison Shafroth.

Louise Olyphant

*Plany
safe*

Memorandum.

Helvering called me today at ten minutes of four, saying that there was to be a conference tomorrow in Russell's office on the Maestri Case.

I recalled the decision of policy made when Justice dismissed the criminal cases. I called Irey to be sure he would be there, and I called Shafroth, asking him to attend, and mentioned to Shafroth also the decision of policy.

September 7, 1937

Exhibit III

September 1, 1957

MR. SHAFROTH:

In re: Abraham L. Shushan,
New Orleans, Louisiana,
and related cases.
Docket No. 85317.

I have approved your memorandum dated July 30, 1957, outlining the procedure to be followed by the Appeals Division of your office in the disposition of the cases listed in your memorandum. This approval is with the distinct understanding that all cases involved in this group will be disposed of solely on the basis of the merits of each issue in controversy and that there will be no so-called "horse-trading" of issues for the purpose of arriving at a settlement of any of the cases. Any cases that cannot be settled on the terms dictated by the attorneys having charge of the cases should be submitted to the Board of Tax Appeals for decision.

(Signed) Herman Oliphant

Herman Oliphant
General Counsel

RHT-afh 8-31-57

Exhibit IV

Dec 1, 1937 34

MEMORANDUM

In re: Robert S. Maestri,
New Orleans, Louisiana.

A thirty-day letter was issued in the above-mentioned case under date of September 16, 1936 covering the years 1925 to 1929, inclusive, disclosing deficiencies in tax of \$144,334.65 and penalties of \$72,167.33, a total of tax and penalty of \$216,501.98. In response to this letter, under date of January 18, 1937 the taxpayer called in person accompanied by Senator Allen J. Ellender and a discussion was had on that date with the following representatives of the Bureau of Internal Revenue:

J. W. Carter, Head Special Adjustment Division
George H. Reges, Jr., Conferee, Special Adjustment Division
Paul May, Auditor, Special Adjustment Division
C. O. Pierce, Auditor, Special Adjustment Division

No protest had been filed at the date of this hearing and no evidence was presented. It was agreed, however, at this conference that the taxpayer would be furnished with a net worth statement prepared by the Internal Revenue Agents which formed the basis for the deficiencies and penalties proposed in the thirty-day letter dated September 16, 1936.

A number of extensions of time for filing the protest were requested by the taxpayer and on May 29, 1937 the taxpayer made a further request in writing stating that due to illness a further request for an extension was made in order to give him an opportunity to protest against the proposed assessment. On June 24, 1937 the taxpayer was advised that a final extension of 15 days from the date of that letter was granted for the purpose of filing a protest. Under date of July 16, 1937 the first protest in writing was received in the Bureau. A conference was arranged for August 19, 1937 to be held in the Internal Revenue building which was later postponed to September 9, 1937. Under date of September 8, 1937 the taxpayer supplemented his protest and a conference was held on September 9, 1937. The taxpayer at this conference was represented by Mr. Harold G. Wentworth, an attorney of New York, New York. The Bureau was represented at this conference by the following:

Mr. Morrison Shafroth, Chief Counsel, Bureau Internal Revenue
Mr. Chas. T. Russell, Deputy Commissioner
A. D. Burford, Special Agent in Charge,
Mr. Harold Norman, Special Attorney, Penal Division, Chief Counsel's
office
Mr. J. W. Carter, Head, Special Adjustment Division
C. O. Pierce, Auditor, Special Adjustment Division
Paul May, Auditor, Special Adjustment Division
George H. Reges, Jr., Conferee, Special Adjustment Division

In re: Robert S. Maestri.

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At the conclusion of this conference there was additional information or evidence which Mr. Wentworth desired to submit for consideration of the Bureau representatives. This information was received under date of September 25, 1937. Under date of September 30, 1937 a conference was held in the Commissioner's office attended by Mr. Guy T. Helvering, Commissioner, Mr. Wenchel, Chief Counsel for the Bureau of Internal Revenue, C. T. Russell, Deputy Commissioner, Mr. Harold Norman, Special Attorney, Penal Division, Chief Counsel's office, Mr. J. W. Carter, Head, Special Adjustment Division, Mr. George H. Reges, Jr., Conferee, Special Adjustment Division, Paul May, Auditor, Special Adjustment Division. At the above conference the following items were discussed:

- (1) The taxpayer's contention as to the \$100,000.00 on hand in 1910,
- (2) The taxpayer's contention as to the \$150,000.00 gift in 1916,
- (3) The taxpayer's contention as to the \$80,000.00, proceeds from the sale of stock in 1923,
- (4) The taxpayer's contention as to the \$103,413.57, proceeds from partition sale in 1927,
- (5) The taxpayer's contention as to the \$1000.00 and \$12,000.00 mortgage notes,
- (6) The taxpayer's contention as to the \$10,000.00 living expenses,
- (7) The taxpayer's contention as the fraud penalties.

At this conference it was concluded that the taxpayer's contention on the \$100,000.00 on hand in 1910 should be denied; that the taxpayer's contention as to the \$80,000.00 proceeds received from the sale of stock in 1923 should be conceded; that the taxpayer's contention as to the \$103,413.57 proceeds from partition sale in 1927 should be conceded; that the taxpayer's contention as to the \$1000.00 and \$12,000.00 mortgage notes should be conceded; that the taxpayer's contention as to the fraud penalty should be denied and the taxpayer's contention as to the \$10,000.00 living expenses should be denied. This left only one item still in dispute; that is, the taxpayer's contention as to the \$150,000.00 gift in 1916. On this item it was the opinion of the Commissioner and Mr. Wenchel, Chief Counsel, that the full amount of this gift should not be conceded but it was their conclusion, based on the evidence in the case, that if the taxpayer would concede one-half of \$75,000.00 of this item that that would be a fair settlement.

Under date of October 4, 1937 a hearing was held in the Internal Revenue Building, the taxpayer being represented by Mr. Harold G. Wentworth, attorney New York, New York, and the Bureau was represented by:

- Chas. T. Russell, Deputy Commissioner,
- J. W. Carter, Head, Special Adjustment Division
- Paul May, auditor, Special Adjustment Division
- George H. Reges, Jr., conferee, Special Adjustment Division.

At this conference Mr. Wentworth was advised as to the Bureau's position on the several items involved in this case and at 2:30 P.M. on the same date Mr. Wentworth returned to the office and proposed that his client's case be closed by the disallowance of only one-fourth of the \$150,000.00 gift and by adding \$5000.00 as living expenses for the years 1925 to 1928, inclusive and \$10,000.00 for the year 1929. Mr. Wentworth was advised that his proposal relative to the reduction in living expenses would be recommended but that his proposal to tax only 25% of the \$150,000.00 item would not be recommended.

In re: Robert S. Maestri.

He finally agreed that he would recommend to his client a settlement of his case by the disallowance of 50% of the \$150,000.00 item or \$75,000.00. Mr. Wentworth was informed that the aforementioned basis of settlement would be presented to the Commissioner for his approval or disapproval, and that he should call Mr. Carter, Head, Special Adjustment Division, the next day to ascertain the Commissioner's decision.

On October 5, 1937 Mr. Russell conferred with the Commissioner and Mr. Wenchel, Chief Counsel, Bureau of Internal Revenue. Mr. Russell advised Mr. J. W. Carter on the evening of October 5 that the Commissioner had approved the settlement basis and that Mr. Wenchel, Chief Counsel, had also approved the settlement. On October 6, 1937 Mr. Wentworth called Mr. J. W. Carter on long distance telephone from New York to ascertain the Commissioner's decision and he was advised by Mr. Carter that the proposed basis of settlement had been approved by the Commissioner.

Following aft Wash. Oct 5th 4.45 P.M.
Oct 6th
 A letter was prepared addressed to Mr. Wentworth covering the years 1925 to 1929 inclusive, enclosing an agreement Form 870 for these years and stipulation covering the case for the years 1931, 1932 and 1933, which were before the Board pending on appeal. This letter had reached the Acting Commissioner's office for signature when a telephone message was received in the Acting Commissioner's office from Mr. Wenchel calling from the Treasury saying "Not to take any action on the Maestri case until he sees you."

On October 7, 1937 a conference was held in the office of the Under Secretary of the Treasury, Mr. Magill. The following individuals were present at that conference:

Mr. Roswell Magill, Under Secretary of the Treasury,
 Mr. Herman Oliphant, General Counsel, Treasury Department
 Mr. John P. Wenchel, Chief Counsel Bureau Internal Revenue
 Mr. Elmer L. Irely, Chief, Intelligence Unit
 Mr. Chas. T. Russell, Deputy Commissioner
 Mr. A. D. Burford, Special Agent in Charge
 Mr. J. W. Carter, Head, Special Adjustment Division
 Mr. George H. Reges, Jr., conferee, Special Adjustment Division

The aforementioned basis of settlement was rejected and a 90-day letter covering the years 1925 to 1929, inclusive, was issued under date of October 8, 1937.

Chas. T. Russell

In re: Robert S. Maestri.

The returns for the years 1925 to 1929, inclusive, have been destroyed except for the year 1929. The statute of limitations has expired for all years and all of the tax will be lost unless the Government is successful in establishing fraud. The income is computed on the basis of net worth and the agents have been unable to trace any of the sources of unreported income.

The Commissioner of Internal Revenue

Mr. Russell:

Mr. Wenchel called you from the Treasury just after you left for lunch.

He says not take any action on the Maestri case until he sees you.

JMG

December 1, 1937.
10:03 a.m.

- H.M.Jr: I just want to tell you, on the loud speaker, see. This conference is going on. Mr. Helvering and the others are here.
- Elmer L. Irey: Yes.
- H.M.Jr: The question has come up, whether you or Burford, Burford having sat in on this conference when they considered this Maester case. I mean would you or Burford sign this report recommending that we accept the hundred and thirty four thousand?
- I: You say, would we sign such a report?
- H.M.Jr: Yes.
- I: Why, I haven't gone into the figures enough to know about that, Mr. Secretary. I mean it's been so long since I went through the case I don't remember the tax setup, nor what the explanation is.
- H.M.Jr: Well, what about Burford?
- I: Well, Burford, of course, is down in Dallas, Texas. I can't say for him, but I can communicate with him, today, and find out. And I also can go into the case myself today and find out how I feel about it.
- H.M.Jr: Well, why wasn't it ever brought to your attention before they recommended it to be accepted?
- I: Well, I am sure I don't know that, Mr. Secretary, but, when we - the usual procedure in these tax cases is when the criminal phase is out, it's not then referred to us for any further attention. It's handled by the tax branches of the Bureau.
- H.M.Jr: Well, Burford sat in on it.
- I: Yes, Burford sat in over at Mr. Magill's office on it, and I also sat in at that time, on it.
- H.M.Jr: No, he sat in on it on September 9th, when they had the hearings.
- I: Yes. Well, I didn't know about that - I didn't remember about it.

H.M.Jr: Well, now just a minute, let me ask Mr. Helvering.
(aside) Mr. Helvering states that Mr. Burford
told him that this was a good settlement, and based
on that Mr. Helvering recommended the thing be
settled.

I: Well, of course, that's perfectly all right, then.
I didn't have any discussion with Burford as to
the tax liability so I don't -

H.M.Jr: Well, I'm not - I'm not going to check up on
Mr. Helvering's way. I'll take Mr. Helvering -
word

I: Surely. There isn't any doubt but what Burford
told him that.

H.M.Jr: Yes, well I'm not going to check up on Mr. Helvering.

I: Yes.

H.M.Jr: But it's not customary that you sign these things.

I: No, sir. It's not.

H.M.Jr: Well, I'm not going to check up on Mr. Helvering.

I: Yes.

H.M.Jr: Thanks.

I: All right, sir.

H.M.Jr: I may - all right, thank you very much.

I: All right.

Ephelbit VII

IT:Aj
GHR-21838

Mr. Harold G. Wentworth,
39 Broadway,
New York, New York.

In re: Robert S. Maestri,
New Orleans, Louisiana,
(1925 to 1933, inclusive)

Sir:

Reference is made to the conference held in the aforementioned case before this office under date of October 4, 1937.

In accordance with agreement reached with you on behalf of the taxpayer as a result of that hearing, there is enclosed a qualified agreement form 87GM covering the years 1925 to 1929, inclusive. There are also enclosed stipulations covering the agreed to deficiency for the years 1931, 1932 and 1933.

In order that the case of your client for the years covered by said agreement and stipulations may be closed promptly, it is requested that said agreement form and stipulations be promptly signed and returned to the Special Adjustment Division within fifteen days from the date of this letter.

It appears that you have not filed your notice of appearance with the United States Board of Tax Appeals. If you have not already done so, it is suggested that you comply with the Board's rule in this respect in order that the stipulations, if signed by you, may be filed promptly.

Respectfully,

Acting Commissioner.

Enclosures:
Form 87GM
Stipulations.

GHR/EMO

December 1, 1937

To: The Secretary

From: Mr. McGill

Congressman Vinson called me last night at home and asked to come and see me about policy questions that were troubling him. He and Mr. Doughton arrived together about eight o'clock and stayed until ten. They told me that Congressman Beiter of Buffalo filed a petition in the House yesterday afternoon to discharge the Ways and Means Committee from further consideration of a bill to repeal the undistributed profits tax. Messrs. Doughton and Vinson expect that Republicans will all sign such a petition; that 50 or 60 Democrats opposed to the President will do so; and, in addition, some other Democrats who think they will gain prestige in their own district in advocating repeal of this tax. Mr. Vinson does not think that the petition will be signed by the necessary half of the membership but he also feels that it is an important symptom of dangerous unrest on this subject in the House. He would like to make a speech to the House outlining the plans of the subcommittee on the undistributed profits tax but he cannot do so until (1) the subcommittee agrees finally upon a program, the present plan having been adopted tentatively; and (2) the President indicates his approval of the program. Mr. Doughton reported that the President had told him that the rates of the Vinson plan were too low and suggested an alternative plan which involves keeping the present undistributed profits tax for corporations which do not distribute as much as 75 percent of their incomes.

Mr. Doughton expressed his judgment that the present undistributed profits tax would be repealed by the House if it had a chance to vote on it and he thought further that the House would not accept the present form of tax, even if the rates were changed. He said the President's plan outlined to him on Saturday was to impose a 20 percent flat tax on corporations with an exemption of 25 percent of their earnings from any undistributed profits tax. Thus, if a company distributed 75 percent or more of its earnings, it would pay a 20 percent tax on its net income. Corporations would also be given credits for amounts used for debt retirement or improvements and for reserves earmarked as such. If after all these credits the corporation still had undistributed net income, it would be subjected to tax at the rates now in the law. Mr. Vinson said he thought the President's plan was impractical and Mr. Doughton said that in his opinion the House would not accept it. Mr. Vinson further believes that Senator Harrison's speech is an indication that the Senate will repeal the undistributed profits tax or any substitute therefor, such as the present Vinson plan.

We all agreed that the next step was for the draftsman to prepare legislation embodying the Vinson plan, plus a broadening of the provisions applicable to corporations which unreasonably withhold earnings from their stockholders. As soon as the draftsman and the committee can

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put

iron out the various questions which will arise in the course of reducing the general plans to specific form Messrs. Vinson and Doughton would like to have the President advised, secure his approval, and then proceed to announce what has been decided to the House, in order to forestall hasty action looking toward repeal of the undistributed profits tax entirely.

Both men felt that Mr. Vinson's proposed speech to the House should be made before the end of the week. In my opinion it will be extremely hard for the draftsmen to complete their work and for the President's approval to be secured in any such time. I think what Messrs. Doughton and Vinson really want, although they did not say so directly, is for you and me to advise the President that the Vinson plan is the best that he can hope for and that insistence upon higher rates is apt to bring about the repeal of the undistributed profits tax entirely without any substitute embodying the principle.

Subject to your further suggestions, I am going to tell Messrs. Doughton and Vinson that so far as I can see the essential next step is for the draftsmen to work out the details of the Vinson plan, plus a satisfactory enlargement of the present provisions for taxing corporations which accumulate unreasonable surpluses. Until their work is pretty well completed I do not see what we could convey to the President beyond what he apparently knows already.

Rm

December 1, 1937

To: The Secretary
From: Mr. Magill

Following my conversation with you this noon I called Congressman Doughton and told him that it would be impossible for you to see Mr. Vinson and himself this afternoon since your time was completely occupied with your December financing. I said further that I understood from the draftsmen that they had run into a good many snags in working out the Vinson plan for taxing corporate income. Hence, I thought Messrs. Doughton and Vinson ought to talk to the draftsmen and settle some of the policy questions involved before making up their own minds as to the course of action the committee should follow. Mr. Doughton said he would call Mr. Vinson at once and would try to talk to the draftsmen, Messrs Beaman and Parker, later this afternoon. Mr. Doughton asked me to see him before the committee meeting tomorrow morning.

Mr. Doughton said he would like to talk to you tomorrow afternoon but I will do my best to take care of his doubts and fears tomorrow morning.

I am perfectly clear that you and I should send no message to the President at this time on the subject of the undistributed profits tax.

Rm

Copy for the Secretary

December 1, 1937

To: Mr. Graves

From: Mr. Magill

The Commissioner and I have often discussed the various steps which might be taken in order to insure greater accuracy in the deficiency letters sent out by his office. Taxpayers frequently complain that after they have failed to reach an agreement with the Bureau upon the amount of income tax, the Bureau determines a deficiency largely in excess of the amount which is due, even under the Bureau's own theories. Moreover, you have doubtless observed that the percentage of deficiencies as determined by the Commissioner which is finally approved by the Board runs comparatively low. We would all like to see the machinery for the determination of deficiencies perfected to the point that the deficiency letter sent to the taxpayer would represent an accurate statement of what the Bureau honestly believes the taxpayer to owe.

There may be some instances in which duplicate determinations are necessary to protect the Government as, for example, in cases in which the deficiency is asserted against a transferee of the taxpayer as well as against the taxpayer himself. It would seem, however, that these situations should be exceptional.

In the course of the discussion of the case of Robert S. Maestri this morning the Secretary and the Commissioner both requested me to ask you to assign one of your staff to investigate this entire question and recommend any changes in procedure or personnel which may be necessary to insure increased accuracy in the determination of deficiencies. In the Maestri case a contested item of \$100,000 was, as I understand it, asserted to be income for the period 1925-29 and also for the year 1931, although a tax had already been paid on about \$42,000 of this amount as income for 1930. The procedure which was pursued as to this item tended to cast a serious doubt upon the accuracy of the whole determination and thus to prejudice the effective presentation of our case before the Board. There may have been some extenuating circumstances about which I am not informed but in any event it is certainly essential that we should do everything we can to increase the accuracy of our determinations. The prima facie presumption of accuracy which the Commissioner's determinations enjoy before the Board becomes useless in practice when the Board realizes that we do not believe in the accuracy of our determinations ourselves.

MEETING WITH EXECUTIVE COMMITTEE OF
FEDERAL RESERVE OPEN MARKET COMMITTEE

December 1, 1937
11:00 a.m.

Present: Mr. Taylor
Mr. Bell
Mr. Seltzer
Mr. Lochhead
Mr. Harris
Mr. Eccles
Mr. Burgess
Mr. Sinclair
Mr. Williams
Mr. Goldenweiser
Mr. Piser
Mr. McKee
Mr. Harrison
Mr. Ransom

H.M.Jr: All right, Bell, let's have the picture.

Bell: This program contemplates the continuation of the present bill program of 50 million dollars a week for December 8 and December 15, maturing in March, just refunding the usual weekly maturities; and then, beginning the 22d, in all probability issuing 90-day bills; and on December 15 having a note issue of 450 million dollars, just the amount of the maturity of the special Treasury bills at that time. That would give us balances going into December of about 605 million, going out of December of 914 million. And then in January we'd probably issue a hundred million dollars of new bills for cash and two hundred million dollars in February for cash, ...

Burgess: Of June.

Bell: Both maturing in June. ...leaving us a balance going out of January of 925 million and going out of February of 995 million. Then in March there wouldn't be, so far as we can see, any financing other than the refunding of the maturing notes of 455 million and paying off out of the tax receipts of the 400 million special Treasury bills maturing at that time.

The December note issue also contemplates picking up the 277 million Treasury notes maturing on February 1.

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Don't see much use of extending it beyond March.

H.M.Jr: Anybody want to ask Mr. Bell any questions?

Harrison: 450 of Treasury notes?

Bell: 450 million dollars of Treasury notes.

Eccles: And the 270.

Bell: And that would be used to pay off the 450 million dollars of Treasury bills maturing, and at that time we would pick up the 277 million Treasury notes maturing on February 1, offering an exchange privilege for the new notes issued on December 15.

Eccles: Well, what that would amount to, if the exchange was fully exercised - would mean seven hundred and some odd million of notes, wouldn't it?

Bell: 727 million in a sense refunded.

Eccles: Yes, be no new money taken out of the market.

Bell: That's right.

Eccles: And you'd start issuing June bills in January - a hundred million for January and two for February.

Bell: Yes, about the middle of January, I should say. That would be six issues from the 15th of January to the end of February.

Eccles: And then on the 9-month bills you'd

Taylor: 90-day.

Eccles: ... 90-day, commencing on the

Bell: 22d of December.

Eccles: 22d of December. That would start doubling up the 90-days ...

Bell: March 23.

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Eccles: Start doubling up, wouldn't it - I mean 300 million then for a period - no - no, you'd be through issuing the June bills....

Bell: That's right.

Eccles: ...before that time, so it would be just 200 million ...

Bell: No, just a hundred million a ...

Burgess: Is 300 million enough for the June tax date?

Bell: I think so, yes.

Burgess: You think that will take care of the money market. You could of course put out another hundred million there if you need the money.

Bell: That's right.

Burgess: You've got that much leeway.

Eccles: Does this contemplate any payment for gold or any receipts from gold exports? Is it taken account of in the Treasury figures?

Bell: It contemplates an expenditure of 50 million dollars beginning in February for gold, 60 million dollars in March.

Eccles: Anything in January?

Bell: Nothing. Prior to that it's a wash.

Eccles: Just washes out.

H.M.Jr: Anybody want to ask Mr. Bell anything else? Before I call on Mr. Burgess - I haven't had a chance to read that letter of yours this morning; I was going to ask you if you'd read it, if you don't mind, out loud.

Burgess: Which one is that?

H.M.Jr: Well, the one you gave me, or else a summary.

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Before I get on that - I mean as to how the market feels and how you feel - I'd like to ask if between now and the 15th of March the Federal Reserve System has anything in mind which will affect the Treasury financing one way or the other.

- Eccles: Between now and what, did you say?
- H.M.Jr: 15th of March. I mean whether the Federal Reserve System proposes anything one way or the other which would affect the Treasury bond market - I mean Treasury - when I say bonds I mean Treasury market for Treasury issues.
- Eccles: Well, of course, that's quite a long way off. All you want to know is, is there anything at the moment that we can ...
- H.M.Jr: Well, I mean we're taking - we're being very frank with you people. I mean we've got to make commitments from now until the 15th of March and I'd like to know whether the System or the Board - anything that they're contemplating which will affect the Treasury issues. That's a fair question.
- Eccles: Well, it was my - I know of nothing that would - that would certainly affect them adversely in any way.
- H.M.Jr: Well, is the System - what are they contemplating doing after this issue is out of the way? I mean are you going to sell Governments, are you going to buy Governments, are you going to do anything about reserve requirements, are you going to do anything about the stock exchange?
- Eccles: I wish I knew, but when you've got 12 men to deal with I can't predict what they'll do.
- McKee: Mr. Secretary, do you have in mind some major operation?
- H.M.Jr: Nothing - I'm not trying to spar, not trying to be smart. You people come over at our invitation and we tell you everything that we've got in mind that

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will affect you; then we work together. And I think it is only fair that I ask the same thing. Have you people got anything in mind which will affect us? I mean I'm not ...

- McKee: I understand. But what I meant in my question to you was whether or not you're speaking of a buying program that may be necessary to ease the situation or whether you're thinking of some major operation.
- H.M.Jr: I don't know; I'm just asking, is there anything that you people are thinking about which we ought to know to help us in making up our mind? I mean because, after all, while we could sell this issue, it is my responsibility to see that the thing stays sold. See what I mean? I just don't want to put out something and have it go sour. You people might have something in mind - you've been meeting for a couple days - which would affect our - the United States Government issues one way or the other, and I'm just asking if you people have got anything that you are considering.
- Harrison: I think that's a fair question.
- H.M.Jr: I think it's a perfectly fair question. I think it's a perfectly fair question.
- Eccles: Well, we've been discussing every aspect of the problem, but there's been no decision made whatever, except that we are everyone agreed that nothing should be done that would in any way diminish the ease of the money market, either now or an indefinite time in the future.
- Now, whether we should continue to operate in the market, increasing reserves through open market operations, is a matter that we haven't been able to make a decision on yet.
- What may be done with reference to reserves is another matter that has been discussed, and that is a matter that it is up to the Board to act on definitely. But we've been discussing the whole thing with members of the Committee, and there has been no decision made on that.
- But I think I express the feeling of the whole Committee

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and the Board when I say that there is certainly nothing that I am sure would be done that would be adverse to the Treasury's financial program, because we appreciate the need of cooperation and the fact that we have some responsibility in connection with this, especially where we advise with you regarding it. And nothing would be done, certainly, without consultation with you.

I don't know - does that ...

H.M.Jr: Well, partly - I mean partly.

Eccles: If somebody else here can answer it more fully, I'll be glad to have them do it.

McKee: In adding to what Marriner said, when you speak of something adverse to the Treasury position, I think that could be taken in two ways. I don't think you want to see and I don't think we want to see this Government bond market go too high again, for then it's going to come back to haunt us at a later date. Would you consider that adverse to your interests?

H.M.Jr: Well, I'd say this. If you're going to contemplate doing something to put the Government bond market down, I'd certainly want a chance to ...

McKee: Oh, I grant you that would be adverse. But do you still think on the other side it might not be considered such also?

H.M.Jr: Well, I'd like to know how you're going to - what you're going to do. What I'm trying to find out - I haven't got it yet; if you don't want to tell me, it's all right with me.

Eccles: I wish I could.

H.M.Jr: It puts me in the position - I'm going to ask questions; I don't like to do it. I'll be specific. What are you going to do about buying or selling Governments after this financing? That's a direct question.

Eccles: We don't know. We haven't decided. We discussed the thing all yesterday afternoon and we're going back

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again today. There's been no decision made. We can let you know, I think, by the end of this afternoon.

- H.M.Jr: Can you let me know in time enough so we can talk about it if we don't think that - if we don't agree with you?
- McKee: Well, it's only fair to tell the Secretary that the Open Market Committee has recessed, it hasn't adjourned.
- H.M.Jr: But I still say, can the Treasury have a chance to talk about it? It won't be decided in the afternoon and then we're told in the afternoon you're going to do it that afternoon?
- Harrison: I think the Chairman has covered it as fairly as he can in view of the situation as it stands now.

I think I can speak for myself personally without violating any confidences at all. I had thought the position of excess reserves and the whole banking situation had reached a point where there was no longer any need for the Federal Reserve System to add to excess reserves by continued open market purchases. I think that most of the things that need to be done by way of recovery are probably in the non-monetary field rather than the monetary, and that the less we do by way of picayune efforts here and there in the monetary field, the more we will do to restore confidence and make it possible for a recovery to take place.

On the other hand, I think it is fair to say that some of the others with whom I have talked in our group feel that perhaps, having bought Governments for three weeks, we should continue to buy some more before Christmas. I don't see how that would do any good except psychologically. And I feel a little what I think was implied in John McKee's question - that so far as it has any effect at all, it may be further to stimulate the rise in Government securities and widen that spread between corporate and Government bonds, which is growing now. And that's what I'm fearful of, as much as anything.

Eccles: I have felt that we should continue - tell you what my feeling is - to operate in the open market at least in a modest way, to be active in the short-term market; that it would not materially affect the long-term bonds; that they are still slightly lower than they were in August; that the discontinuance might have an adverse psychological effect.

There is in the case of an open market operation - it gives reserves to the money market banks; it does not give reserves to the country banks. The country banks are selling, and the excess reserves in the money market banks, of course, create a ready market for the sale of the longer bonds that the country banks are selling because of two reasons: First, the much lower price of agricultural products means less money going into them. And the Government reduction in relief and other expenditures will mean less money going in from that source in the country areas, which means that their deposits and hence their reserves are likely to fall. Certainly they are not rising; they are falling some now. That might make it necessary to consider a reduction of reserve requirements in country banks only, so as to create a uniform situation of excess reserves throughout the country. An open market operation readily gives excess reserves to the money market, but with the situation that I have just outlined it does not give the excess reserves to particularly the country banks. And it has seemed to me necessary to have an adequate amount - in fact, we are much safer to have too much than too little of excess reserves at a deflationary stage such as you have now.

Now, as to the decision that the Committee may make, as to the decision that the Board may make, it is entirely a question that ...

H.M.Jr: Well, when will they make this decision?

Eccles: Well, so far as the Committee is concerned, on the one question of open market policy, certainly I think we've got to make it this afternoon, and I think it will - I think the matter will be decided one way or the other as to open market, whether we will continue after the 15th or not continue.

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Whether - with reference to the other matter, that is a matter that I don't think there is any immediate hurry about. It is a matter that the Board itself is responsible for and will give consideration to and study to in the immediate future.

H.M.Jr: You mean on the reserves?

Eccles: Yes, in reference to that one aspect of it.

H.M.Jr: But on the open market - I mean we can't decide - what's the use of Burgess telling me to sell this or that or the other thing? The after-market is the most important thing, because we're in business here to stay and we're much more interested - I am - in the after-market and if the thing stays sold. Until we know here what you fellows are going to do, there isn't much use my deciding whether I'm going to sell a bill, a note, or a bond. I mean that's why I'm pressing so.

Eccles: Yes. Well, we can tell you this afternoon.

H.M.Jr: Fair enough. I mean the reason - I've got a very practical reason. I mean we offer some kind of merchandise on Monday. Well, we'll sell it. But what's going to happen two weeks from Monday and three weeks from Monday and four weeks from Monday? And Burgess is down there and it's his job to keep the market sweet for both of us.

Harrison: Is there any point, Mr. Secretary, from the point of view of the Treasury - put it this way: is there anything in the situation that would make it advantageous to you to have us buy some Government securities beginning December 15?

H.M.Jr: From the Treasury standpoint?

Harrison: Yes.

H.M.Jr: No, absolutely no.

Golden.: Mr. Secretary, you don't think that it will have an adverse influence, it will be in any way out of line with Treasury policy, if the System should buy,

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say, ten millions a week for two or three more weeks?

H.M.Jr: As far as the Treasury is concerned, it wouldn't affect us one way or the other.

Harrison: Drive bonds higher.

H.M.Jr: Pardon me?

Harrison: It would tend to drive your bonds higher.

McKee: That's what I'd just like to know - whether your advisers and yourself, Mr. Secretary, have come to a place in this Government ~~bonds~~ market - whether our absorbing more of the offerings is now not going to be more pronounced in the market price; our continuous buying - whether we haven't absorbed the slack in the market, so that any action from now on is going to be very quickly felt in the market price.

H.M.Jr: You mean it will or will not?

McKee: It will. I just wondered what you gentlemen feel about it marketwise.

H.M.Jr: Well, I'm not - after I've seen some of these people that Burgess has arranged for me, I'd know more about it. But I've only seen one crowd this morning and I'll know more about it Friday night. But I'm not - that's on an hourly basis - I'm not close enough to that; I don't know. I mean unless a fellow sits there with a half dozen telephones and

Eccles: I take it from what you said, then, it would make no difference whether we - so far as the Treasury is concerned, whether we continue an open market operation in the short-term bonds, notes, and bills, or whether we don't.

H.M.Jr: No, I didn't - no, I - because

Eccles: I think that's the impression that

H.M.Jr: No, it makes a difference in this way. If we know you're going to buy, it would make a difference certainly that Burgess and the rest of us - how we

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price the thing, huh?

Burgess: That's right.

Sinclair: Sure, affects the price right away - present state of the market.

H.M.Jr: What?

Sinclair: It affects the price right away in the present state of the market.

H.M.Jr: Surely. I mean if you people say, "Well here, in confidence, we're going to buy...." - did I hear you say bills, notes, and bonds?

Eccles: Well, short bonds; bonds with less than five-year maturities, see?

H.M.Jr: Well, anyway, you people say you're going to buy. I mean I think that Burgess and the rest of us would sit here and price it differently than if you said you weren't going to do any, or said "Well, we want to sell some." That's the thing. Wouldn't it make a difference in your (Burgess) mind?

Burgess: Might very well make a difference.

Eccles: You mean if we were going to sell.

H.M.Jr: No matter what you do. You've got a choice of three things: do nothing, buy some, or sell some.

Harrison: Another thing: buy and sell.

H.M.Jr: What you're going to do - it makes a difference how we're going to price this thing.

Eccles: Do I get it that so far as you're concerned all you want is to know so that you can price it - as to whether we do one thing or the other? You have no suggestions to make or no

H.M.Jr: Well, I don't - I don't know the situation. I don't know how your reserves look. I don't know. I mean if I knew what reserves were, sure, I'd have an

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opinion. But I don't know what facts your technical staff has laid before you, so I don't know how you're going to arrive at a decision.

Taylor: We certainly have the impression that you are not contemplating selling any of your total portfolio; you may do some switching and you may stop buying, but if you - I mean I just don't get any conversation at all that indicates any

Eccles: No, there is no thought of selling.

Taylor: You can almost eliminate the third possibility.

Eccles: That's right.

Harrison: Of course, we told the country in September we probably would sell in January.

Eccles: Permit bills to run off.

Taylor: Well, you have some changed conditions.

Eccles: That's right. We have recognized that, and we feel that there is nobody contemplating, so far as I know in fact, any idea of selling.

Taylor: Switching, sure, but not

Eccles: The whole question is whether to continue to buy a modest amount so as to be in the market, because of, first, psychological influences as much as actual, - psychological even more. The fact that we did buy 38, 40 million for a period of three weeks - and then to discontinue altogether doesn't seem to me to be warranted at this time. And another 50, 75 million over the period of the next month would certainly not - true, it would give the money market - might say it's got 400 million of excess reserves now in New York; might give it 500 million excess reserves. Well, after all, 500 million - it doesn't make much difference whether it's five or four, and they're both large excess reserves and they both make for easy money. You have easy money with 400 million and you'd possibly not have much easier with five.

But the psychology of doing this, it seems to me,

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might be - it's open to argument, I'll admit, but it seems to me it might be favorable, desirable.

Harrison: Wouldn't contemplate it after Christmas, would you, when the money comes back?

Eccles: I'd want to wait until the end of the year.

Harrison: Between Christmas and New Years you get the biggest return flow.

Eccles: Well, the question is - naturally, if it begins to build up from that source, then that answers it.

Burgess: Certainly up until that time, immediately after - a couple weeks up until Christmas, there would seem to me to be every reason for it, and justification for it.

Harrison: Well, the fact that the Secretary is interested in whether we're going to buy or not because it would influence his pricing of his issue shows that he feels it would certainly have some effect upon the prices of Government securities. Even our last purchases beginning in November - early in November, had a fairly appreciable effect, I think, upon the price of Government securities. It was more than a coincidence that they went up as they did in those middle weeks of November. And you've got to recognize that the Treasury is not increasing its debt, not putting out more bonds that we can absorb. What we are doing - we are acting, as somebody said a moment ago, on a more sensitive market than when you were increasing your debt, and I am fearful that continued operations of the System might concern you not in adversely depressing your bonds, but in artificially stimulating them to a point where you would have a problem of control. That's my case.

H.M.Jr: Well, another thing. If the Federal Reserve Board contemplated within a reasonable time - that is, some time between now and the end of the year - to change reserve requirements on the country banks, that would have an effect on the price, and it also

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would influence me as to whether we should sell a note or a bond, because - I think I'm right, am I not, Burgess, that - let's say they lowered reserve requirements for the country banks; they might buy more bonds.

Burgess: They would undoubtedly.

Eccles: It doesn't amount to much. The country banks would not buy bonds. They might hold some of the bonds they have been selling. I think it would be bad for them to buy more bonds. They've got now too large a proportion of long bonds, and if there should be a substantial depreciation at some time, it could affect them very adversely. They have practically no bills or notes; their holdings are largely bonds now, and they are rather large. It would tend to stop a sale of bonds that they hold in order to maintain an excess reserve picture. The amount involved in that case would not be great. If the entire increase of last March and May was reversed, it would only amount to 150 million.

H.M.Jr: Well, it only takes about a million dollars in a day

Burgess: They could buy a billion dollars worth of bonds on that, though, if they used it fully, couldn't they?

Eccles: No, the excess reserves don't pyramid just within country banks.

Burgess: No, but throughout the System.

H.M.Jr: Is this something you might do between now and the end of the year?

Eccles: Well, I - it is my personal opinion that it is a matter that we should possibly delay until after the first of the year. But we'll get a little more information on the development of the picture. The excess reserves of the country banks have not diminished; they have stayed about 300 million. They are - by percentage they are still large.

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- Viner: Are they well-distributed?
- Eccles: Pretty well, yes. The difficulty is that their desire to maintain large reserves tends to cause them to sell bonds in order to maintain a very excessive reserve picture. That has been a good thing for the market, in a way, because, with the high excess reserves in the cities I imagine bonds would have gone up very much higher and faster, which might have been bad, if there hadn't been that amount of some selling by them to the market. That has tended, I think, to stabilize the bond market, because one group was buying and another was selling.
- Harrison: Mr. Secretary, may I ask a question which I hope you will frankly say you don't want to answer; - but are there any funds in the Treasury which are apt to influence the market in any way between now and the first of the year?
- Bell: I don't think so.
- H.M.Jr: What? Do you know of any?
- Bell: Investment funds, you mean?
- Harrison: Yes.
- Bell: No.
- Burgess: Or disinvestment. We're all through this sale of bonds, are we?
- Bell: There is a 25 million dollar sale of Home Loan Bank debentures which comes in today, probably less than 12 million of which will be invested, but not until after this financing is over.
- Burgess: But you're not going to sell any more bonds from your accounts probably.
- Bell: There isn't anything else in there.
- Eccles: The F.D.I.C. And these funds have got the cash.
- Taylor: Well, they can get cash from special obligations of one kind or another. I don't think that there

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is really much possibility of anything that you would consider a movement one way or the other in any amount.

Bell: That isn't big.

Taylor: Pardon?

Bell: That isn't big.

Taylor: No. I mean our available balances in Postal and F.D.I.C. they want to keep uninvested at the present time, and they are not very large.

~~Harrison:~~ There is no need for them to sell to get further balances, is what I'm asking.

Bell: As a matter of fact, the F.D.I.C. will have assessments coming in in January.

H.M.Jr: Does that answer your question?

Taylor: But all those funds recently have been invested right along, as they have gone along. We haven't held back any.

McKee: Mr. Secretary, maybe I'm too conscious of this market situation because I feel that if the market goes much higher, you're going to bring out a lot of selling; if we can keep it from going too high, that these bonds are going to remain where they are now located. Now, I may be entirely wet on that, but I think that we all should be interested to see that we don't disturb the Government bond market too much. And I think we're running a risk by letting the prices go too high. Now, maybe I'm alone in that thought, but I think there is a risk there that you are running, and we are all assuming a responsibility if and when the thing gets out of hand. And by continuing buying - while I am in sympathy with easing credit at a time like this, it is a question of whether you can do much of it through a bond-buying program, whether you can do enough to get the effect you need. I'm speaking out in the open, and anybody else who has any other idea - it's all right.

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- H.M.Jr: I don't think there's any question that when you fellows keep increasing your portfolio it has an effect right straight through the whole series of Governments. You may be buying bills, and if you buy ten million dollars, increase your portfolio by ten million dollars, it has an effect on the long-term Governments as well as the intermediate market and everything else. I think all you've got to do is just look at the prices.
- McKee: The one question Mr. Harrison asked is, if and when - I know you've been investing right along - your trust funds - and if and when you had some liquidation in the somewhat reasonable future, that you could probably offset a rise in bond prices.
- Now, we're not worried - I'm not personally worried about the cheapness of the short-term paper, but I am worried about the bond prices, because that's the thing that is going to affect the majority.
- H.M.Jr: Well - I mean I'm not sure - I mean the last week that you people did that I thought it would have an effect - was too close to our financing, and if the decision had been mine, I wouldn't have done it, but you people did it and that's that.
- Eccles: It didn't have any appreciable effect, though.
- H.M.Jr: The only thing that you people - I don't know whether you know about it or not - is that during the - oh, I don't know the exact period, but sometime during the last 30 days we have sold ten million dollars worth of 2-7/8s out of the Stabilization Fund, and we have held them a long time and I wanted to get that fund in such shape that if there was another sharp break we'd be in a position to buy, because our Postal Savings and F.D.I.C. are not in a position to buy. So we have sold ten million of that, so we are in a position - and if there is another sharp break and they should go below par again, why, we are in a position to buy them back.
- Eccles: Speaking to what Mr. McKee expressed, whether we buy bills in the market to give reserves to the market, whether reserves are given to the market in most any way, it will tend to have the effect of

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increasing bond prices. And we think of Government bonds, but look at all other high-grade paper. And the easy - the recession in business, with the absence of investment demand, has tended to put up prices on all of your prime - not only Government bonds, but on other - on your Triple A securities and your prime paper generally.

Harrison: They haven't gone up with Governments, have they?

Eccles: Well, they've gone up, George. They have - now, not like the Government - not like Government bills and Government notes, but they have gone up. Now, it's just a question of - true, you could sell securities and put them down.

Harrison: That isn't the point. I don't think any of us want to sell in January as we see the situation today. The only question in my mind is whether there is any economic or monetary reason which would justify our adding 50 or a hundred million to excess reserves in the month of December right after a Treasury financing, that would offset the possible risks; and by risks I mean artificial stimulation of the Government bond market, which goes up for two reasons: First, if we increase excess reserves, as you point out; and second, because we are buying a particular commodity.

Eccles: Well, that was the same argument last April when we went into the open market. Same argument used in February - that the money market did not call for it. And yet we did act, and we certainly didn't act too soon; if anything, it was too late.

Lochhead: When we had a falling bond market some time ago, the Board sold some of their shorts and bought long-term Government bonds. I wonder if any consideration would be given, if your bond market was going up too high, to selling out your long and going back to short. Outside of your excess reserves, that is one way you have of controlling your long-term Government bond prices.

Burgess: I think we ought to cover that in our authorization.

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- McKee: I have had that in mind. Just wondered what the Treasury could add to that, in assisting to do that.
- H.M.Jr: We don't want to be ex-officio members of your Open Market Committee.
- McKee: Still thinking of your future as a borrower - the largest borrower in the world, or in the United States.
- Burgess: Make it the world, John, it's all right.
- Eccles: But you did sell ten million during this period, which was a good thing at a time when the market was strong; so that, after all, it had the effect of being an ex-officio member anyway.
- Harrison: Opposition member.
- Eccles: No, I think it was very helpful.
- Harrison: Offset what we were doing.
- Eccles: That was all right. They were operating in the long-term market and we were operating in the short-term market.
- Lochhead: Two things: one, the long-term Government bond market; the other, the supply of credit.
- Taylor: An unconscious switching operation.
- H.M.Jr: Well, as a matter of fact, it in no way offset what you people were trying to do.
- Eccles: No, it didn't. It was a good thing. Helped to stabilize the long market. And it seems to me that that might even be done to a greater extent, because it certainly is a good thing to get cash at a time when the market is unusually strong in the long bonds.
- Harrison: All I meant, Marriner, was, whether it's offsetting it or not, it does, to the extent that they sell, offset the amount of excess reserves we put in, and if it is for the Stabilization Fund account, those excess reserves are not put back by Treasury expenditures, as you argue.

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Eccles: Well, even that's all right.

Harrison: Therefore, I just raise a question: if the Treasury is going to do that, and it's a good thing, and I'm not objecting to doing it; I would have done it too had I been in the Secretary's place - the question raises itself in my mind, then, why are we buying, because we are buying short-time stuff that's already been driven down to ten and which certainly needs no support; we are not buying to put in excess reserves, because the Treasury takes them out to the extent they sell; and I don't see why we're buying except to give an impression. As far as an impression at this time, the impression isn't necessary so far as the bond market is concerned. Now, I agree with the Secretary that that is more of an argument for the Open Market Committee than this meeting.

Taylor: And also it's academic, because the further possibilities along those lines aren't in the picture.

Eccles: You mean - what lines?

H.M.Jr: Well, we've only got five million more.

Taylor: What we could do further. The only thing we could do would be to make some switches in our investments, which is something we very seldom do.

H.M.Jr: I want to say now - there's no mystery - if there is again a boiling market and the 2-7/8s are jumping two or three points a day, we're going to sell the other five million we've got. I want to get down to a basis of ten million. Then when those things go bad - and knowing how you people feel about long-term Governments, I think you'd be tickled to death to know there's 15, 20 million dollars purchasing power for long-term Governments. Save you a lot of weeping. So - I mean that's the whole object; it's just so if and when things should turn for bad, why, we've got 15 or 20 million dollars purchasing power to buy long-term Governments. And as I say, now, if the 2-7/8s jump two or three 32ds a day - they jumped one day 9-32ds - why, we'll sell those five million 2-7/8s. But the ten million 2-1/2s - we'll hold those until at least they cross par. Now, you can tell me when they'll do that.

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Taylor: That's our maximum possibility.

H.M.Jr: The maximum possibility is that we can sell, or will sell, and - I mean at any time there is another boiling market for the 2-7/8s. We own five million and we'll sell those on a stiff rising market. And outside of that we've got nothing. And that would follow out McKee's thing: at least to keep the thing from going up too fast. But that isn't why we're doing it; we're doing it because we feel that some time, as sure as the sun rises, there will be another period where nobody wants long-term Governments, and we're there with 15 or 20 million dollars of purchasing power. And - I mean that's what we're doing ~~it~~ for. May be three months, six months, or a year, but we'll sit there and wait until there is a bad crack in the long-term Governments, and we're there to relieve you of that embarrassing situation.

Harrison: I wouldn't want you to think that anything I said was critical of anything, because I would have done - I think you're quite right. My position is more one of envy that we can't be doing the same thing you are.

H.M.Jr: This is getting too subtle for me.

(Hearty laughter)

This conversation is getting beyond me. Now, if everybody is feeling all right - now, Mr. Burgess, if you'll give these people a survey of what our customers would like as of today.

Burgess: Well, first a word about the changes in the market. Since the middle of September, when we did the last financing, there's been quite a change in the market. Not so much in price; the prices are still up somewhat, both notes and bonds. But there's been a shift, I think, in willingness to buy.

Both in June and September we offered a choice between two different kinds of notes, a short and a longer note. We felt that was necessary to meet the market. I think that the gap between short and

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long notes has been bridged; that is, people who before would limit their purchases to two or three year notes, or four year, now think of a five-year note as something they can take in their stride without the same hesitation.

Similarly, there has been a shift of interest into bonds. We talked about bonds last time - this is not the Burgess plan, Mr. Secretary - we talked about bonds, perhaps in a rather academic way. You can think about it somewhat more seriously now, because there has been a shift of interest.

I would say that, as far as our purchases had an effect, that's the most noticeable one, that it did lead to more interest in the bonds. The savings banks came in again after being out for a long time and made some purchases, and banks and others have showed some interest in long bonds - the first time those long bonds have moved at all; and there's been more general interest in the shorter bonds; some of the banks in New York have been buying them. Now, of course, you've got to discount that slightly because of our operations; the psychology of that made them willing to buy bonds more than they had, and you have to discount that a little; it's one of those temporary waves, but I don't think very much. The market hasn't changed a great deal in actual point since we did our buying.

But I think the Treasury can feel free to sell anything up to eight years, can run that scale, and determine the thing on the basis of its own requirements and on the basis of the price and of the effect on the capital market, which I think is very important at the present time. Now, there are two distinct views, you'll find - you probably have found already - on the part of

H.M.Jr: No, I haven't really got into this thing yet. No, I haven't got - and I'm sorry that we had - we had a tax case this morning.

Burgess: That's quite all right.

H.M.Jr: Which I had to take care of. And no one could do

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it but myself. And that's what tied me up. This was one case where the taxpayer got a dirty deal; so it took the Undersecretary, the General Counsel, the Commissioner of Internal Revenue, and the head of the Income Tax Bureau - we were at it for an hour and a quarter this morning. That's what tied me up.

Burgess: Well, that probably paid.

Well, you'll find there's a distinct divergence of view in the market. There are a certain number of people that say that the Treasury has a very large short-dated debt, that it would be sound financing whenever you get a chance to borrow at somewhat longer terms and push the thing ahead, leaving your borrowing capacity at short term larger for anything that may occur. They also say that psychologically there would be a favorable effect on the capital market. They say if the Treasury is afraid to go out beyond five years, why should anybody else take the risk? Of course, the capital market has been practically closed for six weeks and we are all anxious to see it opened up.

Now, on the other hand, you will find a number of equally vigorous exponents of the theory that the best thing to do for the capital market is for the Treasury to keep out of it and starve it and leave the thing free for corporate issues. I think you can toss that up in the air and call heads or tails and one is probably about as good a guess as the other.

In view of the necessity for discounting a little bit the present market in view of our operations, the safest, most conservative thing to do would be to put out a five-year note. You could sell it at 1-3/4, I think, on the present market. Might change in the next few days. But I am equally confident that you, if you wanted to, could sell an 8-year bond.

Now, that is without going into details of what different people think, and so on. We can go into that later. I think in our discussion this morning the Governor and others favored the note, felt that was wiser.

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- H.M.Jr: Well, inasmuch as this really was the purpose the meeting was called for, I think we ought to go around. I do think what's happened the last 55 minutes was illuminating and helpful to me, and I think some of you people got some stuff out of your chest, which didn't really affect the Treasury, but - well, you all look much happier.
- Eccles: I never have anything on my chest. I have to get it off.
- Harrison: That's the trouble with both of us.
- Eccles: Yes, we ...
- H.M.Jr: Well, as I say, so let's go around, and I'd be more than pleased to hear what you people have to recommend. Who wants to start?
- Sinclair: Well, I'm next to the Stenotypist on this side. Shall I start?
- H.M.Jr: Please.
- Sinclair: I think in Philadelphia it is awfully hard to get it clearly analyzed. There is considerable sentiment in some of the banks, some of the insurance companies and savings funds, for an 8-year bond. I think we reflect there probably the two points of view.
- H.M.Jr: You say there is?
- Sinclair: There is some sentiment. I think we reflect probably pretty well the two points of view that Dr. Burgess has outlined. I think at some stage of the game that the bond ought to be given serious consideration. Personally, I am not too affirmative in that at this time. I think that the five-year note would be probably the most conservative thing to do, but I don't think we ought to overlook the possibility at some stage, whether it is now or later on, next year - the bond possibility, in accordance with conservatism and the problems that the Treasury is going to have in refunding this shorter debt. I talked last night when I was in Philadelphia to one of our younger bankers who is

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pretty close to the money market, watches things very carefully. He was very affirmative on the 8-year bond. I think one of our large insurance companies would be in favor of that, and one of the other large insurance companies would be in favor of the five-year note, - much more. So I think as far as we are concerned, you can count on the two types of demand.

H.M.Jr: Insurance companies, five-year note?

Sinclair: Yes, one of the large insurance companies. Last year, last spring, it was absolutely - take nothing over a year or year and a half. But I think they have spread out a bit, would spread out into the five-year note.

One thing we have in Philadelphia in large bulk is a lot of trust funds. Their problems of investment in the longer market are difficult from their point of view, and I think the 8-year bond would be a real attraction to them.

Whether or not the increased cost to the Treasury would make it worth while to spread the difference from five to eight years is a problem you'd have to decide. That's all I have to say.

H.M.Jr: Thank you.

Professor Williams.

Williams: I favor the note. I don't know much about what the market would take just now, but I think that is secondary to the questions that might arise later on. I think we have a very unstable interest rate structure now, and our chief question, it seems to me, is to do what we can to prevent its becoming more unstable than it is.

Now, one of the elements in that is the banks' holdings of bonds. The more bonds they hold, the more possibility there is of a reversal of price movement, which I think can have a very bad effect not only in the Government bond market, but very generally in investment markets related to refunding

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and new capital issues and everything else. And I think it is imprudent - really bad policy at this stage to issue longer-term securities. I don't know just how to weigh the difference between five years and eight years, but in general I am in favor of the shorter maturity, for that reason.

And my attitude toward the other question which is out is very much the same - that it would mean danger now. We have easy money. The main danger is of making this unstable interest rate structure more unstable.

H.M.Jr: How do you mean?

Williams: Well, under conditions like these, there are elements of risk and so on affecting the private securities, opening up a gap between the interest rates on public securities and the interest rates on private securities. And the more that gap spreads, the more danger there is of a setback and some internal confusion, disorder. People ask themselves which rate is out of line with which, and as your Government security prices go up, that is increasingly a question, and the possibility of setback increases.

Now, those are two topics - different - but they are related to each other.

H.M.Jr: But they both point towards the five-year note.

Williams: I think so. That's all I have.

Golden.: I don't think - I don't feel very strongly between five and eight years. I do lean somewhat towards the note too, because I think that if there is money for bonds, it would be desirable to have it go into corporate bonds; if there is investment money, that there ought to be an encouragement for the use of it in that capital market, which does need some support. That's all I have to say, Mr. Secretary.

Lochhead: I think the present market favors a five-year note; think it would be much the more natural financing right now.

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Ransom: The arguments in favor of the note seem to me to be much stronger than those advanced for the bond, Mr. Secretary. Weighing the two of them as I have heard them over the past two - past week, I have a very definite feeling that a strong argument could be made in favor of the note.

H.M.Jr: Jake?

Viner: (No comment)

Seltzer: We have a pretty heavy concentration of maturities in that medium-term bond, and I think too that we pay too much interest for - the spread between the ~~rate~~ on a five-year note and the rate on an 8-year bond would be too great. And I'd rather reserve a bond issue for a time when we can float a longer term bond issue, get away from that heavy concentration of maturities between '45 and '49. So I don't think we'd gain enough between a five-year note and an 8-year bond to go into the bond at this time.

H.M.Jr: Is that all, Larry?

Seltzer: Yes.

Taylor: Note.

H.M.Jr: Note.

Sinclair: To the point.

Piser: I have talked to a number of banks and other investors over the past month, and the demand seems to concentrate pretty much on the five-year period. There are some of them who would be willing to purchase a longer issue, a 7- or 8-year bond, but a number of those that I talked with said frankly that they would purchase them solely for the premium, that they would plan to sell and take their point profit soon after the issue. And practically all of them agreed that ten years was the maximum, that they wouldn't even want to speculate in an issue of more than ten-year maturity. So with that background it seems to me the five-year note would be desirable.

H.M.Jr: McKee?

McKee: I favor the note, because I think the short-term market needs a supply more than the long-term market. I'd like to approach it from that angle.

H.M.Jr: Is that all? So snappy around here.
Dan?

Bell: I favor the note for reasons expressed by Larry Seltzer, I think, from the standpoint of the Treasury.

H.M.Jr: Is that all?

Harrison: I never like to say anything here except that I preface it with my usual statement that from the point of view of the Treasury I think it is ultimately desirable that you convert as much of your short-time debt into long-time debt as is possible. But I also agree that you do not accomplish that by an intermediate shift from five to eight years. I don't think that is enough to conform to the principle that I had in mind.

I think that Burgess is right; from the point of view of the capital market, whether it would be better to have the note or the bond is pretty nearly a toss-up. On the whole, I think I would favor the note, as I see things today. If, however, the Federal Reserve System does undertake an open market program of purchases, I would seriously consider the bond as one of the offsetting factors to the continued rise of long-time bond prices.

H.M.Jr: Is that all?

Harrison: That's all.

Eccles: I favor the note very strongly, for the reason that the note will be - much larger proportion would be taken by the banks, and in so doing it would create new money through credit or it would stop at least the diminishing of deposits through the paying off of obligations. In other words, the banks own bills and if the bills were paid and they didn't take the new issue, it means that the total deposits diminish. That is undesirable. Therefore,

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I think we should give - make an issue that the banks are likely to take. They would be much more likely to take the note issue. That leaves, then, the private funds seeking investment, and it would therefore help the capital market because you wouldn't be supplying them with a bond. And I feel pretty strongly about the matter.

H.M.Jr: Harris?

Harris: The note.

H.M.Jr: What?

Harris: The note.

H.M.Jr: You (Burgess) going to say something now?

Burgess: No, I'm all through.

H.M.Jr: Note? Is that what you said?

Burgess: I would incline to a note, yes.

H.M.Jr: What you and I have got to do for the next three days is find out why we shouldn't sell a bond, then. Otherwise, there's no excuse to see anybody, is there? What?

Burgess: Oh well, you'll get something from it.

H.M.Jr: I hope so.

Well, thanks very much. And then, if and when the Open Market Committee makes up its mind, I'll be amongst the first to know it?

Eccles: Not amongst the first. The first.

December 1, 1937.
3:47 p.m.

H.M.Jr: Hello.
Herbert Fels: Yes, Henry.
H.M.Jr: Herbert?
F: Yes, Hello.
H.M.Jr: Henry.
F: Yes sir. I hope I don't disturb you.
H.M.Jr: No.
F: Look here. Mr. Hull had to rush off, right after lunch, to a meeting of the Board of the Pan American Union, and seemed to think that you wanted an answer from him pretty speedily on that question you asked him in regard to Mexico.
H.M.Jr: He called me.
F: Yes.
H.M.Jr: Himself, this afternoon. About half an hour ago.
F: Well, then he got in ahead -
H.M.Jr: Yes.
F: Ahead of me.
H.M.Jr: And I told him we'd do nothing on Mexico this week, but I'd take it up with you the first of next week.
F: Yes, he told me that, but he seemed to have the impression, I don't know - it had been posed to him or maybe he posed this question in his own mind, he gave me the impression that you asked him - that suppose these fellows said they'd actually put up that gold and silver -
H.M.Jr: Yes.
F: As collateral.
H.M.Jr: That's right.

F: Well, I said then, since he put it to me in the form of a question, that if they did that, I thought that - that merely showed to him advance on - on specie, and that brought it much more closer to things, I understood that you had done before.

H.M.Jr: Exactly.

F: And would be a much simpler operation for you.

H.M.Jr: That's right.

F: And for our part I didn't think we should say anything, and leave it up to you.

H.M.Jr: Well, but in order to help you out, I thought I'd just stall even on that this week. I didn't think I'd answer them at all.

F: All right.

H.M.Jr: And unless there's any pressure from the State Department, we won't say peep this week on Mexico.

F: Right.

H.M.Jr: See what I mean. I don't think he got that - I said he -

F: He didn't seem to have it clear at all.

H.M.Jr: Well, what he said to me was this. He said, "Now I understand the technical reasons and so forth why you can't do it this way."

F: Yes.

H.M.Jr: "The way they put it up to you." He most likely explained it to them, and I said, "Yes, but - they'll come back and say how can you do it, and I'll pay the way, we did it before, and that is that you put up the gold and silver on deposit."

F: Yes.

H.M.Jr: As security.

F: Yes.

H.M.Jr: Then I say if they do that we've got to say yes.

F: Well, that's what he was testing me out on and I luckily gave him the same answer.

H.M.Jr: But I said, "Rather than put it up to them, and have to say 'yes', in order to help you out," I said, "I won't do anything before Monday, and the excuse I give is my Government financing, so you people have got to square me with Josephus Daniels."

F: Well, now -

H.M.Jr: You and I are together.

F: All right, I'll -

H.M.Jr: You and I are together. Mr. Hull, I don't think quite had it. There's no reason why he shouldn't.

F: Well, now you want us to get some word down to Daniels.

H.M.Jr: Simply tell him that I think, as a matter of courtesy, he should send a cable to Mr. Daniels, simply saying that the Secretary of the Treasury is so occupied this week getting ready for his financing on Monday, that he can't take on any outside matters before next Tuesday.

F: Right.

H.M.Jr: That stalls the thing over a week, you see.

F: I'll do it.

H.M.Jr: But I think Daniels is entitled to an answer.

F: Right sir.

H.M.Jr: Now, did that places the statement

F: Completely, and on the other hand I think if and as it comes up next week, and they actually offer you that specie collateral -

H.M.Jr: We got to go ahead.

F: You've got to go ahead with it.

H.M.Jr: But we're absolutely together.

F: Right.

H.M.Jr: But I won't see the Mexican Ambassador before next Tuesday, and when I do, I'll have you - see you first, and then I'd like to have you here when I do see him.

F: Right. May I ask you one other question, again, the Secretary keeps asking this to me in a rather vague way. You haven't decided on the renewal of those agreements, the silver purchase agreements, on that you've reached no decision, yet?

H.M.Jr: I - I haven't even mentioned it to the President of the United States and won't until he gets back.

F: Right, sir.

H.M.Jr: Now, we won't take it up until the President gets back.

F: All right. Now on Far East.

H.M.Jr: Yes.

F: Two things, first we have had no further confirmation at all -

H.M.Jr: Yes.

F: From the Far East regarding the idea that they were going to - they might declare war.

H.M.Jr: Yes.

F: Nothing at all. On the other hand in response to Mr. Hull's cable, wired to the President, asking him how promptly we ought to act. The President wired back saying 'Get all the proclamations in readiness for me, and I'll sign them and send them back.'

H.M.Jr: I see.

F: That doesn't mean that they necessarily go out at once.

H.M.Jr: Yes.

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F: But I read it to mean that he wouldn't delay any longer than might be necessary to make sure of the situation, you see?

H.M.Jr: Yes.

F: Which indicates to me that his disposition would be to move fairly promptly.

H.M.Jr: I see. Well, now, but nothing's happened.

F: Nothing to - no confirmation that they are going to declare war.

H.M.Jr: I see.

F: But an indication that if they do, the President's inclination would not be delayed very long before announcing the Neutrality Act in effect.

H.M.Jr: Well, what I've got to do is to make up my mind what I want to do about China.

F: That's what - I thought that might -

H.M.Jr: And I think maybe we ought to tell China we've taken fifty million ounces of silver from ^{over} the last four or five weeks, and I might tell them informally now, we may take another fifty million from them you see.

F: Yes.

H.M.Jr: And so I could say well we did that before in cases like that.

F: Well, that was in my mind, too.

H.M.Jr: And I may do that tomorrow or Friday.

F: Yes. Well - well, that's what was in my mind.

H.M.Jr: I'm going to talk -

F: I think that's what was in the Secretary's mind.

H.M.Jr: Well, I'm going to talk to Taylor and Lockheed tonight about it.

- 8 -

F: All right.

H.M.Jr: See?

F: Yes.

H.M.Jr: And the other thing, while I've got you, may interest you, we haven't got the details yet, but on the telephone, but France has negotiated a loan from Holland, and as I understand it, I haven't got all the details yet, but it looks as though Holland wants to buy fifty million dollars worth of gold from us, see? - In order to take the place of the gold which they're shipping to France, which is a very nice piece of business for us.

F: That's - I was going to say, it is, isn't it?

H.M.Jr: When I have the details, I'll ask Lochhead tomorrow to give you a ring and explain it to you. The facts, on account of it being on the telephone was a little buzzy.

F: Yes.

H.M.Jr: But I - I thought that was a nice piece of business.

F: I think - I think it's very nice.

H.M.Jr: Well, I'm going to move on China - try to move this week, I think, maybe tomorrow, we'll see.

F: Uh-huh.

H.M.Jr: All right.

F: Thank you.

December 1, 1937.
4:30 p.m.

H.M.Jr: Hello.

Operator: Mr. Parkinson.

H.M.Jr: Hello.
Mr.
Parkinson: Hello.

H.M.Jr: Mr. Parkinson?

P: Yes.

H.M.Jr: Morgenthau.

P: Oh, hello, Mr. Secretary.

H.M.Jr: How are you?

P: Very well, thanks.

H.M.Jr: I'm sorry you're going to be tied up Thursday and Friday.

P: But it - it's just this week that we have both the President's - the Vice-President's meeting, the Insurance Commissioners meeting, and I also have the Rockefeller Foundation annual meeting.

H.M.Jr: Uh-huh.

P: But notwithstanding all of that if it's really - be of any service to you I can come down Friday morning.

H.M.Jr: Well, that's very nice but I think maybe you can do some work for me up there.

P: All right.

H.M.Jr: This is what I'd like. If you, in circulating around, would ask your other Presidents - other companies, what kind of a Government securities they're in the market for.

P: Yes.

H.M.Jr: See?

P: Yes.

H.M.Jr: I mean -

P: Right now, you mean.

H.M.Jr: Right now, we would offer it Monday for payment on December 15th, see?

P: Yes.

H.M.Jr: And we haven't got your December 1st figure, how much cash all these insurance companies have on hand. I think the last figure we had was September, which was around six hundred and eighty million.

P: Yes.

H.M.Jr: And I'd - I'd kinda like to know whether there were thirty eight or forty companies, the life insurance companies, what their cash position was December 1st. And then as I say, what would they buy - I mean I can't get out a penny or two and three quarters, you see?

P: No. Well, I tell you, I'll have a fairly good chance to do that tomorrow and - and Friday, because they'll practically all be here.

H.M.Jr: That's what I thought.

P: At this meeting.

H.M.Jr: And then could you call me Friday afternoon?

P: Not later than Friday afternoon.

H.M.Jr: Yes. And would you just sorta sound them out?

P: Yes I will.

H.M.Jr: And then if you'll also let -

P: I think - I think I could find more about the first question you asked than the cash position.

H.M.Jr: Uh-huh.

P: That might be a bit hard.

- 3 -

H.M.Jr: Well -

P: To get - to get a really accurate idea.

H.M.Jr: Well, that -

P: But I might get something that would indicate whether it had changed much since - since September.

H.M.Jr: Well, that - that would be just as useful if it's gone up since then, or down.

P: Yes.

H.M.Jr: And also the - how hungry are they.

P: Yes.

H.M.Jr: See?

P: Yes. We're all kind of hungry.

H.M.Jr: Pardon me?

P: We're all kind of hungry.

H.M.Jr: Uh-huh.

P: For securities, I mean.

H.M.Jr: Well, one - one - I needn't tell you, but right now, an eight year two and a half would be about - have a one point premium, I mean, that's what -

P: Yes.

H.M.Jr: Suggested,

P: And that's something to shoot at, and see what they think of it?

H.M.Jr: Yes.

P: All right.

H.M.Jr: And the other thing is, would they all be interested in a five year one and three quarters.

P: Five, one and -

H.M.Jr: Yes.

P: All right. I'll use those to shoot at.

H.M.Jr: Thank you very much.

P: Not a bit.

H.M.Jr: And I'll hear from you Friday afternoon.

P: Yes, surely.

H.M.Jr: Thank you.

P: All right.

IMPROVING FEDERAL ADMINISTRATION

Speech delivered before
a meeting of some members
of the House of Representa-
tives on December 1, 1957.

December 1, 1937

I have just been rereading the life of Andrew Jackson which was written within two years of his death, which my grandfather bought from some book agent at the time and which to me, as a small boy, was the most attractive book in the limited supply of reading material we had there in the woods of north-central Indiana. The picture of what the Federal Government was like when Jackson was President is admirably portrayed in this old book from a mere reading of what his messages to Congress said and what Congress did about his recommendations. When he told Congress of the final payment about to be made which would wipe out the entire national debt, with evident pride, he said there would be over \$40,000 left in the Treasury. Less than 30 years before, Jefferson wrote, "We are a rural farming people. We have little business and few manufacturers among us, and I pray God it will be a long time before we have much of either."

Our early Federal Government in actual operation comprised little more than the Congress to enact laws and the Courts to interpret and enforce them. The Executive branch of the Government was small and the amount of public business it had to handle was relatively slight. Contrasting that picture with the picture of the Federal Government today, the outstanding difference is not so much the expansion of the field of Federal legislation or the enlargement of the jurisdiction of the Federal Courts, as it is the enormous development of the Executive branch of the Government. This three-fold enlargement of the sphere of Federal rule has come about for reasons so often stated

that they are trite; and, while all thoughtful men would avoid the unnecessary enlargement of Federal functions, the man who hopes for a return of the former simplicity of Federal Government is wholly out of touch with contemporary realities in the fields of modern communication, commerce, finance and industry.

Reverting to the stupendous growth of the Executive Branch of the Federal Government, it now touches and affects the intricate complexity of modern life in such a multitude of ways that one of the major problems of our time is the improvement of our administrative processes and techniques, not by a spurious simplification, the complexity of our problems precludes simple answers, but by devising new and improved administrative methods and procedures. In the matter of administration, we still follow old forms for the most part. In few fields of human endeavor has there been less inventive thinking. If Federal administration is not markedly improved, it will become a serious retarding factor in the business and life of the nation and important parts of it will collapse of their own weight.

My experience in the administrative end of the Government during the war and again since March 1953, has suggested numerous points at which important improvements in Federal administration might be made, but there are two basic aspects of this many sided problem to which I should like to direct your attention. One is the problem of preventing an overgrowth of the bureaucracy required for Federal administration and to keep at a minimum the extent to which Federal officials must interfere in the operation and management of private affairs. The

other is the problem of letting the citizen know what the Government expects of him at the time when he needs to know it in order to plan his affairs and go on about his business with reasonable assurance.

Simplified Administration

Granted a certain quantum of Federal law which has to be administered, then, I believe, the one consideration which will do most to minimize the Federal bureaucracy necessary for such administration and the interference in private affairs involved in that administration is the choice between two broad types of administrative implementation of legislation. If Congress says a citizen shall do so-and-so, it may, to effectuate its will, set up what I would call the traditional administrative mechanism. This would provide the personnel and procedures for watching how citizens act and detecting their infractions of the rule laid down. It would provide penalties for such infractions and, finally, administrative and judicial machinery for enforcing such penalties. This traditional type of implementation necessarily involves large personnel, complicated administration and wide-spread interference in private affairs.

The other type of implementation puts the initiative on the citizen. This minimizes bureaucracy and governmental intervention in private affairs. One or two simple examples will make clear the enormous practical difference between these two types of legislative implementation. Suppose a given legislative body wants all banks to close at a given time, say 3 p.m. It might, adopting the traditional method, secure a certain degree of compliance by making it an offense, with penalties, to remain open after that hour,

but this would involve personnel and governmental machinery necessary for inspection, detection and enforcement of such penalties. If, on the other hand, that legislative body provided that banks might not debit their depositors' accounts with defective checks if cashed after 3 p.m., little, if any, policing would be required to secure uniform closing. Again, assume a policy to discourage marriage below a certain age without parental consent. Legislation might provide, with an appropriate penalty, that it would be an offense for a county clerk to issue a marriage license to those under the stated age without parental consent. If, on the other hand, it gave the parent of a child under age the right to collect \$100 from a county clerk improperly issuing a marriage license to youngsters, the legislation would be largely self enforcing.

You will, of course, find a great many sporadic examples of Federal legislation implemented in this more ingenious way, but the study of this possibility in connection with all legislation needs to be systematized and thorough-going. A striking example of our use of this more or less automatic process is the way our present capital stock and excess profits taxes were set up. Taxpayers were given the liberty of fixing the amount of their capitalization. But this tax legislation is so framed that, if they fix it too high, their capital stock tax will be unattractively high, while if they fix it too low, the tax on their excess profits will become too burdensome.

At the very root of the tax on undistributed corporate earnings is this fundamental policy of simplicity of administration. Whatever the imperfections of that tax, I doubt if its critics have fully weighed its alternative, which may be outlined briefly as follows:

With tax rates on large personal incomes higher than those on corporate income, we have had for a long time, and will continue to have,

the problem of preventing the avoidance of the higher rates on personal income by the retention of earnings in corporations. Congress first tackled this problem in what I have called the traditional manner, i.e., it imposed a penalty tax on corporations whose earnings were retained "for the purpose of preventing the imposition of surtaxes on shareholders". This method has proven ineffective because of the practical impossibility of proving this purpose which is a state of mind. A subjective fact, difficult of proof in any case and especially so here, is by this legislation made the test for the imposition of the penalty tax.

As the rates on personal incomes mounted, the problem of preventing avoidance became more acute, and Congress next tried the other or more automatic type of implementing the tax law, which I have already described, i.e., in the Revenue Act of 1936, it left the initiative as to the distribution of corporate profits and the reasons therefor with those managing the business, stipulating only that the loss of revenue from individuals due to excessive retention should be made up at least in part by added taxes to be paid by the corporations.

Eliminating this aid to administration would not eliminate the problem of surtax avoidance. We shall ultimately have to face it. The only alternative to the present automatic method would seem to be to revert to, and perfect, the traditional method by adopting an objective test of what constitutes undue retention, and by setting up the increased personnel and administrative machinery necessary to go into the affairs of all the corporations involved in order to apply that object in test and thereby ascertain whether there has been undue retention and to enforce the penalties therefor. As in other cases of the use of the traditional method, this would maximize governmental interference in business and greatly increase the bureaucracy necessary to enforce our tax laws.

Telling People What the Government Expects

The second possible angle of attack on the problems generated by the marked growth in the administrative function relates to the citizen's timely knowledge of his rights and duties under Federal statutes and regulations.

Early in my experience in these problems of administration in the Treasury, a man presented this problem to me: He had in mind the purchase of a large building in the financial district in New York. The feasibility of the transaction depended on what the tax liability of each of the parties to this proposed deal would be, that depending on how certain future events might turn out, and it not being feasible to provide for these contingencies in the contract. I had to say to this man that he could not be advised as to what his rights would be, that he would have to go ahead and make the deal, and, not until the whole transaction was closed and the tax had accrued could the question of tax liability be determined under our system of tax administration by the Bureau, the Board of Tax Appeals and the Courts, and that, if he did not want to take the risk, there was nothing for him to do but forego the deal.

For further example, other men have sought to learn the tax status of proposed corporate reorganizations necessitated by the widespread difficulties created by the depression. They had to be told that, under our method of administration — the only one permitted under existing legislation — they would have to go it blind or forego their undertakings. Frequently this meant that the reorganizations failed and thus businesses were destroyed with the resultant unemployment and other consequences of liquidation.

Take a case where the Commissioner of Internal Revenue became bold and tried to be helpful in one of these situations, and note the consequences.

At the request of an agent, acting on behalf of Henry Ford in the purchase of the minority interest in the Ford Motor Company, including that of the late Senator Couzens, and after an extensive investigation, the Commissioner of Internal Revenue ruled that the Bureau was "disposed to regard \$9,489.34 as a fair market value of the stock as of March 1, 1933, and one which should be used in computing any profit made on the sale." The deal was closed on this basis, and the taxpayer made his income tax return in conformity with this pronouncement. Later the taxpayer was assessed on the basis, not of \$9,489.34, but of \$3,547.84 per share, and the Board of Tax Appeals held that the earlier finding of the Commissioner was not binding upon his successor in office, nor upon it. It reexamined this whole question of value and fixed \$10,000 per share as the proper valuation.

Under our present system of tax administration, and what I say here applies to much of the balance of Federal administration, the taxpayer is confronted with a two-fold difficulty. He cannot ascertain, in advance of the time when he must act, what his legal rights and liabilities consequent upon such action will be; and, when they are finally determined, the law is applied retroactively, and retroactively not only as to him, but as to all others similarly situated. If Federal administration is not to become unconcionably burdensome on the life and business of the country, we must, in view of its present and growing magnitude find some way to administer Federal law otherwise than in the retroactive fashion involved in the present process. A partial, but only a partial, solution of this difficulty is to be found in our

legislation providing for declaratory judgments, but such judgments cannot be obtained in that great mass of cases where people have not yet acted and need to know their rights and liabilities before they act. It is true, if a contract has been made, if a deed has been executed or a status, such as marriage entered into, or divorce obtained, the declaratory judgment can be used in many situations to define rights incident to such a consummated arrangement or status, but a declaratory judgment would afford no help to a man who wants to embark upon a business undertaking and needs to know his rights and liabilities before he dare do so. That field is not covered, and a long stride forward in solving the growing problem of administration will be made if we can find a device for advising people what their rights and liabilities are at a time when they need to know.

Developing that new device was a general problem which I put before the Legal Division of the Treasury more than two years ago as a chore for us all to work on as the press of immediate tasks permitted. Later this was made the sole problem of an assistant with special training, who has garnered the collective thinking on the problem and sought outside suggestions and guidance. All of this work has now culminated in what we think is a feasible device, which, for want of a better name, I have called "Declaratory Administrative Ruling" a "Declaratory Ruling". We hope soon to lay the plan of this new device before Congress, with the idea of trying it out in one branch of the Treasury Department, viz., in the administration of our tax laws.

Perhaps the plan can best be presented in terms of a typical case in which it arises. John Smith owns valuable mining property which he desires to sell. The important factor in the transaction is what will be fixed as the value of this property for tax purposes. Before he makes the sale John Smith naturally desires to know what value the Commissioner

of Internal Revenue will place upon this property. If today he asks the Commissioner for a ruling on this question prior to the sale, the Commissioner will probably not give him a ruling. Moreover, even if the Commissioner fixed the value, the taxpayer would have no assurance that, after he had completed the sale in reliance upon such a ruling, the Commissioner or his successor in later determining his tax liability in the due course of tax administration would abide by such previous valuation.

Briefly, the proposal is this: The taxpayer would file with the Commissioner an application for a Declaratory Ruling. In this application he would state in detail the facts pertinent to the proposed transaction. The Commissioner would examine the application to determine whether it merited his consideration. If he found that it did, he would ascertain if there were sufficient information provided to enable him to reach an intelligent conclusion. If not, he could either request more information from the taxpayer or make any other investigation that he deemed necessary to the same extent that investigation of closed cases coming before him are now made. The taxpayer would have an opportunity to appear in person and present any additional information or considerations that he thought relevant. The Commissioner would then issue a Declaratory Ruling in which, in the example supposed, he would fix the value of the property or make such other ruling as was requested or was appropriate in the case before him. He could make the effectiveness of the ruling depend upon compliance either by the taxpayer or by other persons with certain terms and conditions such as the consummation

of the contemplated sale within a definite period of time, the substantial accuracy of certain representations, the existence of certain facts which he might deem to be crucial, etc.

The taxpayer, having received the Declaratory Ruling, might decide that it was inadvisable to complete his transaction. If so, the Declaratory Ruling would become ineffective. If the taxpayer decided to proceed with the sale and pay a tax upon the value fixed in the Declaratory Ruling, the transaction would be ended. If, however, the taxpayer did not believe that the Commissioner's determination of the value was the correct determination, he could not appeal from the Commissioner's ruling (the Commissioner is given an absolute discretion with regard to his ruling), but he could proceed to complete the sale and test out his tax liability before the Board of Tax Appeals or in the courts as he may do today. In that event the Commissioner would not be bound by the Declaratory Ruling which he made, since the taxpayer himself had chosen not to be bound by it and the matter would be litigated in the courts as if no Declaratory Ruling had been issued.

However, if the taxpayer acquiesced in the ruling and completed the transaction in accordance with the terms of the Declaratory Ruling, neither the Commissioner who issued it nor any later Commissioner could alter or repudiate it. The Commissioner, however, would be free to change the Ruling, or to make a different Ruling, with regard to transactions not expressly included in the Ruling and persons not parties to it.

After the sale had been consummated, the taxpayer if he desired might request the Commissioner to issue a certificate of compliance stating that the taxpayer had complied with the terms and conditions set forth in the Declaratory Ruling. The issuance of this certificate would make its binding effect a matter of record.

Another example of an administrative mechanism calculated to advise people in advance as to what their rights and liabilities are, so that they can act with assurance and reliance upon such advice, is a provision which you will find in an amendment to the Securities Act. There was much complaint in 1954 that bankers, underwriters and others interested could not go forward with capital issues because of the uncertainty as to their liabilities under the various provisions of the Securities Act as originally enacted.

It seemed to me that this problem was not to be solved by a multitude of new provisions further particularizing the various provisions of the Securities Act. What seemed to be required was an administrative mechanism that would be prospective in operation, and this suggestion was embodied in Section 209(b) of the Securities Exchange Act of 1934, which reads as follows:

"No provision of this title imposing any liability shall apply to any act done or omitted in good faith in conformity with any rule or regulation of the Commission, notwithstanding that such rule or regulation may, after such act or omission, be amended or rescinded or be determined by judicial or other authority to be invalid for any reason."

But there is nothing new under the sun. I later found this same device tucked away in Section 1108(b) of the Revenue Act of 1926,

which provides that in cases where a sale or lease is made in reliance upon a ruling, regulation or Treasury Decision existing at the time, and holding that the sale or lease was not taxable, no tax under the act should be imposed.

The device embodied in the amendment to the Securities Act and the similar but more elaborate device here described as a Declaratory Ruling both should have, in addition to the virtue of being prospective in operation, the advantage of enabling administrative officers using them to exercise greater freedom to clarify legislation by the process of administrative interpretation.

To sum up, I have suggested ways to do two things: To place the initiative of law administration on the parties concerned and to tell them what the law will require when they need to know. I venture to believe that these two are among the things which cut to the heart of the growing incubus of government.

Prepared by Mr. Daggit

Division of Research and Statistics

Date..... Dec. 11937

To: Miss Chauncey

From: Miss Kailey *EK*

I read the attached memorandum to Mr. Haas over the telephone, and he asked that it be given to the secretary directly, without waiting for his signature.

99

*Recd 1 o'clock
me.*

TREASURY DEPARTMENT

99

INTER OFFICE COMMUNICATION

DATE December 1, 1937

TO Secretary Morgenthau
FROM Mr. Haas

In response to your request, we are giving herewith a statement as to the present financial interest of the Government in the cotton crop. The total figure to date, including Government-guaranteed loans on cotton by Southern banks, is approximately \$447,000,000. This is made up of the following items:

1. Cotton loans. The Commodity Credit Corporation reports outstanding loans on cotton as of November 27, 1937, of \$139,551,404.30. This is divided as follows:

Balance loaned on previous crops	\$116,012,019.34
Loaned on 1937 crop to date	23,539,384.96
Total	<u>\$139,551,404.30</u>

In addition to this sum, a total of \$107,177,408.72 has been loaned by banks in the South on this year's crop under the terms of the Government loan, but these loans have not yet been turned over to the Commodity Credit Corporation.

2. Price adjustment payments. A total of \$130,000,000 has been set aside for price adjustment payments on cotton, and AAA opinion is that this definitely will all be spent.

3. Conservation and benefit payments. It is not possible to estimate accurately how much will be spent for soil conservation and benefit payments on cotton this season, since they are tied up with other crops, and payments will be made mostly next spring. The best opinion of the AAA is that the total applicable to cotton will be about \$70,000,000, a decline from the \$82,300,000 paid last season.

December 1, 1937

My dear Mr. President:

Your two Henrys were walking down town this morning and reached the conclusion that if there is to be Government participation in advertising to enlarge the demand for cotton, it had best come by way of the Commodity Credit rather than by way of Section 32.

Herman Oliphant has satisfied himself as to the legality of this approach and has checked the matter with the Acting Comptroller General.

Tomorrow, Thursday, your two Henrys are eating lunch with Jesse Jones and we hope to have something more specific to report by tomorrow.

You can get up a "hat pool" as to whether the two Henrys will take in Jesse or Jesse will take in the two Henrys.

Sincerely yours,

(Sgd) Henry Morgenthau, Jr

(Sgd) Henry A. Wallace

The President,
Miami, Florida.

DATE December 1, 1937.

TO Secretary Morgenthau
 FROM Mr. Haas
 Subject: Reported large shipments of cotton to British India.

Reported United States exports of cotton to British India during the past few weeks (about 20,000 bales) are in excess of her previous annual takings.

United States Domestic Exports of Cotton
 to British India
 (In bales)

Crop year 1936 (June to July)	6,800
Crop year 1937 (June to July)	13,045
August and September 1936	265
August and September 1937	356

Mr. Alfred Boedker of Volkart Brothers (head office in Bombay) stated on the telephone that India has bought 100,000 bales of American cotton which will be used in Indian mills. Most of this cotton was bought during July and August and practically no cotton has been bought in past six weeks and no more is expected to be bought. The cotton is largely high grade cotton of 1-3/32 to 1-1/8 inch staple. He said ordinarily they would use Indian or African cotton, but they were very bullish on the market and American cotton was only cotton they could buy ahead. Bought in July and August; just now being shipped.

A possible explanation for these purchases by India in July and August was an expectation on the part of the Indian mills that the Sino-Japanese war would increase their sales at the expense of Japanese and Chinese mills, but we have no information as yet on that score.

December 1, 1937.
9:04 a.m.

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HMJr: Hello.

Operator: Mr. Jones.

HMJr: Hello.

Jesse

Jones: Hello.

HMJr: Good morning, Jesse.

J: Good morning.

HMJr: Are you at home?

J: Yes.

HMJr: Jesse, I want to take a minute or two to explain what I've been working on very quietly, for the President, see.

J: All right.

HMJr: And I asked him - we talked about it, whether somebody couldn't work on cotton with the idea that eighteen million bales of cotton is a good thing, and let's see whether we can't do something to get rid of it.

J: Yes.

HMJr: Rather than just sit around and tell tales of woe, see?

J: Yes.

HMJr: Well, I've been working on this thing quietly for a couple of weeks, and we finally evolved an idea of a national advertising campaign in conjunction with the industry, and we work through the textile industry, and they're tremendously enthusiastic about it and ready to put up some money, see.

J: Who?

HMJr: The textile industry.

J: Yes.

- 2 -

HMJr: Through the cotton institute.

J: Yes.

HMJr: You know. Well, we've got the thing and I first thought we could do the Section 32 money, but Wallace doesn't like it that way, so we looked up and we - Oliphant's given us the opinion we can do it through Commodity Credit.

J: Yes.

HMJr: And yesterday afternoon we put it up before the Comptroller General and he said he'd O.K. it. Now I just walked down with Wallace and he's far enough long that he said he'd like to meet with you and me, and talk this thing over, see.

J: Yes.

HMJr: Now would lunch tomorrow be convenient? And if you'd like - I'd like you to get more details so you can have a chance to think about it. I'd like Wayne Taylor to come over and talk to you at your convenience, he's all full of it.

J: Well, suppose - suppose he do that today, and what time - how early could we have lunch?

HMJr: Well, we'll fix it - are you going to leave town?

J: I was going to leave town. I am - I am going to leave town tomorrow afternoon.

HMJr: Well -

J: I was going today, but Wagner wants me to come up there and get before his committee on the Housing thing in the morning.

HMJr: Well, do you want to make it quarter of one?

J: Yes, well - well that'll be all right, and if we get through - I might take a two o'clock train or at least a three.

HMJr: Oh, yes. Now, supposing I have Wayne contact you, see.

- 3 -

J: All right.

HMJr: And give you the thing - so as you won't get this thing cold.

J: All right.

HMJr: And - I mean - I'm quite enthusiastic about it.

J: Well, I hope - I hope that I agree with you.

HMJr: Well, I don't know, but -

J: I say I hope I do, and I -

HMJr: I want to give you twenty four hours to think about it.

J: Well, I've got to go to the Hill at ten-thirty to testify on the House side
for the Housing bill.

HMJr: Yes.

J: And so suppose I leave word, and maybe I can get it - I'll call Wayne and maybe I can get a lunch engagement with him today.

HMJr: Yes, well shall I leave it that you'll call Wayne.

J: Yes. I'll call him right now.

HMJr: You'll call him right now.

J: Yes.

HMJr: Wayne doesn't know I called you, because I just got into the office.

J: Well, if you'll tell him -

HMJr: Well, supposing I tell Wayne to call you right away.

J: Tell him to call me, and -

HMJr: And I'll tell him what's it about.

J: Tell him to call me through the office.

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HMJr: Through the office?
J: Yes.
HMJr: Through the office.
J: My office, yes.
HMJr: I'll do that.
J: Thank you.
HMJr: He'll call you in two minutes.
J: All right. Fine.

December 1, 1937.
9:08 a.m.

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H.M.Jr: Wayne.
Wayne
Taylor: Yes.

H.M.Jr: Wayne, I just got through walking with Wallace and he and I have written a joint letter to the President. Wallace is pretty well sold on this Commodity Credit thing, see.

T: Attaboy.

H.M.Jr: Now, we're going to have lunch tomorrow at 12:45. I just - to which you're invited.

T: Fine.

H.M.Jr: I just called up Jesse, so he could be thinking about it.

T: Yes.

H.M.Jr: And he'd sorta like to have lunch with you today, so that you could kind of fill him up with it.

T: All right.

H.M.Jr: So he said if you'll call him right away, now.

T: Yes.

H.M.Jr: Through his office, he'll make a date with you, but I thought - give Jesse twenty four hours to think about it.

T: All right. Fine.

H.M.Jr: See. But Wallace, I'd say, is two-thirds sold.

T: Good boy.

H.M.Jr: All right.

T: I'll get hold of Jesse right away.

H.M.Jr: And the lunch tomorrow at 12:45.

T: Right.

H.M.Jr: Thank you.

December 1, 1937.
10:03 a.m.

HMJr: I just want to tell you, on the loud speaker, see. This conference is going on. Mr. Helvering and the others are here.

Elmer L. Irey: Yes.

HMJr: The question has come up, whether you or Burford, Burford having sat in on this conference when they considered this Maester case. I mean would you or Burford sign this report recommending that we accept the hundred and thirty four thousand?

I: You say, would we sign such a report?

HMJr: Yes.

I: Why, I haven't gone into the figures enough to know about that, Mr. Secretary. I mean it's been so long since I went through the case I don't remember the tax setup, nor what the explanation is.

HMJr: Well, what about Burford?

I: Well, Burford, of course, is down in Dallas, Texas. I can't say for him, but I can communicate with him, today, and find out. And I also can go into the case myself today and find out how I feel about it.

HMJr: Well, why wasn't it ever brought to your attention before they recommended it to be accepted?

I: Well, I am sure I don't know that, Mr. Secretary, but, when we - the usual procedure in these tax cases is when the criminal phase is out, it's not then referred to us for any further attention. It's handled by the tax branches of the Bureau.

HMJr: Well, Burford sat in on it.

I: Yes, Burford sat in over at Mr Magill's office on it, and I also sat in at that time, on it.

HMJr: No, he sat in on it on September 9th, when they had the hearings.

I: Yes. Well, I didn't know about that - I didn't remember about it.

- 2 -

HMJr: Well, now just a minute, let me ask Mr. Helvering.
(aside) Mr. Helvering states that Mr. Burford told him that this was a good settlement, and based on that Mr. Helvering recommended the thing be settled.

I: Well, of course, that's perfectly all right, then. I didn't have any discussion with Burford as to the tax liability so I don't -

HMJr: Well, I'm not - I'm not going to check up on Mr. Helvering's way. I'll take Mr. Helvering -

I: Surely. There isn't any doubt but what Burford told him that.

HMJr: Yes, well I'm not going to check up on Mr. Helvering.

I: Yes.

HMJr: But it's not customary that you sign these things.

I: No, sir. It's not.

HMJr: Well, I'm not going to check up on Mr. Helvering.

I: Yes.

HMJr: Thanks.

I: All right, sir.

HMJr: I may - all right, thank you very much.

I: All right.

December 1, 1937.
10:23 a.m.

H.M.Jr: Hello.

Operator: Ellender.

H.M.Jr: Hello.
Sen.
Ellender: Hello.

H.M.Jr: Senator Ellender.

E: Yes, Mr. Morgenthau, how are sir?

H.M.Jr: We just concluded another conference. We made a decision and Commissioner Helvering is going back to his office and he'll communicate it with you.

E: Yes, sir.

H.M.Jr: See.

E: Yes, sir.

H.M.Jr: And - well, he'll let you know, and I think you'll be entirely satisfied.

E: Well, I'm certainly obliged to you Mr. Secretary.

H.M.Jr: And I dropped everything and - we've just finished, but I'd like him to let you know officially.

E: All right, sir. That's very kind of you, sir.

H.M.Jr: Goodbye.

E: Thank you very much.

December 1, 1937.
12:23 p.m.

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Leffingwell: Mr. Stanley?

H.M.Jr: Yes.

L: Oh, intimately.

H.M.Jr: Intimately.

L: He used to be my partner, you know.

H.M.Jr: Well that's what I thought.

L: And I - I - I'm a devoted friend of his.

H.M.Jr: Well, do you suppose that you and he'd like to come down here Friday and have lunch with me?

L: I'd love it. I'll try and get him.

H.M.Jr: Good. Well, what I had in mind was, we've got a Government financing next Monday, you see.

L: Yes.

H.M.Jr: And various people tell me that to do this, it will or won't help the private offerings, you see.

L: Yes.

H.M.Jr: And after all I don't suppose anybody could tell me better than yourself and - it's Harold Stanley, isn't it?

L: Yes, Harold Stanley.

H.M.Jr: Yes. So that's what I have in mind, so if the two of you would care to come down Friday and have lunch in the Treasury with me at one o'clock, I'd be delighted.

L: Well, I'll - I'll telephone Harold. I don't even know whether he's in town or not.

H.M.Jr: Uh-huh.

L: But I'll - I'll - I haven't - I haven't seen him for some time, but I'll telephone Harold and call you back.

H.M.Jr: Yes, and if I'm not available would you let Mrs. Klotz know . K-L-O-T-Z.

L: Yes, I'll tell her.

H.M.Jr: Thank you.

L: You - you - you want me anyway?

H.M.Jr: Sure.

L: If I can get Harold or not.

H.M.Jr: Sure. Always.

L: All right, I'll come anyway.

H.M.Jr: Right.

L: I - I'll have to break an engagement with our friends up at Harvard. They had asked me to come up there and discuss foreign policy.

H.M.Jr: Oh.

L: But I know a lot more of - I think I know a lot more about domestic finance and an invitation from you is both a pleasure and a command.

H.M.Jr: Well, I don't want you to - if Colonel Stanley isn't there would there be anybody else who knows the - what do you call it - I call it the private corporate market, you know.

L: There isn't anybody that - there isn't anybody as nearly as good as Harold anywhere.

H.M.Jr: Right. Well -

L: I'll try to get him.

H.M.Jr: Good.

L: I'll try to get him if he's accessible. He might be off shooting somewhere, that's the only thing. He hasn't been very well, and -

H.M.Jr: I see.

- 3 -

L: His partners were trying to get him off.
H.M.Jr: All right.
L: But I'll try to get him. I'll call back.
H.M.Jr: Thank you.
L: Thank you ever so much, Mr. Secretary.

December 1, 1937.
3:47 p.m.

HMJr: Hello.
Herbert
Feis: Yes, Henry.
HMJr: Herbert?
F: Yes, Hello.
HMJr: Henry.
F: Yes sir. I hope I don't disturb you.
HMJr: No.
F: Look here. Mr. Hull had to rush off, right after lunch, to a meeting of the Board of the Pan American Union, and seemed to think that you wanted an answer from him pretty speedily on that question you asked him in regard to Mexico.
HMJr: He called me.
F: Yes.
HMJr: Himself, this afternoon. About half an hour ago.
F: Well, then he got in ahead -
HMJr: Yes.
F: Ahead of me.
HMJr: And I told him we'd do nothing on Mexico this week, but I'd take it up with you the first of next week.
F: Yes, he told me that, but he seemed to have the impression, I don't know - it had been posed to him or maybe he posed this question in his own mind, he gave me the impression that you asked him - that suppose these fellows said they'd actually put up that gold and silver -
HMJr: Yes.
F: As collateral.
HMJr: That's right.

- 2 -

F: Well, I said then, since he put it to me in the form of a question, that if they did that, I thought that - that merely showed to him advance on - on specie, and that brought it much more closer to things, I understood that you had done before.

HMJr: Exactly.

F: And would be a much simpler operation for you.

HMJr: That's right.

F: And for our part I didn't think we should say anything, and leave it up to you.

HMJr: Well, but in order to help you out, I thought I'd just stall even on that this week. I didn't think I'd answer them at all.

F: All right.

HMJr: And unless there's any pressure from the State Department, we won't say peep this week on Mexico.

F: Right.

HMJr: See what I mean. I don't think he got that - I said he -

F: He didn't seem to have it clear at all.

HMJr: Well, what he said to me was this. He said, "Now I understand the technical reasons and so forth why you can't do it this way."

F: Yes.

HMJr: "The way they put it up to you." He most likely explained it to them, and I said, "Yes, but - they'll come back and say how can you do it, and I'll pay the way, we did it before, and that is that you put up the gold and silver on deposit."

F: Yes.

HMJr: As security.

F: Yes.

HMJr: Then I say if they do that we've got to say yes.

F: Well, that's what he was testing me out on and I luckily gave him the same answer.

HMJr: But I said, "Rather than put it up to them, and have to say 'yes', in order to help you out," I said, "I won't do anything before Monday, and the excuse I give is my Government financing, so you people have got to square me with Josephus Daniels."

F: Well, no -

HMJr: You and I are together.

F: All right, I'll -

HMJr: You and I are together. Mr. Hull, I don't think quite had it. There's no reason why he shouldn't.

F: Well, now you want us to get some word down to Daniels.

HMJr: Simply tell him that I think, as a matter of courtesy, he should send a cable to Mr. Daniels, simply saying that the Secretary of the Treasury is so occupied this week getting ready for his financing on Monday, that he can't take on any outside matters before next Tuesday.

F: Right.

HMJr: That stalls the thing over a week, you see.

F: I'll do it.

HMJr: But I think Daniels is entitled to an answer.

F: Right sir.

HMJr: Now, did that places the statement

F: Completely, - and on the other hand I think if and as it comes up next week, and they actually offer you that specie collateral -

HMJr: We got to go ahead.

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F: You've got to go ahead with it.

HMJr: But we're absolutely together.

F: Right.

HMJr: But I won't see the Mexican Ambassador before next Tuesday, and when I do, I'll have you - see you first, and then I'd like to have you here when I do see him.

F: Right. May I ask you one other question, again, the Secretary keeps asking this to me in a rather vague way. You haven't decided on the renewal of those agreements, the silver purchase agreements, on that you've reached no decision, yet?

HMJr: I - I haven't even mentioned it to the President of the United States and won't until he gets back.

F: Right, sir.

HMJr: Now, we won't take it up until the Presidents gets back.

F: All right. Now on Far East.

HMJr: Yes.

F: Two things, first we have had no further confirmation at all -

HMJr: Yes.

F: From the Far East regarding the idea that they were going to - they might declare war.

HMJr: Yes.

F: Nothing at all. On the other hand in response to Mr. Hull's cable, wired to the President, asking him how promptly we ought to act. The President wired back saying 'Get all the proclamations in readiness for me, and I'll sign them and send them back.'

HMJr: I see.

F: That doesn't mean that they necessarily go out at once.

HMJr: Yes.

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F: But I read it to mean that he wouldn't delay any longer than might be necessary to make sure of the situation, you see?

HMJr: Yes.

F: Which indicates to me that his disposition would be to move fairly promptly.

HMJr: I see. Well, now, but nothing's happened.

F: Nothing to - no confirmation that they are doing to declare war.

HMJr: I see.

F: But an indication that if they do, the President's inclination would not be delayed very long before announcing the Neutrality Act in effect.

HMJr: Well, what I've got to do is to make up my mind what I want to do about China.

F: That's what - I thought that might -

HMJr: And I think maybe we ought to tell China we've taken fifty million ounces of silver from her over the last four or five weeks, and I might tell them informally now, we may take another fifty million from them you see.

F: Yes.

HMJr: And so I could say well we did that before in cases like that.

F: Well, that was in my mind, too.

HMJr: And I may do that tomorrow or Friday.

F: Yes. Well - well, that's what was in my mind.

HMJr: I'm going to talk -

F: I think that's what was in the Secretary's mind.

HMJr: Well, I'm going to talk to Taylor and Lochhead tonight about it.

F: All right.

HMJr: See?

F: Yes.

HMJr: And the other thing, while I've got you, may interest you, we haven't got the details yet, but on the telephone, but France has negotiated a loan from Holland, and as I understand it, I haven't got all the details yet, but it looks as though Holland wants to buy fifty million dollars worth of gold from us, see? - In order to take the place of the gold which they're shipping to France, which is a very nice piece of business for us.

F: That's - I was going to say, it is, isn't it?

HMJr: When I have the details, I'll ask Lockheed tomorrow to give you a ring and explain it to you. The facts, on account of it being on the telephone was a little buzzy.

F: Yes.

HMJr: But I - I thought that was a nice piece of business.

F: I think - I think it's very nice.

HMJr: Well, I'm going to move on China - try to move this week, I think, maybe tomorrow, we'll see.

F: Uh-huh.

HMJr: All right.

F: Thank you.

December 1, 1937
4:30 p.m.

HMJr: Hello.

Operator: Mr. Parkinson.

HMJr: Hello.
Mr.
Parkinson: Hello.

HMJr: Mr. Parkinson?

P: Yes.

HMJr: Morgenthau.

P: Oh, hello, Mr. Secretary.

HMJr: How are you?

P: Very well, thanks.

HMJr: I'm sorry you're going to be tied up Thursday and Friday.

P: But it - it's just this week that we have both the President's - the Vice-President's meeting, the Insurance Commissioners meeting, and I also have the Rockefeller Foundation annual meeting.

HMJr: Uh-huh.

P: But notwithstanding all of that if it's really - be of any service to you I can come down Friday morning.

HMJr: Well, that's very nice but I think maybe you can do some work for me up there.

P: All right.

HMJr: This is what I'd like. If you, in circulating around, would ask your other Presidents - other companies, what kind of a Government securities they're in the market for.

P: Yes.

HMJr: See.

P: Yes.

HMJr: I mean -

P: Right now, you mean.

HMJr: Right now, we would offer it Monday for payment on December 15th, see?

P: Yes.

HMJr: And we haven't got your December 1st figure, how much cash all these insurance companies have on hand. I think the last figure we had was September, which was around six hundred and eighty million.

P: Yes.

HMJr: And I'd - I'd kinda like to know whether there were thirty eight or forty companies, the life insurance companies, what their cash position was December 1st. And then as I say, what would they buy - I mean I can't get out a penny or two and three quarters, you see?

P: No. Well, I tell you, I'll have a fairly good chance to do that tomorrow and - and Friday, because they'll practically all be here.

HMJr: That's what I thought.

P: At this meeting.

HMJr: And then could you call me Friday afternoon?

P: Not later than Friday afternoon.

HMJr: Yes. And would you just sorta sound them out?

P: Yes I will.

HMJr: And then if you'll also let -

P: I think - I think I could find more about the first question you asked than the cash position.

HMJr: Uh-huh.

P: That might be a bit hard.

HMJr: Well -

P: To get - to get a really accurate idea.

HMJr: Well, that -

P: But I might get something that would indicate whether it had changed much since - since September.

HMJr: Well, that - that would be just as useful if it's gone up since then, or down.

P: Yes.

HMJr: And also the - how hungry are they.

P: Yes.

HMJr: See?

P: Yes. We're all kind of hungry.

HMJr: Pardon me?

P: We're all kind of hungry.

HMJr: Uh-huh.

P: For securities, I mean.

HMJr: Well, one - one - I needn't tell you, but right now, an eight year two and a half would be about - have a one point premium, I mean, that's what -

P: Yes.

HMJr: Suggested,

P: And that's something to shoot at, and see what they think of it.

HMJr: Yes.

P: All right.

HMJr: And the other thing is, would they all be interested in a five year one and three quarters.

P: Five, one and -

- 4 -

HMJr: Yes.

P: All right. I'll use those to shoot at.

HMJr: Thank you very much.

P: Not a bit.

HMJr: And I'll hear from you Friday afternoon.

P: Yes, surely.

HMJr: Thank you.

P: All right.

December 1, 1937.
4:39 p.m.

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H.M.Jr: Hello.

Operator: Mr. Mitchell.

H.M.Jr: Thank you.

O: Go ahead.

H.M.Jr: Hello.

Mr. Mitchell: Good evening, Mr. Secretary.

H.M.Jr: How are you?

M: Well, thanks.

H.M.Jr: I want a little help.

M: Yes.

H.M.Jr: And I think the National Bureau of Economic Research might do it for me. I am talking to you as I understand you're director of that?

M: Yes, I'm Director of Research. Do anything we can for you.

H.M.Jr: Well, this is what I'd like, and I'd like to have from your Bureau - looking back over as many years as you deem advisable, what are the signs that one can look for and count on when one is reaching the bottom of a recession, and then what are the signs that one can look for that would be turning the corner? Now what I have in mind is this - Government bonds, high grade bonds, second grade bonds -

M: Yes.

H.M.Jr: Commodities, etc., etc., you see?

M: Yes.

H.M.Jr: And I'd like to have an independent agency of the first class, like yours, do that sort of thing, so that we won't be doing just what you said Mr. Hoover was doing -

M: Yes.

H.M.Jr: Some wishful thinking.

M: Yes.

- 2 -

H.M.Jr: Now if this requires extra expenditure, why we have the money to pay for it.

M: Well, how - how soon do you want a letter on that head.

H.M.Jr: Well, I think the first time, I think we'd better have a little face to face talk about it.

M: All right.

H.M.Jr: And just to go over the sort of thing that you would do, and then what I'd like is something once a week.

M: Once a week?

H.M.Jr: Yes.

M: Well, oh I see - I see what you mean, you'd like us not only to make up a statement of what to look for but also be on the lookout for it.

H.M.Jr: Yes. To follow it every -

M: Now, the first thing is very much more in our line than the second. I really think that if we - if we could provide you on the basis of materials that we had are in pretty good shape now.

H.M.Jr: Yes.

M: A statement of what to look for and then your people could do the looking.

H.M.Jr: Well, that's - that would be all right.

M: Yes.

H.M.Jr: But then you could also check their looking, couldn't you?

M: Yes. I suppose so. Yes, probably.

H.M.Jr: Well, let's - when - when could you come down and tell me with a statement what we should look for.

M: Well, I should like to do that rather carefully, you know.

- 3 -

H.M.Jr: Yes. Well.

M: Now, next week end I might be able to -

H.M.Jr: Next week end.

M: I think I can probably get something in order by that time.

H.M.Jr: That would be the 11th and the 12th?

M: Yes. Yes, I suppose so.

H.M.Jr: Say Saturday the 11th.

M: Yes, or Friday perhaps.

H.M.Jr: Or Friday - it will have to be in the forenoon, because we'd have a Cabinet meeting that afternoon.

M: I see. Yes.

H.M.Jr: So it'd be Friday morning, the 10th?

M: Well, - well, I'm not perfectly sure that I could get it ready by that time. It'd probably be safer to say Saturday, if I can catch you.

H.M.Jr: Well, Saturday morning?

M: Saturday morning. I'll try to have something at least in shape by Saturday morning the 11th.

H.M.Jr: Or would you rather come down Monday?

M: No, it - it's better for me to do it Saturday.

H.M.Jr: Well supposing we say - what time Saturday morning.

M: Any time you set. I can come down on a night train, you know.

H.M.Jr: Uh-huh. Well, let's say ten o'clock Saturday morning?

M: Ten o'clock Saturday morning in your office?

H.M.Jr: At the Treasury.

M: Good.

H.M.Jr: And you bring anybody with you, that you want to.

M: All right.

H.M.Jr: And - and - I don't know how the Bureau does those things, but all I can say is we have funds to pay for either -

M: Well - this will entail some expense, not - not a great deal, and I'll - I'll tell my people to -

H.M.Jr: Well, whatever -

M: To take count of the current expense - we'll tell you what it is.

H.M.Jr: Well, whatever it is, you let us know, and traveling expenses to Washington or anything like that, or per diem expenses, - anything like that we - we'll pay for it.

M: All right, it won't be a thing that will interfere with balancing the Budget.

H.M.Jr: Well, that's - I'm glad of that.

M: Yes.

H.M.Jr: But I'll leave it to your good judgment.

M: All right.

H.M.Jr: I just want to let you know we have the funds.

M: Yes.

H.M.Jr: And I'll for - you bring whoever you want, with you.

M: All right. I think I may bring one of my assistants down with me.

H.M.Jr: That'll be fine. Thank you.

M: You're welcome.

C A B L E

From: Netherlands Bank
Amsterdam, Holland

To: Federal Reserve Bank of N. Y.

Date: December 1, 1937

#176. CONFIDENTIAL FOR KNOKE.

With reference to our telephone conversation we cable to ask you to apply to United States Treasury and ask on behalf of Dutch Exchange Equalization Fund special license for converting into gold \$50,000,000 held at present by De Nederlandsche Bank for account of said Fund. This license is asked in connection with monetary policy of Dutch Equalization Fund which is directed to maintain reasonable relation between Dutch guilders and gold. License is asked with a view to the fact that for the time being it does not seem likely that Dutch Equalization Fund will have to sell dollars in order to combat high dollar rates here. Intention would be to ask you to take gold in question in safe custody earmarked for our Special Account "A".

(Signed) De Nederlandsche Bank

C:ek

December 1, 1937

From: Mr. L. W. Knoks
Federal Reserve Bank of New York

To: Mr. Lochhead

Subject: Telephone Conversation with Netherlands Bank

Mr. de Jong called at 9:42 today and referred to our telephone conversation of November 8, when I had explained to him that conversion into gold of dollars acquired outside the Tripartite Agreement was possible ~~only with~~ a license to be issued by the Secretary of the Treasury with the approval of the President. He stated that they would like to convert into gold \$50,000,000 now held in their regular account and place the gold under earmark with us, and inquired as to the procedure to be followed by him. I suggested that he make this request by cable to us, advising us at the same time as to the purpose for which the gold was required and as to its ownership. de Jong explained that the gold would be the property of the Exchange Equalization Account which, in connection with the recent Dutch loan to the French, was temporarily out of gold; this was the reason for the Netherlands Bank planning to make the transfer. I assured de Jong that, immediately upon receipt of his cable, I would take the matter up with the Secretary of the Treasury; he asked whether I thought it would take very long to get a reply and I told him I did not expect so.

In view of the interest which de Jong had previously shown in our Government Bond market, I mentioned that 3-Mo. Treasury Bills could now probably be bought at a price to yield about .10% per annum, which he had previously, in his cable of November 9, stated was the lowest yield that would interest them. I inquired whether they intended to renew their selling order for guilders in this market

-2-

Subject: Telephone Conversation with Netherlands Bank.

but de Jong explained that the market had been so remarkably stable recently that dollar operations had become entirely unnecessary for them and even in sterling they had done very little in recent weeks. I made reference to their statement published yesterday and asked whether it was correct to assume that the 43,000,000 guilder loss of gold shown therein had to do with the Dutch loan to the French. His reply was, "Absolutely, yes".

C:ek
12.1.37

December 1, 1937
Wednesday

The Netherlands Bank, Amsterdam, telephoned to the Federal Reserve Bank of New York today and on behalf of the Dutch Exchange Equalization Fund made application for \$50,000,000 of gold. Confirmation of their telephone conversation was made by a cable message. Memorandum covering the telephone conversation, and copy of the cable, are attached hereto.

After consulting Secretary Morgenthau, he authorized the Federal Reserve Bank of New York, who informed the Netherlands Bank, that we would sell them the gold requested.

It was finally decided by the Secretary that this gold should be supplied out of gold holdings of the Exchange Stabilization Fund at this time rather than from the Sterilized Gold Account. His reason for doing so was to avoid any change in the December 15th financing, the amount of which had already been decided upon, and to prevent an increase in excess reserves which might possibly occur. If the gold was taken from the Sterilized Account, in order to keep our cash position even it would be necessary to cut down the financing by \$50,000,000. On the other hand, if the total amount of the financing was left unchanged and the gold taken from the Sterilized Account, it would increase the Treasury balance, and in time the excess reserves, by the same amount. On the other hand, if the gold was taken from the Stabilization Account, it would leave the Stabilization Account with funds to absorb any new additions to the gold stock of the country up to this amount without increasing the Sterilized Gold Account.

Mr. Morgenthau, after discussing this with A. Lochhead, checked with Mr. Taylor, who was in accord with the decision made.

FEDERAL RESERVE BANK
OF NEW YORK

131
DATE December 1, 1937.

OFFICE CORRESPONDENCE

CONFIDENTIAL FILES

SUBJECT: TELEPHONE CONVERSATION WITH

NETHERLANDS BANK.

FROM: L. W. Knake

Mr. de Jong called at 9:42 today and referred to our telephone conversation of November 8, when I had explained to him that conversion into gold of dollars acquired outside the Tripartite Agreement was possible only with a license to be issued by the Secretary of the Treasury with the approval of the President. He stated that they would like to convert into gold \$50,000,000 now held in their regular account and place the gold under earmark with us, and inquired as to the procedure to be followed by him. I suggested that he make this request by cable to us, advising us at the same time as to the purpose for which the gold was required and as to its ownership. de Jong explained that the gold would be the property of the Exchange Equalization Account which, in connection with the recent Dutch loan to the French, was temporarily out of gold; this was the reason for the Netherlands Bank's planning to make the transfer. I assured de Jong that, immediately upon receipt of his cable, I would take the matter up with the Secretary of the Treasury; he asked whether I thought it would take very long to get a reply and I told him I did not expect so.

In view of the interest which de Jong had previously shown in our government bond market, I mentioned that three-months Treasury bills could now probably be bought at a price to yield about .10% per annum, which he had previously, in his cable of November 9, stated was the lowest yield that would interest them. I inquired whether they intended to renew their selling order for guilders in this market but de Jong explained that the market had been so remarkably stable recently

FEDERAL RESERVE BANK
OF NEW YORK

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OFFICE CORRESPONDENCE

DATE December 1, 1957.CONFIDENTIAL FILES
L. W. KNOKESUBJECT: TELEPHONE CONVERSATION
WITH NETHERLANDS BANK.

- 2 -

that dollar operations had become entirely unnecessary for them and even in sterling they had done very little in recent weeks. I made reference to their statement published yesterday and asked whether it was correct to assume that the 45,000,000 guilder loss of gold shown therein had to do with the Dutch loan to the French. His reply was, "Absolutely, yes."

LWK:KMC

RECEIVED
DEC 8 1957
FEDERAL RESERVE BANK
OF NEW YORK

FEDERAL RESERVE BANK
OF NEW YORKOFFICE CORRESPONDENCE
CONFIDENTIAL FILESDATE December 1, 1947.SUBJECT: TELEPHONE CONVERSATION WITH

L. W. Knack

BANK OF FRANCE.

FROM

Mr. Cariguel called at 11:05 today and requested that we ship to him on the Lafayette on December 4 another \$5,000,000 worth of gold. I assured him that his request would have our prompt attention.

Things continued to go very satisfactorily, Cariguel said. Today, he had not been able to buy any dollars for which there had been considerable demand from England as well as from France. He had managed to get in a little sterling.

LWK:KMC

RECEIVED
FEDERAL RESERVE BANK
OF NEW YORK
DEC 3 1947
TELETYPE UNIT

LMS

GRAY

Paris

Dated December 1, 1937

Rec'd 4:15 p. m.

Secretary of State,
Washington.

1684, December 1, 8 p. m. (SECTION ONE)
FOR TREASURY.

Transactions on the exchange and security markets here have been on a reduced scale. We understand that the fund has been able to secure a fair amount of sterling at 147.09 around which the rate has moved during the day. The dollar strengthened to 29.49, without intervention of the fund, it seems.

Rentes and the other French securities were unsettled and showed a weaker tendency.

Tomorrow the Chamber is expected to commence its examination of the 1938 budget. As it leaves the Finance Committee revenue is estimated at 53,781,000,000 francs and expenditures 52,179,000,000. However, the paper balance of 1,600,000,000 francs of the more than wiped out when Parliament finally votes the Government's bill providing for increases totaling 1,700,000,000 francs in the pay and allowances of civil servants. It will be recalled that in addition to the ordinary budget the special
armament

LMS 2-No. 1684, December 1, 8 p. m., Sec. 1, from Paris.

armament and public works budget for next year totals about 14 and a half billion francs which is to be covered by loan issues (see Embassy's despatch 1145 of October 15 last).

(END FIRST SECTION)

BULLITT

CSB

LMS

GRAY

Paris

Dated December 1, 1937

Rec'd 5:40 p. m.

Secretary of State,
Washington.

1684, December 1, 8 p. m. (SECTION TWO)

The financial press continues to publish rumors of an early loan by the Government. The impression appears to be that the Minister of Finance intends to issue the unused balance (2,500,000,000 francs) of the 10,500,000,000 franc exchange guaranty and option loan authorized by Parliament on March 10 last and that a further loan of from 5 to 6,000,000,000 francs will be issued in January. This prospect is not welcomed in financial circles which point out that under these circumstances the relief that might have been afforded to starved private enterprise through repatriated funds will be absorbed once more by Government borrowing. JOURNEE INDUSTRIALE remarks that repatriated funds have not yet found their way back to circulation to any appreciable degree.

AGENCE ECONOMIQUE today carries an apparently inspired statement to the effect that information circulated relating to an early loan issue by the Treasury "is premature".

LMS 2-No. 1684, December 1, 8 p. m., Sec. 2, from Paris.

ture". This paper goes on to comment that although the situation of the Treasury is now less strained the Minister of Finance will probably not wait until the last moment to assure himself of cover for maturing obligations. The statement invites attention to the high cost of recent loan issues of certain public bodies carrying the guaranty of the state and the difficulties thus raised for the Minister in obtaining funds.

END OF MESSAGE

BULLITT

SMS:NPL

sms

GRAY

Paris

Dated December 2, 1937

Rec'd 6:45 p.m.

Secretary of State,
Washington.

1688, December 2, 4 p.m.

FOR TREASURY

Business on the exchange market here today was almost at a standstill. There was a certain pressure on the franc and we understand that the fund paid out a fair amount of sterling at 147.15 to maintain the rate which has now fallen to 147.10. The dollar continued to show strength. It is now around 29.48 after 29.50.

The security market was depressed. There were average losses in rentes of about 50 centimes. Weakness in the latter appeared to be due in part to sales by holders desiring to subscribe to the new Treasury loan.

The Bank of France statement dated November 25 and published today shows no important changes. The gold reserves are unchanged, and no new advances have
been

sms 2 - No. 1688, December 2, 4 p.m. from Paris.

been made to the Treasury. Commercial advances up 507,000,000 francs. Note circulation up 141,000,000. Deposits down 90,000,000. Percentage of gold cover 53.23 percent compared with 53.26.

A certain amount of notice has been given in the financial press to news cabled from the United States that the Senate Agriculture Committee in its report on the new farm bill recommends a further reduction in the value of the dollar. It would seem (from?) for comment noted that no one believes that such advice will be given serious attention at Washington. In fact referring to the recent strength of the dollar, the financial press of today contends that this firmness is due notably to evidence that no menace of devaluation exists at this time, indication that President Roosevelt is turning towards a more orthodox policy, and improvement in the American commercial balance.

BULLITT

sms

emb

December 2, 1937.

MEMORANDUM

TO: Secretary Morgenthau
FROM: Mr. Gaston

The Government's Stake in Existing Cotton Stocks.

(1) Cotton Loans

Amount outstanding on pre-1937 crops	\$116,012,019.34
Estimate of loans on 1937 crop	
July 1, 1938	260,000,000.00

Of above amount loans already made as follows:

By C.C.C.	\$23,539,384.96
By banks in South .	107,177,408.72

(2) Price Adjustment Payments

It is estimated by A.A.A. that the full amount set aside for this purpose will be expended \$130,000,000.00

(3) Soil Conservation and Benefit Payments \$ 70,000,000.00

Total \$576,012,019.34

While the Government's investment in the 1937 cotton crop and existing stocks of cotton may be regarded as embracing all of the above items, ~~was~~ certainly the fate of loans amounting to an estimated \$376 millions will be directly affected by any method which proves effective on the market situation. Government expenditures are also likely to be affected in another way; namely the amount of Works Progress and other relief which will be needed in the South during the winter. It was the opinion of Mr. Stevens that practically every additional dollar of pay-roll expenditure in the textile industry would be reflected in a reduction of relief expenditures. The amount which it is proposed the Government expend for promotion purposes - one million dollars - would probably be equivalent to about 500,000 worker days. The employment of 50,000 additional people in the textile mills fourteen days would offset this expenditure if there is the direct relation indicated between textile employment and relief payments.

December 2, 1937

HM, Jr called Secretary Hull at 10:30 this morning and read him the following message to the President which HM, Jr had sent the evening before:

"For the President:

Am dining with the Chinese Ambassador Thursday night and would like to have your advice before seeing him on the following two propositions stop

First comma in view of the possibilities of Japan declaring war am inclined to tell the Chinese that we will buy another fifty million ounces of silver from them over a period of the next ten weeks stop

Second comma our agreement with the Chinese permitting them to borrow foreign exchange against gold on deposit with us expires December thirty first stop I would like to extend this for another year stop

Would appreciate your sending me an answer by radio Kindest regards (Signed) Morgenthau"

HM, Jr then read to Secretary Hull the following reply received from the President:

"From the President.
To The Secretary of the Treasury

0001 in regard to your suggestions please see the Secretary of State I have informed him by wire that I was inclined to go along with them but that both of them might be affected by any later declaration of Neutrality. In the absence of any such declaration of neutrality we should continue our friendly policy just as if there existed no conflict. 2345."

HM, Jr asked Secretary Hull to call him on the telephone and discuss the messages after he had had an opportunity to go over them. He also told Mr. Hull that Oliphant has ruled that even though they put on the involuntary neutrality against China and Japan (see carbon

December 1, 1937

CONFIDENTIAL SECRET

FOR THE PRESIDENT:

Am dining with the Chinese Ambassador Thursday night and would like to have ~~is~~ ~~able~~ your advice before seeing him on the following two propositions stop

First comma in view of the possibilities of Japan declaring war am inclined to tell the Chinese that we will buy another fifty million ounces of silver from them over a period of the next ten weeks stop

Second comma our agreement with the Chinese permitting them to borrow foreign exchange against gold on deposit with us expires December thirty first stop I would like to extend this for another year stop

Would appreciate your sending me an answer by radio Kindest regards

Henry Morgenthau Jr

-2-

of Oliphant's memo of July 15, 1937 and his memo of September 3rd, 1937, attached hereto) that we could continue to buy gold from Japan and silver from China. HM, Jr said that while he had the benefit of Oliphant's ruling, he, HM, Jr, was just being doubly cautious and that was the reason he had sent his message to the President.

December 2, 1937

My dear Mr. Secretary:

In accordance with our telephone conversation, I am inclosing herewith a copy of the message I sent to the President yesterday and a copy of his reply.

After you have had an opportunity to go over these messages, would you be good enough to call me on the telephone.

Sincerely,

The Honorable

The Secretary of State.

TELEGRAM

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The White House
Washington

Copy of Confidential Message Via Naval Communications.

From The President:
To: The Secretary of The Treasury:

(CONFIDENTIAL)

0001 in regard to your suggestions please see the Secretary of State I have informed him by wire that I was inclined to go along with them but that both of them might be affected by any later declaration of Neutrality. In the absence of any such declaration of neutrality we should continue our friendly policy just as if there existed no conflict. 2345.

JUL 15 1937

Secretary Morgenthau

Bernan Oliphant

Re: Neutrality Act of 1937.

A question has arisen concerning the applicability of section 5 of the Neutrality Act of 1937 (Pub. Res. No. 27, 75th Congress) to the Government of the United States. More specifically, does the phrase "it shall thereafter be unlawful for any person within the United States to purchase, sell, or exchange bonds, securities, or other obligations of the government of any belligerent state or of any state wherein civil strife exists, see or to make any loan or extend any credit to any such government," apply to this Government whenever the President shall have issued a proclamation under the authority of section 1 of the act? It is believed that such prohibition does not apply to the Government of the United States.

It may be stated at the outset that the definitive interpretation of the Neutrality Act, being a question of law which would necessarily involve several Departments, is a matter which would be appropriate for the determination of the Attorney General. Sections 564, 566 and 561 of the Revised Statutes of 1878, (U.S.C., title 5, sections 505, 504 and 508). The following discussion is intended for the use of the Treasury Department, pending such definitive interpretation.

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The prohibition in section 8 of the Neutrality Act relating to the purchase, sale or exchange of securities of belligerent governments and the making of loans to such belligerents, is a prohibition upon "any person within the United States." The term "person" is defined in section 13 to include "a partnership, company, association, or corporation, as well as a natural person." There is nothing in the act to indicate that Congress intended to include the Government of the United States within that definition. Indeed, the fact that Congress also specifically set forth in section 13 of the act a definition of the term "state" as including "nation, government, and country", is a rather clear indication that there was no intention to include a government within the definition of the word "person."

There is good authority for the principle of statutory construction that the sovereign is not bound by statutes that may tend to diminish any of its rights and interests unless the sovereign is named in the statute by special and particular words. The rule was well stated in Dollar Savings

Bank v. United States, (1878) 66 U.S. 227, 236, as follows:

It is a familiar principle that the King is not bound by any act of Parliament unless he be named therein by special and particular words. The most general words that can be devised (for example, any person or persons, bodies politic or corporate) affect not him in the least, if they may tend to restrain or diminish any of his rights and interests. He may even take the benefit of any particular act, though not named. The rule thus settled respecting the British Crown is equally applicable to this Government, and it has been applied frequently in the different States, and practically in the Federal courts. (Underlining supplied.)

In United States v. Harrison, (1878) 67 U.S. 221, 235, it was stated
* * * when a statute is general and any prerogative, right, title,

14B

or interest would be divested or taken from the king, in such a case he shall not be bound unless the statute is made by express words to extend to him, &c. &c.

"Sanctioned as that principle is by two express decisions of this court, it would seem that further discussion of it is unnecessary, as it has never been questioned by any well-considered case, State or Federal, and is founded in the presumption that the legislature, if they intended to divest the sovereign power of any rights, privilege, title, or interest, would say so in express words; and where the act contains no words to express such an intent, that it will be presumed that the intent does not exist."

See also Davis v. Finkle, (C.C.A. 4th, 1924) 1 F. (2d) 600, 605; Affirmed, (1925) 266 U.S. 215.

To adopt a construction of the general terms of the Neutrality Act which would divest the sovereign power of a right or privilege which it otherwise possess, would be contrary to the rule of statutory construction above mentioned.

Not only is the Government not specifically mentioned in section 5 of the Neutrality Act, but, as above pointed out, the word "person", as contrasted with "state", has been so defined as to preclude the possibility that the prohibition was meant to apply to the Government of the United States.

Section 5 of the Neutrality Act as finally enacted is couched in language somewhat different from that in the House bill (H.J. Res. 245, 76th Congress), but means the same thing, and covers all of the House bill. (Conference Report No. 728, 76th Congress, page 15.)

Section 5 (that pertaining to financial transactions) of H.J. Res. 245 is practically a restatement of section 2 of Public Resolution No. 74, 74th

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Congress (49 Stat. 1152), which extended and amended the Joint Resolution, approved August 31, 1935 (49 Stat. 1081). The prohibition against financial transactions with belligerents first appeared in Public Resolution No. 74. That that legislation was under consideration the Committee stated:

We feel that this will safeguard and prohibit any credit or transactions undertaken to be carried on in this country by a belligerent country during any warfare, * * * (House Report No. 2001, 74th Congress, underscoring supplied.)

However, it should be pointed out that the phraseology now under consideration is clear and unambiguous and resort may not be had to committee reports and congressional debates in an effort to impart a different meaning to the words. Empire Printing Press Co. v. Dering (1920) 264 U.S. 445, 474; Penn. R. R. Co. v. International Coal Co. (1912) 250 U.S. 184, 189. Such aids are only admissible to solve doubt and not to create it. Ballrod Company v. Chicago B. & O. R. Co. (1922) 257 U.S. 565, 569. The phrase "any person within the United States" presumably was used deliberately by the Congress in the statute, and also the word "person" was defined in section 13 thereof. Nevertheless, the foregoing statement by the Committee on Foreign Affairs, while not admissible under strict rules of evidence in a court of law, is indicative of the spirit of the legislation, and it might possibly be contended that, when Congress enacted the legislation, it had in mind an absolute prohibition of financial transactions of every character in the United States (except ordinary commercial and retail transactions) including those of the Government.

The Johnson Act (49 Stat. 874) by its terms specifically exempts a public corporation created by or pursuant to special authorization of Congress, or a corporation in which the Government of the United States has or exercises

- 5 -

a controlling interest through stock ownership or otherwise. The neutrality legislation contains no such specific exemption and, accordingly, the contention might be made that a government created or controlled corporation would be subject to the prohibition contained in section 3. Such question, however, is not herein considered and no opinion is rendered thereon.

(Signed) Herman Oliphant

JHE-es 7-15-57
Retyped as revised
HOabc 7-15-57

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE SEP 3 1937

TO Secretary Morgenthau
FROM Herman Oliphant

You asked in your telegram of August 31, for a clear-cut positive statement from me as to what duties would fall on the Treasury in case the President should invoke the Neutrality Act against China and Japan or any other country. Particularly, you wish to know whether we would be permitted to continue to purchase gold, silver and foreign exchange from these countries.

The following would be the legal situation:

A. The Neutrality Act would not affect the legal situation of the Treasury at all. Its prohibition of financial transactions with belligerents does not apply to the United States Government because it was not mentioned in the Neutrality Act and the sovereign is not bound by legislation unless specifically named therein.

B. Besides the Neutrality Act, we have to consider the general rules of international law as to unneutral acts. The effect of those rules on the Treasury would be as follows:

1. It would not be an unneutral act for the Treasury to continue, in the ordinary course, to deal in foreign exchange with a belligerent, the purpose being not to extend a line of credit, but to protect the dollar in foreign exchange.

- 2 -

2. It would be an unneutral act for the Treasury to advance a line of credit to a belligerent. Our outstanding arrangement with China is an arrangement to advance credit. The fact that this arrangement was made before a state of war existed would not prevent the advancing of credit under it being an unneutral act.

3. Since it would be just as convenient for China to liquidate her gold now under earmark here as to get a line of credit under our arrangement with her, the next question is as to the law governing her disposition of this gold. This involves four questions: Could the Treasury buy her gold? Could an American bank buy her gold? Could she take the gold to London and sell it? Could she transfer her earmark to Britain, the gold remaining here?

(a) There are no precedents one way or the other on the question whether it would be an unneutral act for the Treasury to buy gold or silver from a belligerent government, the purpose of that government being known to be to acquire dollar credits with which to pay for war materials. Accordingly, the Treasury could buy gold or silver from a belligerent government or decline to do so, depending on how the broad questions of policy involved were determined.

I believe, however, that the sounder position from the point of view of international law would be for this government to refrain from buying gold or silver from a belligerent. Obviously, such broad questions of policy should be considered by the Administration as a whole.

(b) It would not violate the Neutrality Act and would not be an unneutral act for an American bank to buy the gold China has on earmark here, but, for the Treasury immediately to buy this gold from the American bank would come close to raising the unsettled question mentioned in (a) above.

(c) The Treasury would have to give the American bank a license to buy this gold, but it would not have to do anything if China withdrew the gold from earmark and sent it to London for sale, and that would be all right, both under the Neutrality Act and under international law.

(d) Finally, China could leave the gold here, transferring the earmark to Britain. The Treasury would have to authorize this, but there would be no violation of the Neutrality Act or of international law.

It is not believed that an opinion of the Attorney General would be helpful at this time. However, there has been prepared for possible use a request for his opinion on all the points covered by the foregoing, together with the usual opinion of the General Counsel to accompany such request.

Herman Ohlendorf

December 2, 1937. 154

Herbert
Feis:

At a Departmental session, on those two points you raised.

H.M.Jr:

Yes.

F:

And this is about the upshot, which I was asked to pass on to you, first as to the purchase of silver.

H.M.Jr:

Yes.

F:

As far as we can see, no comment.

H.M.Jr:

Uh-huh.

F:

Go ahead if you want.

H.M.Jr:

Uh-huh.

F:

No comment to make. On the second -

H.M.Jr:

Yes.

F:

The Secretary says he thinks his informal advice would be -

H.M.Jr:

Yes.

F:

To keep yourself free of any commitment that you'd have to follow through should there be either a declaration of war or an application of the neutrality proclamation, or both.

H.M.Jr:

Uh-huh.

F:

You see. We'd rather not even have to talk it out with you, as a matter of general international law. That is, we'd like to not make a precedent and not in any way limit our possible future freedom of action, and that's why he asked me to put it to you as a matter of informal advice.

H.M.Jr:

Well now, I - you see - just let me take a minute -

F:

Sure.

H.M.Jr:

Oliphant holds and so advised me that if the Neutrality Act is invoked, that that particular

arrangement with China would not be affected, see?

- F: That's right, under the Neutrality Act.
- H.M.Jr: Yes.
- F: The question of the customary rules of international law.
- H.M.Jr: Yes.
- F: Under the customary rules of international law, loans by a Government to a belligerent Government are contrary to the ordinary rules of neutrality.
- H.M.Jr: Well, this isn't a loan.
- F: Well, it's an advance.
- H.M.Jr: Yes.
- F: Backed on specie.
- H.M.Jr: Yes.
- F: And our legal advisor holds that it would go against the customary rules of neutrality.
- H.M.Jr: Nice spot.
- F: That's only if there's a declaration of war.
- H.M.Jr: I see.
- F: If and what you get is an application of the neutrality act.
- H.M.Jr: I get what.
- F: Just an application of our neutrality act. That's a local action on our part.
- H.M.Jr: I see.
- F: And what the Hell, the rules of international law would be.
- H.M.Jr: I see.

F: Is more difficult. But above all else the Department thinks from its point of view and from yours, it's best to avoid making anything that could be considered a formal precedent, you see. But to you to retain complete liberty to avoid any commitment to them as to making advances should there be either a declaration of war or should we apply our neutrality legislation.

H.M.Jr: Uh-huh. Well, well - here's the point. This thing expires December 31st.

F: Yes.

H.M.Jr: We - I think under our arrangement, have to let them know by the 15th of December.

F: Yes.

H.M.Jr: Whether we're going to renew it.

F: Yes.

H.M.Jr: So that part, I would like Oliphant to have a discussion with your counsel, how's that?

F: Yes. -

H.M.Jr: As to what we should do between now and the 15th in regard to the extension -hello?

F: Yes.

H.M.Jr: In regard to the extension of that which let's call it.

F: Sure.

H.M.Jr: You see they've got fifty million dollars worth of gold here now, against which they have borrowed.

F: Yes.

H.M.Jr: Thirty million dollars worth of yuan.

F: Yes.

H.M.Jr: And which they put up thirty million dollars worth of yuan on their books, in China, to our credit.

F: Yes.

H.M.Jr: And we also have the gold against that as collateral, you see.

F: Yes.

H.M.Jr: Now, I think the best thing to do is to let - I think that you and your counsel and Oliphant and Lochhead and White had better sit down and have a little meeting on that.

F: Whenever you want, but - and now I was thinking from your point of view, as well as from ours -

H.M.Jr: Yes, well I -

F: I can see pretty strongly the way the minds of our legal advisor offices are operating, and if you can get into a formal legal discussion of them - with them, we're going to get, I'm afraid, something restrictive.

H.M.Jr: Yes, but now, wait a minute. Between - I've got to give these fellows - what am I going to do, let this thing expire?

F: Well couldn't you -

H.M.Jr: I mean -

F: Couldn't you carry it along without an agreement?

H.M.Jr: No.

F: Well all right then, certainly yes whenever you want to send Oliphant and the rest over, fine or whenever you'd want Ackworth and his group to come over.

H.M.Jr: Fine.

F: You have Oliphant - do you want Oliphant -

H.M.Jr: Well, I mean we've got to do one of two things between now and the 15th.

F: All right.

H.M.Jr: We've got to either extend it or let it drop.

F: I see.

H.M.Jr: Now the normal thing, not knowing anything about anything would be - would be to extend it - not necessarily for a year, let's say three months.

F: That's right.

H.M.Jr: I mean the normal thing would be - would be just the one existing today with Mexico, I wouldn't even say - let's take Canada. If we had one with Canada that expired on the first of January, the chances are I wouldn't even ask you fellows, I'd just extend it.

F: Yes, but suppose you did extend it and then you got a declaration of war. Would you act under it?

H.M.Jr: Well, I - I would continue until you people advised me to stop.

F: I see.

H.M.Jr: See?

F: Yes.

H.M.Jr: I would continue until you people said no.

F: I see. Well I think your suggestion is the best suggestion.

H.M.Jr: I mean I - don't misunderstand me I'm not trying to put the State Department on the spot.

F: Oh, no, I don't - you're not.

H.M.Jr: And on the other hand -

F: We were - really were trying to avoid putting you in one.

H.M.Jr: Yes. But what I am trying to do is - the terms of the Administration - reason I raised it was that I was trying to avoid an embarrassing situation.

F: Exactly.

H.M.Jr: But I don't see why without any memorandum why this can't be discussed -

F: I agree.

H.M.Jr: See?

F: All right, and Oliphant -

H.M.Jr: As to the silver, buying fifty million ounces, you people have no comment.

F: No comment, no objection either in law or policy.

H.M.Jr: Now, all right, well this is what we'll do. We'll tell them to make a commitment along those lines for the silver you see.

F: Uh-huh.

H.M.Jr: What?

F: Yes.

H.M.Jr: Because, well I'd frankly like to help them out, because I think it's good for United States Government.

F: Exactly.

H.M.Jr: You check on that, don't you?

F: Exactly.

H.M.Jr: Your Embassy in Tokio told us not so long ago, that somebody in a Government bank there said no more gold the rest of this year.

F: Yes.

H.M.Jr: Without by your leave or anything else they put another six million - they put twenty five million yen on the boat, just - just came over this minute from - from the State Department.

F: It's arrived here.

H.M.Jr: No, they - here's the thing, December 2nd, 11 a.m. Referring to Department's telegram and so forth - now find that - well -

practically thirty two thousand certified bars of Japanese gold have been shipped on -

F: Did you say this was from us?

H.M.Jr: Yes, it just came this second.

F: No - I probably haven't yet seen it.

H.M.Jr: It just came this second, signed by Scott.

F: I - I -

H.M.Jr: What's the use of these people telling your representative over there they're through and then they ship another twenty five million yen - I mean to arrive in San Francisco, December 15th.

F: Uh-huh.

H.M.Jr: I mean it, kinda makes me sore, but I don't want - I can say that to you without saying it to the Japs. Think about it, will you?

F: And taken in conjunction with that information that you've got.

H.M.Jr: Yes.

F: That they're building up their balances here.

H.M.Jr: Yes, you know what they are don't you? Forty five million dollars.

F: Forty five million.

H.M.Jr: And here comes another twenty five million yen.

F: Yes.

H.M.Jr: I don't like it. I mean -

F: Well, if you want us -

H.M.Jr: Well, I - I've got to take gold, -

F: You've got to take it, and furthermore if - in one sense the quicker they use it up, I mean -

H.M.Jr: But I'm not going to say anything, except to you, but -

F: All right.

H.M.Jr: I mean what's the use of sending an official of the American Embassy in Japan over to their national bank and they tell him one thing, and then - just don't mean anything.

F: I know it. That's what happens to us the world over.

H.M.Jr: Right.

F: Exactly.

H.M.Jr: All right, now Herbert.

F: Yes.

H.M.Jr: I'll tell our Chinese friends just about this. What kind of a cable did the President send Mr. Hull on this.

F: I've got it here. Wait a minute. Oh, to us?

H.M.Jr: Yes.

F: Nothing.

H.M.Jr: Oh, didn't he?

F: No.

H.M.Jr: Well you notice in my cable he said I'm sending Mr. Hull a message.

F: Well, let me ask Hamilton, the head of our Far East who's sitting here. (aside) Did we get anything from the President on this. - Oh, all it did was to ask Mr. Hull to confer with you.

H.M.Jr: I get you.

F: That's all it said.

H.M.Jr: Well, then this thing is closed, and I will tell Taylor, to arrange for a meeting with you and the people over there.

F: At his convenience.

H.M.Jr: Right.

F: Right.

H.M.Jr: Well, just let me take a minute. Did I tell you about the Holland thing?

F: You did. Has that gone through?

H.M.Jr: Yes. And be - come through next week though!

F: Good.

H.M.Jr: But -

F: I suppose the heads of the newspapers will interpret as a send out -

H.M.Jr: No, because we're handling it through the Stabilization Fund and it won't show up at all.

F: Oh, good.

H.M.Jr: It won't show up at all.

F: Good.

H.M.Jr: And incidentally, in the last fifteen minutes, today, the stock market went up three points.

F: I wonder why.

H.M.Jr: I don't know. Randolph Burgess was in here and he says it's because Marriner Eccles is on the Hill. (laughs) He's not in here now, but I mean he was in here when the market closed.

F: Well if he can do it we'll give him roller skates.

H.M.Jr: No, he isn't in here now, but I meant when he was in here before.

F: Yes:

H.M.Jr: All right. Thank you very much.

F: Thank you.

Mrs. Small

Will you substitute this
memo for the one you have of
the same date, and let me have
the one you now have?

McGuire

From: MR. OLIPHANT

TREASURY DEPARTMENT

163

INTER OFFICE COMMUNICATION

DATE

September 3, 1937

TO

Secretary Morgenthau

FROM

Herman Oliphant

You asked in your telegram of August 31, for a clear-cut positive statement from me as to what duties would fall on the Treasury in case the President should invoke the Neutrality Act against China and Japan or any other country. Particularly, you wish to know whether we would be permitted to continue to purchase gold, silver and foreign exchange from these countries.

The following would be the legal situation:

A. The Neutrality Act would not affect the legal situation of the Treasury at all. Its prohibition of financial transactions with belligerents does not apply to the United States Government because it was not mentioned in the Neutrality Act and the sovereign is not bound by legislation unless specifically named therein.

B. Besides the Neutrality Act, we have to consider the general rules of international law as to unneutral acts. The effect of those rules on the Treasury would be as follows:

1. It would not be an unneutral act for the Treasury to continue, in the ordinary course, to deal in foreign exchange with a belligerent, the purpose being not to extend a line of credit, but to protect the dollar in foreign exchange.

2. It would be an unneutral act for the Treasury voluntarily to extend a line of credit to a belligerent. It is not clear that such an extension of credit would constitute a violation of international law if it were granted pursuant to an agreement with the belligerent government entered into prior to the outbreak of war, for a normal peacetime purpose and without relationship to the existence of a state of war. However, it is not necessary to resolve this question because the agreement with China does not constitute the making of a loan or an extension of credit but is an exchange transaction constituting a part of the United States Government's legitimate program to stabilize the value of the dollar in terms of foreign currencies.

3. Since it would be just as convenient for China to liquidate her gold now under earmark here as to get a line of credit under our arrangement with her, the next question is as to the law governing her disposition of this gold. This involves four questions: Could the Treasury buy her gold? Could an American bank buy her gold? Could she take the gold to London and sell it? Could she transfer her earmark to Britain, the gold remaining here?

(a) There are no precedents one way or the other on the question whether it would be an unneutral act for the Treasury to buy gold or silver from a belligerent government, the purpose of that government being known to be to acquire dollar credits with which to pay for war

materials. Accordingly, the Treasury could buy gold or silver from a belligerent government or decline to do so, depending on how the broad questions of policy involved were determined.

(b) It would not violate the Neutrality Act and would not be an unneutral act for an American bank to buy the gold China has on earmark here, but, for the Treasury immediately to buy this gold from the American bank would come close to raising the unsettled question mentioned in (a) above.

(c) The Treasury would have to give the American bank a license to buy this gold, but it would not have to do anything if China withdrew the gold from earmark and sent it to London for sale, and that would be all right, both under the Neutrality Act and under international law.

(d) Finally, China could leave the gold here, transferring the earmark to Britain. The Treasury would have to authorize this, but there would be no violation of the Neutrality Act or of international law.

It is not believed that an opinion of the Attorney General would be helpful at this time. However, there has been prepared for possible use a request for his opinion on all the points covered by the foregoing, together with the usual opinion of the General Counsel to accompany such request.



Edzer
10yr $2\frac{3}{4}\%$
w

8yr $2\frac{1}{2}\%$

would take

50mil \$ of

10yr -

and good amount

of 8yr.

Dec 1, 1937

Mr. Garner Vice President Guaranty Trust

Mr. Rouse 2nd V.P. in charge of
trading in Govt securities

(over)

2 1/2 To 8 yr. Bond
be worth 3/4 +

167

Dec 2, 1957

Hevine

suggests ~~stop~~ putting
out a \$yr bond
and he would bet
on that exclusively.

Levi - 5 yv 13/4

Dec 2, 1937

Discount Corp

Exp Bond

Nov 2, 1937

Bankers Trust Corp/min

5yr $13\frac{1}{4}\%$
 8yr $2\frac{1}{2}$

Thinks that to do it
 all in a 8yr Bond
 would be too risky

For themselves would prefer
 take 5yr, Bond

Dec 2, 1937

December 2, 1937. 172
3:28 p.m.

H.M.Jr: Hello.

Operator: Mr. Cummings.

H.M.Jr: Hello.

Walter Cummings: Hello.

H.M.Jr: Walter Cummings?

C: Yes, hello Henry, how are you?

H.M.Jr: I'm fine.

C: That's good.

H.M.Jr: Walter, I'd like to have you sort of check with your Government bond people.

C: Yes. .

H.M.Jr: And let me know how they feel about our financing next Monday, see?

C: Yes.

H.M.Jr: We put out this morning what we're going to do.

C: Yes, I got that.

H.M.Jr: And the argument lies between a five year one and three quarters and eight year two and a half.

C: Yes.

H.M.Jr: And I'd like to know how you people feel and what - what you're advice would be.

C: Yes. On the - on the one and three quarters, would that be on the two seventy five exchange?

H.M.Jr: Well, we could work it this way, that whatever we did, we'd give the February the right to convert.

C: I see.

H.M.Jr: See?

C: Well - you know I can tell you right off because I've been giving a good deal of thought to this, and to tell the truth, I was hoping you might call me.

H.M.Jr: Well, shoot.

C: All right. I think your note issue is fine, one and three quarters.

H.M.Jr: Yes.

C: You can make it a little shorter time, if you want to. The second one is absolutely right, eight years, two and a half.

H.M.Jr: Well, some people think we should do a note, some think we should do both, some think we should only do a bond.

C: No, I'd do both, Henry.

H.M.Jr: Do both?

C: Yes, you bet.

H.M.Jr: Well now, if we did both, and had to divide the four hundred and fifty, how would you divide it as between a note and a bond?

C: I'd put out - I'd put out the four hundred and fifty of bonds.

H.M.Jr: Four hundred and fifty of bonds?

C: Yes.

H.M.Jr: Well, where would the note come in?

C: You've got a good chance. Well you're going to issue two seventy seven, the report came - two seventy five and four fifty.

H.M.Jr: No.

C: Oh, well, the reports came to me wrong.

H.M.Jr: No. What - what - the thing is this -

C: They - they quoted you wrong then, Henry, over the ticker.

- 3 -

H.M.Jr: No the Dow-Jones had it all right.

C: Did they?

H.M.Jr: What we're offering is - we're offering four hundred and fifty million dollars cash.

C: Yes.

H.M.Jr: And then the February -

C: Yes.

H.M.Jr: Notes -

C: Yes.

H.M.Jr: The right to convert it into whatever piece of paper we offer for the four hundred and fifty.

C: All right, then you're going to have four fifty plus two seventy five then, aren't you or - let me get this straight now, because I'm confused. Don't you need the four hundred and fifty new money?

H.M.Jr: We need four hundred and fifty new money, and that's all.

C: And that's all, the rest will be just an exchange.

H.M.Jr: That's right.

C: Uh-huh. All right you get four fifty and two seventy five.

H.M.Jr: That's right.

C: Let me - I'll call you back.

H.M.Jr: What?

C: I'll look over my slip to be sure I'm right on this.

H.M.Jr: Now let me say it again. We're offering four hundred and fifty million.

C: Yes.

H.M.Jr: For cash.

C: Yes.

H.M.Jr: Now we've got to decide what that's going to be.

C: Yes.

H.M.Jr: And whatever that's going to be, then the February note will have a right to convert into that.

C: Yes, I see.

H.M.Jr: Do you get it?

C: Yes, I get it.

H.M.Jr: Yes.

C: All right, I'll call you back.

H.M.Jr: Thank you.

C: Thank you.

December 2, 1937. 173
3:57 p.m.

H.M.Jr: Hello.
Walter Cummings: Hello, Henry this is Walter.
H.M.Jr: Yes. I don't hear you awfully well.
C: Oh, hello, Henry, this is Walter Cummings.
H.M.Jr: Yes.
C: Hear me now?
H.M.Jr: Yes.
C: Henry, our first choice on that would be, of course, to issue all bonds.
H.M.Jr: What?
C: Our first choice would be to have you issue all bonds.
H.M.Jr: All bonds.
C: Yes, I'll tell you why. You've got four hundred and fifty five million due in March.
H.M.Jr: Yes.
C: Like to have you clear there to be in a position to issue notes there because we know that they will take, next March and that wouldn't compete with any demands for capital.
H.M.Jr: I see.
C: That would be my first choice.
H.M.Jr: First choice, all bonds.
C: All bonds, eight year bonds at two and a half.
H.M.Jr: Uh-huh.
C: Now if - if you decide that that isn't the wisest thing to do Henry, then I would offer for cash in exchange the new issue, the five year one and three quarter note eight year two and a half per cent bonds and let it fall wherever it would.
H.M.Jr: I see.

- C: You see then you'd be - you'd be dead sure, you know that the entire offer would be accepted.
- H.M.Jr: Yes.
- C: And to show you how I feel about those bonds, as far as our bank is concerned, we would subscribe the limit and be glad to get them, and I think the bond issue would go over very good right at this time and I'd rather have the - placed in bonds now when we're pretty sure they'll take it rather than take a chance next March.
- H.M.Jr: I see. But your bank would take the limit on the bonds.
- C: Yes. We'd take the limit on the bonds. Happy to get them.
- H.M.Jr: How many - under your limit how many could you subscribe to?
- C: Forty five million.
- H.M.Jr: How much?
- C: Forty five or fifty million. Forty five million we can take.
- H.M.Jr: Uh-huh.
- C: I'm sure that our here in this country that that offer would be - that their bond issue would go over good.
- H.M.Jr: Have you talked to any of your correspondent banks?
- C: Yes, we're in touch with them all the time. Practically every day. Had one of them - well we have them every day, we've been talking this thing for two weeks, Henry.
- H.M.Jr: Yes. And that's the concensus of opinion?
- C: Yes, that is out here.
- H.M.Jr: Well would other banks do the same thing out there?
- C: I - I can't - I can't answer for them. I don't know. But I'm sure that this would go - the bond issue would go over very good. You see, you have

- 3 -

no maturities then, you know, in 1945.

H.M.Jr:

Yes.

C:

Looking ahead you've only got one maturity -

H.M.Jr:

Yes.

C:

Due at that date of a million four hundred thousand.

H.M.Jr:

Yes.

C:

What I'm concerned particularly Henry, is looking ahead to March.

H.M.Jr:

Yes.

C:

You know the notes will go fine.

H.M.Jr:

You mean -

C:

Put those out any time and you'd have no trouble next March on that four hundred and fifty five million and nobody could say that the Government was competing with industry or anybody else for money.

H.M.Jr:

Well -

C:

That's my real reason.

H.M.Jr:

Could you talk to some of your friends and call me back tomorrow afternoon and let me know whether they feel the same way?

C:

Yes, I'll sound out a few more Henry, and call you tomorrow.

H.M.Jr:

Will you do that?

C:

Yes, I'll do that.

H.M.Jr:

Thank you.

C:

All right. Goodbye.

MEMORANDUM OF THE DAY'S ACTIVITIES

December 2, 1937

To: Secretary Morgenthau
From: Mr. Magill

1. Tax Revision

The meeting of the Ways and Means Subcommittee was called off today on account of the absence of Congressman Vinson. Vinson called me in the afternoon and said that he was completely exhausted yesterday evening and stayed in bed this morning. He expects to go on with the meeting scheduled for tomorrow.

You may be interested in the following items bearing upon the general situation:

(1) Mr. Kent informed me this morning that he has had several offers to go into practice and is considering accepting one during the next few months. He does not feel that a government career is as attractive as the position he might secure in practice. I told him that I greatly appreciated his good work and that I knew, of course, that he would not wish to resign prior to the completion of our work on this revenue bill. He agreed and said he would let me know whenever any further developments occurred.

(2) Mr. Doughton asked me to listen to a short speech which is to be read for him next Tuesday at a meeting of the National Association of Tax Administrators in Atlantic City. Although the speech is supposed to be on overlapping of Federal and State taxes, Mr. Doughton devotes it all to general remarks on the subject of the undistributed profits tax and the tax on capital gains. He also spends a good deal of space in attacking some of Senator Harrison's remarks in his recent radio speech. I suggested to Mr. Doughton that he ought to mention at least that the Committee is considering other topics than these two and asked him whether he wanted to make as pointed criticisms of Senator Harrison as he had done. He feels very critical of the Senator since it is his view that the Senator's speech is intended to cast aspersions

- 2 -

upon the Ways and Means Committee on account of its adoption of the undistributed profits tax in 1936.

(3) Mr. Olyphant spoke to me, as I believe he did to you, regarding his meeting with fifty congressmen under the chairmanship of Congressman Maverick. As I understand it these congressmen will put up to us the question of providing them with information on questions now pending before the Ways and Means Committee, in order to enable the congressmen to make speeches on the floor. In the telephone call from Mr. Vinson this afternoon I may have had an echo from this meeting. Vinson said he was informed that several Senators were saying that they understood that the proposed undistributed profits tax rates were too low and that they would not yield sufficient revenue. Vinson felt that these Senators had obtained information of the President's position which he thought no one ought to know except the Treasury and Messrs. Doughton, Vinson and Cooper. I said that he must realize that the Senators' information did not come from me and he assured me that he had no such idea.

Rm

COPY

December 2, 1937

My dear Mr. Ambassador:

This will confirm our conversation of even date in which it was agreed that the United States Treasury purchase from the Republic of China an amount of 50,000,000 ounces of silver .999 fine, the proceeds to be used for the purpose of maintaining the stability of the Chinese yuan.

I will instruct the Federal Reserve Bank of New York, as fiscal agent of the United States, to cable bids through the Central Bank of China for the amount of 10,000,000 ounces each on December 15, December 31, 1937, January 15, January 31 and February 15, 1938, based on the market price for silver on the date the bids are made.

Sincerely yours,

(Signed H. Morgenthau, Jr.)

Secretary of the Treasury

His Excellency
Chenting T. Wang,
Ambassador of China,
Chinese Embassy,
Washington, D.C.

Note: Ribbon copies of this report 182
were sent to the following by
the Secretary on December 4, 1937:

The President
The Secy. of State
The Secy. of War - (Attention
Colonel Strong (G-2))

mas
Letters of transmittal were dated 12/4/37
and were signed by the Secretary.)

TREASURY DEPARTMENT

183

INTER OFFICE COMMUNICATION

DATE December 2, 1937

TO Secretary Morgenthau
FROM Mr. Haas

Subject: Current United States trade with Japan and China
(Preliminary data)

United States trade with Japan during the first four weeks of November 1937

(1) United States exports to Japan during the first four weeks of November were considerably lower than during the first four weeks of October of this year.

United States exports to Japan

	<u>First four weeks of November 1937</u>	<u>October 1937</u>	<u>Month of November 1936</u>
1st week	\$ 1,180,000	\$ 1,727,000	For whole month
2nd week	4,813,000	5,746,000	
3rd week	4,745,000	4,492,000	
4th week	<u>3,730,000</u>	<u>6,763,000</u>	
Total 4 weeks	\$14,468,000	\$18,728,000	\$24,100,000

(2) United States imports from Japan during the first four weeks of November were slightly higher than the imports during the first four weeks of October.

United States imports from Japan

	<u>First four weeks of November 1937</u>	<u>October 1937</u>	<u>Month of November 1936</u>
1st week	\$ 3,245,000	\$ 3,325,000	For whole month
2nd week	3,654,000	3,984,000	
3rd week	4,356,000	3,419,000	
4th week	<u>4,027,000</u>	<u>4,060,000</u>	
Total 4 weeks	\$15,282,000	\$14,791,000	\$15,340,000

Secretary Morgenthau - 2

(3) United States export of cotton to Japan remains negligible.

November 1937:	1st week	\$ 97,000
	2nd week	149,000
	3rd week	266,000
	4th week	<u>161,000</u>
	Total	\$673,000

November 1936, whole month \$14,701,000

(4) The major items in our exports to Japan during the first four weeks of November 1937 are given below, with a comparison of the exports during the first four weeks of October 1937:

United States exports to Japan

	<u>First four weeks of November 1937</u>	<u>October 1937</u>
Petroleum products	\$ 4,451,000	\$ 4,216,000
Copper	1,570,000	1,441,000
Industrial machinery	1,383,000	1,345,000
Iron and steel semi-mfrs.	1,171,000	3,580,000
Paper base stocks	940,000	1,106,000
Vehicles, parts & accessories	840,000	634,000
Cotton, unmanufactured	673,000	941,000
Scrap iron and steel	564,000	994,000
Brass	550,000	418,000
Hides and skins	372,000	833,000
Ferro-alloys	356,000	279,000
Fertilizer	234,000	208,000
Industrial chemicals	216,000	133,000
Pig iron	201,000	887,000
Coal tar products	181,000	255,000
Wood	94,000	192,000
Pig lead	41,000	167,000
Photographic & projection goods	13,000	131,000
Other	<u>618,000</u>	<u>968,000</u>
Total	\$14,468,000	\$18,728,000

Secretary Morgenthau - 3

(5) The major items in our imports from Japan during the first four weeks of November 1937 are given below, with a comparison of the imports during the first four weeks of October 1937:

	<u>United States imports from Japan</u>	
	<u>First four weeks of November 1937</u>	<u>October 1937</u>
Silk	\$ 8,094,000	\$ 8,021,000
Cotton manufactures	979,000	1,119,000
Fish	500,000	333,000
Silk manufactures	455,000	456,000
Wood and manufactures	443,000	163,000
Tea	433,000	457,000
Pyrethrum flowers	373,000	260,000
Perilla oil	357,000	307,000
Porcelain and chinaware	308,000	374,000
Paper and manufactures	260,000	237,000
Earthenware	220,000	197,000
Rayon and manufactures	205,000	356,000
Food products - vegetable	193,000	153,000
Glass and manufactures	189,000	136,000
Wool and manufactures	183,000	272,000
Inedible animal products	163,000	331,000
Flax, hemp and ramie manufactures	142,000	135,000
Metals and manufactures	139,000	156,000
Chemicals	94,000	189,000
Lily bulbs	69,000	183,000
Other	<u>1,484,000</u>	<u>956,000</u>
Total	\$15,283,000	\$14,791,000

Secretary Morgenthau - 4

United States trade with China during the first four weeks of November

(1) The value of our exports to China during the first four weeks of November 1937 is already much higher than our exports during the whole of November 1936.

United States exports to

	<u>North China and Manchuria</u>	<u>Shanghai, South China and Hong Kong</u>	<u>Total</u>
<u>November 1937</u>			
1st 2 weeks	\$ 854,000	\$ 770,000	\$1,624,000
3rd week	1,229,000	1,616,000	2,845,000
4th week	<u>573,000</u>	<u>616,000</u>	<u>1,189,000</u>
Total 1st 4 weeks of November	\$2,656,000	\$3,002,000	\$5,658,000

For whole of China, Manchuria
and Hong Kong

Whole month of November 1936			\$3,769,000
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(2) The value of United States imports from China and Manchuria during the first four weeks of November is considerably higher than during the whole of the same month last year.

United States imports from

	<u>North China and Manchuria</u>	<u>Shanghai, South China and Hong Kong</u>	<u>Total</u>
<u>November 1937</u>			
1st 2 weeks	\$ 797,000	\$1,498,000	\$2,295,000
3rd week	396,000	1,121,000	1,517,000
4th week	<u>652,000</u>	<u>1,279,000</u>	<u>1,931,000</u>
Total 1st 4 weeks of November	\$1,845,000	\$3,898,000	\$5,743,000

For whole of China, Manchuria
and Hong Kong

Whole month of November 1936			\$4,659,000
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Secretary Morgenthau - 5

(3) Leading export items to China

(a) North China and Manchuria, first four weeks of November:

Iron and steel semi-manufactures	\$1,510,000
Vehicles, parts and accessories	312,000
Petroleum products	267,000
Tobacco	197,000
Cotton, unmanufactured	168,000
Wood, unmanufactured	61,000
Other	<u>141,000</u>
Total	\$2,656,000

(b) Shanghai, South China ports and Hong Kong

Petroleum products	\$ 808,000
Iron and steel semi-manufactures	524,000
Tobacco	333,000
Vehicles, parts and accessories	231,000
Edible vegetable products	201,000
Printed matter	133,000
Industrial machinery	130,000
Other	<u>642,000</u>
Total	\$3,002,000

(4) Leading imports from China during the first four weeks of November 1937

(a) From North China and Manchuria

Bristles	\$ 787,000
Wool and manufactures	494,000
Leather	98,000
Perilla oil	63,000
Other	<u>403,000</u>
Total	\$1,845,000

Secretary Morgenthau - 6

(b) From Shanghai, South China ports and Hong Kong

Wood oil	\$ 624,000
Tin	622,000
Flax, hemp and ramie manufactures	423,000
Raw silk	412,000
Inedible vegetable products (other than wood oil)	255,000
Bristles	194,000
Food products - vegetable	142,000
Wool and manufactures	139,000
Tea	132,000
Other	<u>955,000</u>
Total	\$3,898,000

TREASURY DEPARTMENT

189

INTER OFFICE COMMUNICATION

DATE

TO Secretary Morgenthau
FROM Assistant Secretary Taylor

On December 3 a conference was held in my office, at which the question of extending the Chinese foreign exchange agreement was discussed. There were present Messrs. Feis and Hackworth, representing the State Department, and Messrs. Olinhart, Lockhead, White, Opper and myself, representing the Treasury. The question was attacked from the standpoint of the Neutrality Act, on the one hand, and the general rules of international law, on the other. Mr. Hackworth was of the opinion that, if this were a loan and war were actually declared between China and Japan, it would be a violation of international law for the United States to enter into the transaction. He was not prepared to say, however, that the same thing would be true if there were a previously existing commitment to make such a loan. I gathered that Mr. Feis did not place so great an emphasis on the international law prohibition as Mr. Hackworth.

On the question of the operation of the Neutrality Act, the representatives of the State Department agreed that the Neutrality Act would not, by its terms, forbid the transaction, but felt that it would be a seriously debatable policy for the United States to enter into a loan or credit transaction which the policy of the Neutrality Act forbade as regards private individuals.

Some time was then consumed in explaining the real purpose and effect of the arrangement from the standpoint of the interests of the United States in the stabilizing of the dollar. It was pointed out, among other things, that the transaction was not entered into for the benefit of China, but for the purpose of stabilizing the dollar, which was a function of the Treasury and a subject in which the United States was vitally interested; that China could obtain dollar exchange by selling its gold and the fact that it had not sold the gold to us was to our advantage; that the transaction had been entered into originally at a time when there was no thought of war, and that if it were extended it would merely be a continuation of an arrangement which had no relation to the existence of a state of war; and, finally, that it could not be compared to a private transaction since its purpose and intent was not to extend credit but to regulate foreign exchange -- a matter with which private interests are not authorized to deal.

At the conclusion of the discussion, it appeared clear that Mr. Hackworth had no doubts as to the legal questions involved, and that, even in so far as it might be necessary for the action to be justified if it were attached, the foregoing and other aspects discussed would furnish considerations upon which the action could be justified. He said, however, that he thought the policy question was generally one which his Department might want to consider further.

W. J.

December 2, 1937

My dear Mr. Ambassador:

This will confirm our conversation of even date in which it was agreed that the United States Treasury purchase from the Republic of China an amount of 20,000,000 ounces of silver .999 fine, the proceeds to be used for the purpose of maintaining the stability of the Chinese yuan.

I will instruct the Federal Reserve Bank of New York, as fiscal agent of the United States, to cable bids through the Central Bank of China for amounts of 20,000,000 ounces each on December 15, December 31, 1937, January 15, January 31, and February 15, 1938, based on the market price for silver on the date the bids are made.

Sincerely yours,

Secretary of the Treasury

His Excellency
Chenting T. Wang,
Ambassador of China,
Chinese Embassy,
Washington, D. C.

AL:ek
12.9.37

December 2, 1937.

Herbert
Feis: At a Departmental session, on those two points you raised.

HMJr: Yes.

F: And this is about the upshot, which I was asked to pass on to you, first as to the purchase of silver.

HMJr: Yes.

F: As far as we can see, no comment.

HMJr: Uh-huh.

F: Go ahead if you want.

HMJr: Uh-huh.

F: No comment to make. On the second -

HMJr: Yes.

F: The Secretary says he thinks his informal advice would be -

HMJr: Yes.

F: To keep yourself free of any commitment that you'd have to follow through should there be either a declaration of war or an application of the neutrality proclamation, or both.

HMJr: Uh-huh.

F: You see. We'd rather not even have to talk it out with you, as a matter of general international law. That is, we'd like to not make a precedent and not in any way limit our possible future freedom of action, and that's why he asked me to put it to you as a matter of informal advice.

HMJr: Well now, I - you see - just let me take a minute -

F: Sure.

HMJr: Oliphant holds and so advised me that if the Neutrality Act is invoked, that that particular

arrangement with China would not be affected, see?

F: That's right, under the Neutrality Act.

HMJr: Yes.

F: The question of the customary rules of international law.

HMJr: Yes.

F: Under the customary rules of international law, loans by a Government to a belligerent Government are contrary to the ordinary rules of neutrality.

HMJr: Well, this isn't a loan.

F: Well, it's an advance.

HMJr: Yes.

F: Backed on specie.

HMJr: Yes.

F: And our legal advisor holds that it would go against the customary rules of neutrality.

HMJr: Nice spot.

F: That's only if there's a declaration of war.

HMJr: I see.

F: If and what you get is an application of the neutrality act.

HMJr: I get what.

F: Just an application of our neutrality act. That's a local action on our part.

HMJr: I see.

F: And what the Hell, the rules of international law would be.

HMJr: I see.

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F: Is more difficult. But above all else the Department thinks from its point of view and from yours, it's best to avoid making anything that could be considered a formal precedent, you see. But to you to retain complete liberty to avoid any commitment to them as to making advances should there be either a declaration of war or should we apply our neutrality legislation.

HMJr: Uh-huh. Well, well - here's the point. This thing expires December 31st.

F: Yes.

HMJr: We - I think under our arrangement, have to let them know by the 15th of December.

F: Yes.

HMJr: Whether we're going to renew it.

F: Yes.

HMJr: So that part, I would like Oliphant to have a discussion with your counsel, how's that?

F: Yes. -

HMJr: As to what we should do between now and the 15th in regard to the extension - hello.

F: Yes.

HMJr: In regard to the extension of that which let's call it.

F: Sure.

HMJr: You see they've got fifty million dollars worth of gold here now, against which they have borrowed.

F: Yes.

HMJr: Thirty million dollars worth of yuan.

F: Yes.

HMJr: And which they put up thirty million dollars worth of yuan on their books, in China, to our credit.

F: Yes.

HMJr: And we also have the gold against that as collateral, you see.

F: Yes.

HMJr: Now, I think the best thing to do is to let - I think that you and your counsel and Oliphant and Lochhead and White had better sit down and have a little meeting on that.

F: Whenever you want, but - and now I was thinking from your point of view, as well as from ours -

HMJr: Yes, well I -

F: I can see pretty strongly the way the minds of our legal advisor offices are operating, and if you can get into a formal legal discussion of them - with them, we're going to get, I'm afraid, something restrictive.

HMJr: Yes, but now, wait a minute. Between - I've got to give these fellows - what am I going to do, let this thing expire?

F: Well couldn't you -

HMJr: I mean -

F: Couldn't you carry it along without an agreement?

HMJr: No.

F: Well all right then, certainly yes whenever you want to send Oliphant and the rest over, fine or whenever you'd want Ackworth and his group to come over.

HMJr: Fine.

F: You have Oliphant - do you want Oliphant -

HMJr: Well, I mean we've got to do one of two things between now and the 15th.

F: All right.

HMJr: We've got to either extend it or let it drop.

F: I see.

HMJr: Now the normal thing, not knowing anything about anything would be - would be to extend it - not necessarily for a year, let's say three months.

F: That's right.

HMJr: I mean the normal thing would be - would be just the one existing today with Mexico, I wouldn't even say - let's take Canada. If we had one with Canada that expired on the first of January, the chances are I wouldn't even ask you fellows, I'd just extend it.

F: Yes, but suppose you did extend it and then you got a declaration of war. Would you act under it?

HMJr: Well, I - I would continue until you people advised me to stop.

F: I see.

HMJr: See?

F: Yes.

HMJr: I would continue until you people said no.

F: I see. Well I think your suggestion is the best suggestion.

HMJr: I mean I - don't misunderstand me I'm not trying to put the State Department on the spot.

F: Oh, no, I don't - you're not.

HMJr: And on the other hand -

F: We were - really were trying to avoid putting you in one.

HMJr: Yes. But what I am trying to do is - the terms of the Administration - reason I raised it was that I was trying to avoid an embarrassing situation.

F: Exactly.

HMJr: But I don't see why without any memorandum why this can't be discussed -

F: I agree.

HMJr: See?

F: All right, and Oliphant -

HMJr: As to the silver, buying fifty million ounces, you people have no comment.

F: No comment, no objection either in law or policy.

HMJr: Now, all right, well this is what we'll do. We'll tell them to make a commitment along those lines for the silver you see.

F: Uh-huh.

HMJr: What?

F: Yes.

HMJr: Because, well I'd frankly like to help them out, because I think it's good for United States Government.

F: Exactly.

HMJr: You check on that, don't you?

F: Exactly.

HMJr: Your Embassy in Tokio told us not so long ago, that somebody in a Government bank there said no more gold the rest of this year.

F: Yes.

HMJr: Without by your leave or anything else they put another six million - they put twenty five million yen on the boat, just - just came over this minute from - from the State Department.

F: It's arrived here.

HMJr: No, they - here's the thing, December 2nd, 11 a.m. Referring to Department's telegram and so forth - now find that - well -

practically thirty two thousand certified bars of Japanese gold have been shipped on -

F: Did you say this was from us?

HMJr: Yes, it just came this second.

F: No - I probably haven't yet seen it.

HMJr: It just came this second, signed by Scott.

F: I - I -

HMJr: What's the use of these people telling your representative over there they're through and then they ship another twenty five million yen - I mean to arrive in San Francisco, December 15th.

F: Uh-huh.

HMJr: I mean it kinda makes me sore, but I don't want - I can say that to you without saying it to the Japs. Think about it, will you?

F: And taken in conjunction with that information that you've got.

HMJr: Yes.

F: That they're building up their balances here.

HMJr: Yes, you know what they are don't you? Forty five million dollars.

F: Forty five million.

HMJr: And here comes another twenty five million yen.

F: Yes.

HMJr: I don't like it. I mean -

F: Well, if you want us -

HMJr: Well, I - I've got to take gold, -

F: You've got to take it, and furthermore if - in one sense the quicker they use it up, I mean -

HMJr: But I'm not going to say anything, except to you, but -

F: All right.

HMJr: I mean what's the use of sending an official of the American Embassy in Japan over to their national bank and they tell him one thing, and then - just don't mean anything.

F: I know it. That's what happens to us the world over.

HMJr: Right.

F: Exactly.

HMJr: All right, now Herbert.

F: Yes.

HMJr: I'll tell our Chinese friends just about this. What kind of a cable did the President send Mr. Hull on this.

F: I've got it here. Wait a minute. Oh, to us?

HMJr: Yes.

F: Nothing.

HMJr: Oh, didn't he?

F: No.

HMJr: Well you notice in my cable he said I'm sending Mr. Hull a message.

F: Well, let me ask Hamilton, the head of our Far East who's sitting here. (aside) Did we get anything from the President on this. - Oh, all it did was to ask Mr. Hull to confer with you.

HMJr: I get you.

F: That's all it said.

HMJr: Well, then this thing is closed, and I will tell Taylor, to arrange for a meeting with you and the people over there.

F: At his convenience.

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HMJr: Right.

F: Right.

HMJr: Well, just let me take a minute.
Did I tell you about the Holland thing?

F: You did. Has that gone through?

HMJr: Yes. And he - come through next week though.

F: Good.

HMJr: But -

F: I suppose the heads of the newspapers will
interpret as a send out -

HMJr: No, because we're handling it through the Stabilization
Fund and it won't show up at all.

F: Oh, good.

HMJr: It won't show up at all.

F: Good.

HMJr: And incidentally, in the last fifteen minutes,
today, the stock market went up three points.

F: I wonder why.

HMJr: I don't know. Randolph Burgess was in here
and he said it's because Marriner Eccles is on
the Hill. (Laughs) He's not in here now, but
I mean he was in here when the market closed.

F: Well if he can do it we'll give him roller skates.

HMJr: No, he isn't in here now, but I mean when he was
in here before.

F: Yes.

HMJr: All right. Thank you very much.

F: Thank you.

December 2, 1937.
3:28 p.m.

200

HMJr: Hello.

Operator: Mr. Cummings.

HMJr: Hello.

Walter
Cummings: Hello.

HMJr: Walter Cummings?

C: Yes, hello Henry, how are you?

HMJr: I'm fine.

C: That's good.

HMJr: Walter, I'd like to have you sort of check with
your Government bond people.

C: Yes.

HMJr: And let me know how they feel about our financing
next Monday, see?

C: Yes.

HMJr: We put out this morning what we're going to do.

C: Yes, I got that.

HMJr: And the argument lies between a five year one and
three quarters and eight year two and a half.

C: Yes.

HMJr: And I'd like to know how you people feel and what -
what you're advice would be.

C: Yes. On the - on the one and three quarters, would
that be on the two seventy five exchange?

HMJr: Well, we could work it this way, that whatever we
did, we'd give the February the right to convert

C: I see.

HMJr: See?

C: Well - you know I can tell you right off because I've been giving a good deal of thought to this, and to tell the truth, I was hoping you might call me.

HMJr: Well, shoot.

C: All right. I think your note issue is fine, one and three quarters.

HMJr: Yes.

C: You can make it a little shorter time, if you want to. The second one is absolutely right, eight years, two and a half.

HMJr: Well, some people think we should do a note, some think we should do both, some think we should only do a bond.

C: No, I'd do both, Henry.

HMJr: Do both?

C: Yes, you bet.

HMJr: Well now, if we did both, and had to divide the four hundred and fifty, how would you divide it as between a note and a bond?

C: I'd put out - I'd put out the four hundred and fifty of bonds.

HMJr: Four hundred and fifty of bonds?

C: Yes.

HMJr: Well, where would the note come in?

C: You've got a good chance. Well you're going to issue two seventy seven, the report came - two seventy five and four fifty.

HMJr: No.

C: Oh, well, the reports came to me wrong.

HMJr: No. What - what - the thing is this -

C: They - they quoted you wrong then, Henry, over the ticker.

HMJr: No the Dow-Jones had it all right.

G: Did they?

HMJr: What we're offering is - we're offering four hundred and fifty million dollars cash.

G: Yes.

HMJr: And then the February -

G: Yes.

HMJr: Notes -

G: Yes.

HMJr: The right to convert it into whatever piece of paper we offer for the four hundred and fifty.

G: All right, then you're going to have four fifty plus two seventy five then, aren't you or - let me get this straight now, because I'm confused. Don't you need the four hundred and fifty new money?

HMJr: We need four hundred and fifty new money, and that's all.

G: And that's all, the rest will be just an exchange.

HMJr: That's right.

G: Uh-huh. All right you get four fifty and two seventy five.

HMJr: That's right.

G: Let me - I'll call you back.

HMJr: What?

G: I'll look over my slip to be sure I'm right on this.

HMJr: Now let me say it again. We're offering four hundred and fifty million.

G: Yes.

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HMJr: For cash.

C: Yes.

HMJr: Now we've got to decide what that's going to be.

C: Yes.

HMJr: And whatever that's going to be, then the February note will have a right to convert into that.

C: Yes, I see.

HMJr: Do you get it?

C: Yes, I get it.

HMJr: Yes.

C: All right, I'll call you back.

HMJr: Thank you.

C: Thank you.