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1. Establish cooperative relationships with Land Grant Colleges and Extension Service - free from suspicion of domination.
 2. Use government financing and handling of agricultural commodities so as to strengthen our permanent system of cooperative service for agriculture (rather than supplant or weaken it.)
 3. Continue agricultural conservation program, redrafted to simplify, to reduce irritations and to provide for sound farm management and permanent agriculture. (Permit adaptation to local conditions.)
 4. Continue machinery for establishing and operating marketing agreements.
 5. Continue services of F.S.C.C. but on an emergency basis and with minimum of publicity.
 6. Expand purchase of submarginal land and studies of land classification to provide basic information for sound land use programs.
 7. Provide government leadership for research and education and extension program through agricultural colleges designed to promote rural health and better standards of living on farms. Reemphasize farming as a safe and desirable way of living through home-raised food and feed, roads, electrification, refrigeration, etc.
 8. Stimulate program of research for development of new uses for agricultural commodities - utilizing existing facilities of agricultural colleges.
 9. A statement on prices to be formulated carefully.
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1. Do not permit pressure groups to formulate national policies - listen to them.
 2. Stop premature publicity on poorly developed plans.
 3. Eliminate C.C.C. loans, liquidate present stocks as rapidly as possible and take losses.



STATE-PLANTERS BANK AND TRUST CO.

RICHMOND, VIRGINIA

December 5, 1938

Hon. Henry G. Morgenthau, Jr.,
Secretary of the Treasury
Treasury Department
Washington, D. C.

Dear Mr. Morgenthau:

I want to take this occasion to commend the soundness of the Treasury's December financing, the complete terms of which have just been announced. It seems to me to give adequate consideration to the various absorptive channels in the market and likewise to give the necessary weight to the Government's desire to borrow on the cheapest terms possible.

The great problem facing banks is, of course, to avoid the shock of gyrations in the government bond market. To a very substantial degree I believe this aim can be attained by the banks having their maturities carefully spaced, with the weight in the scale being assigned in accordance with the condition of each institution's capital account, deposits and assets.

In view of the above, the offering of a 2% nine-year bond was, I think, from the standpoint of the banking system, a master stroke. I would like to urge that in any future government financing you give some consideration to this fact and allow the banking system to acquire at the market level intermediate maturities as well as long term maturities. It will not be necessary to offer this intermediate maturity for new money and the procedure adopted this time can be carried out in the future, varying the maturity date of this intermediate issue more or less in accordance with your own wishes.

If the banking system continues to be afforded the opportunity which you have given in this December financing, it should be able to protect itself against anything other than a catastrophe and it should be able to develop the necessary elasticities to meet varying conditions. A constant ding-donging by the supervisory authorities against too active trading of bonds is sound if the banking system is fed bonds which it can, with justification, hold. This, I feel, you have shown an awareness of for the first time and I want to again commend the policy.

STATE-PLANTERS BANK AND TRUST CO.
RICHMOND, VIRGINIA

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Will you kindly show this to the under-secretary
or whichever of the assistant secretaries handles the government
financing.

Very truly yours,

J. Harvie Wilkinson, Jr.
J. Harvie Wilkinson, Jr.,
Vice President

JHW/ke

RECEIVED
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SECRETARIA OF THE STATE

December 10, 1938.

Mr. J. Harvie Wilkinson, Jr.,
Vice President, State-Planters Bank and Trust Co.,
Richmond, Virginia.

Dear Mr. Wilkinson:

Secretary Morgenthau has read with great interest your letter of December 5th on the subject of Treasury financing, having particular reference to the present offering. He is also circulating it to others in the Treasury who participate in the financing studies.

He wishes me to tell you that he appreciates very greatly getting your views and he wishes that others would write to him as frankly and as helpfully. He would be glad to hear from you at any time when you have comments or suggestions to make.

Very truly yours,

(Signed) Herbert E. Gaston

Herbert E. Gaston
Assistant to the Secretary.

HEG/mah

*approved
by S. Z. F.*

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TREASURY DEPARTMENT

Washington

FOR RELEASE, MORNING NEWSPAPERS,
Tuesday, December 6, 1938.
12/5/38.

Press Service
No. 15-56

Secretary of the Treasury Morgenthau announced last night that the subscription books for the current offering of 2-3/4 percent Treasury Bonds of 1960-65 and of 1-1/8 percent Treasury Notes of series B-1943 closed at the close of business Monday, December 5, for the receipt of cash subscriptions.

Cash subscriptions for either issue addressed to a Federal Reserve bank or branch, or to the Treasury Department, and placed in the mail before 12 o'clock midnight, Monday, December 5, will be considered as having been entered before the close of the subscription books.

The subscription books for both issues, and also for the issue of 2 percent Treasury Bonds of 1947, will close at the close of business Wednesday, December 7, for the receipt of subscriptions in payment of which Treasury Notes of Series C-1939, maturing March 15, 1939, are tendered.

Exchange subscriptions for any of the three issues addressed to a Federal Reserve bank or branch, or to the Treasury Department, and placed in the mail before 12 o'clock midnight, Wednesday, December 7, will be considered as having been entered before the close of the subscription books.

Announcement of the amount of cash subscriptions and the bases of allotment will probably be made on Friday, December 9.

—oOo—

9:30 GROUP MEETING

December 6, 1938.

Present: Mrs. Klotz
Mr. Duffield
Mr. McReynolds
Mr. Haas
Mr. Bell
Mr. Lochhead
Dr. White
Mr. Gaston
Mr. Gibbons
Mr. Hanes
Mr. Cliphant
Mr. Taylor

H.M.Jr: The funniest thing - I looked at Duffield and saw him talking and I was wondering how they let a reporter get in here.

Group: (Laughter)

H.M.Jr: I have nothing except you (McReynolds) might have someone look at the pump in the garage. It has everything in it except gasoline - sand, gravel and water.

McReynolds: They put in a new pump last week.

H.M.Jr: What happens to the Judge?

Gibbons: It goes to the Grand Jury now. We have nothing further to do with it.

H.M.Jr: I see.

Gibbons: I feel sorry for him. I think he is just a

H.M.Jr: Maybe.

Gibbons: I have no information.

H.M.Jr: You have nothing, Mac, I take it.

McReynolds: No. You have your friend Griffith back on hand here.

H.M.Jr: Griffith?

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McReynolds: Yes, the Touhey case in Seattle - the one that complained about the Receiver here.

H.M.Jr: What do I do about it?

McReynolds: I don't know. He is reviving the bank now on Giannini.

H.M.Jr: Well I have a Banking Committee.

McReynolds: I know - I turned it over to them.

H.M.Jr: Incidentally, Preston Delano asked to see me this afternoon. Is there anything - do you know why?

Duffield: He is working on something to talk to Giannini about.

H.M.Jr: Do you think I ought to wait till I see you gentlemen or what?

Taylor: I think he has been talking to everybody on the Committee and so on as to the main points that should be discussed with Giannini. That's what it is about. I gather he has an agreement on it.

H.M.Jr: (To Mrs. Klotz) Tell him 3 o'clock.

(Note: Mrs. Klotz told the Operator the Secretary would see Preston Delano at 3 o'clock. She also wrote it on the Secretary's calendar.)

Hanes: He had dinner last night with Marriner (Eccles). Maybe he wants to tell you about that.

H.M.Jr: He had dinner with Marriner?

Hanes: Yes.

H.M.Jr: Should I worry?

Hanes: No, I don't think so at all. I suggested that he might want to tell you of his conversation with Marriner. I don't think there is anything in the banking group.

H.M.Jr: Well I will see him - see what he has to say.

H.M.Jr: You know my funny story about the man that returned on the steamer. He saw his son on the dock and he yells out, "Hello Jake. How is business? Should I worry?"

Group: (Hearty laughter)

H.M.Jr: I should say, "Hello Preston. Should I worry?"

H.M.Jr: That's one way of announcing that my financing is a success.

Gibbons: On the front page of the Star - the sour note - Marriner playing the.....

H.M.Jr: No.

Gibbons: You were playing the two billion horn and Marriner.....

H.M.Jr: No, we don't take that.

Duffield: The Evening Star - Sunday.

Gibbons: Merrily we must spend, we must spend.

McReynolds: The boss is playing this big bass horn back there and coming out of that (the horn) is, "the deficit is getting bigger - bigger".

Group: (Laughter)

H.M.Jr: I didn't see that.

Taylor: There was a good one in there the day before on Tydings and Glass in giving their announcement on Chicago - Ickes ran for Mayor.

H.M.Jr: O.K., Taylor, got anything else?

Taylor: No, I have nothing.

H.M.Jr: Stay behind a minute, I would like to talk to you.

Gibbons: Nothing.

Lochhead: Sterling is being supported around 4.69.

H.M.Jr: O.K. Wonderful.

Taylor: If agreeable to you, Mr. Gibbons and Mr. Hanes, I would like to appoint Mr. Waite, on the other side, to be one of two negotiators for this international aviation thing, instead of sending somebody over from here.

H.M.Jr: I don't know what it is about.

Taylor: This is an international convention having to do with aviation.

H.M.Jr: Why aren't we in on it?

Taylor: Because it has to do with Customs and so on.
(Note: Mr. Taylor then read the last paragraph on Page 2, of the letter from the Special Deputy Commissioner. A photostat is attached.)
(Exhibit 1)

Taylor: Rather than sending someone from over here I took it, knowing about it, and I think they can do it on the ground there.

H.M.Jr: Fix it up - it is all right with me.

Gibbons: It is a matter of this international aviation. Under the Customs Laws.....

H.M.Jr: Waite is a good man. All right, anything else?

Taylor: Ran into Aubrey Williams last night in a railroad station and he expressed thanks and practically everything else possible about the action of your committee without a name. He said that the President was overjoyed to receive it and so on and thought it would be interesting.

H.M.Jr: I am very much interested in seeing him. From that day to this I haven't heard a peep out of anybody.

H.M.Jr: The President was pleased?

Taylor: Not only pleased but thinks, in the memo about its effect on economy and so on, it will open up a new field of thought, etc., etc

H.M.Jr: Well I am glad to get the message. It is very interesting.

Bell: I didn't think that was new.

Taylor: Well I am just being an honest reporter.

H.M.Jr: I mean the thing that amazed me was that, once it came through, Hopkins didn't get on the phone at once and say something. I certainly would have if I was in his position.

McReynolds: He certainly tried to get the President to do it for him and he wouldn't.

H.M.Jr: Aubrey Williams did too.

Taylor: It was quite a conversation in view of the meeting yesterday. That was the type of thing that had impressed the President so much.

(At this point the White House telephone rang. The Secretary asked Mrs. Klotz to take the message.)

H.M.Jr: What have you got?

Duffield: The request to the RFC for the preferred stock in the Anglo-California is ready for your signature.

H.M.Jr: Now?

Duffield: Yep.

H.M.Jr: Well aren't you fellows going to prepare me?

Hanes: Anytime you are ready.

H.M.Jr: How about a quarter to twelve?

Hanes: Fine.

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H.M.Jr: Anybody who is in on the Banking Committee, will you please be here? Now I think Preston Delano should be here.

Duffield: I will tell him.

H.M.Jr: Right.

Gaston: I suppose you noticed this item in the papers this morning that Martinez Fraga announced in Cuba that the Export-Import Bank had granted a fifty million dollar credit to Cuba.

White: We have no information about that here, except that they were considering a loan to Cuba.

Gaston: They called me up late last night.

Taylor: I can give you some highlights on it, which is that Pierson and Welles have been working on it for three or four weeks.

H.M.Jr: Will you get it for me? Maybe you could tell me at a quarter to twelve.

Taylor: It is supposedly a public works loan.

H.M.Jr: Fifty million is a lot of money.

Oliphant: When is it to be disbursed?

H.M.Jr: George? (Haas)

Haas: I have nothing.

Gaston: Nothing.

Oliphant: I have here a three page memorandum on the Post Office site, giving you what the defenses are. (Hands memorandum to Secretary Morgenthau.) (Note: A copy of this memorandum is attached - marked "Exhibit No. 2").

Oliphant: I am giving you a copy Mac (McReynolds) along with the file.

H.M.Jr: I will read it. Anything else?

White: I don't propose to use it until before noon.
After you see it, I shall change some of the
appendix as written.

H.M.Jr: Well, it is up at the house.

December 1, 1938.

MEMORANDUM FOR:

Mr. Taylor, Assistant Secretary of the Treasury.

Supplementing our conversation of yesterday evening, I discussed this morning with Mr. Thomas M. Burke, Chief of Division of International Communications of the State Department, the proposed multilateral convention suggested by the British Government. In our letter to the State Department of November 1, 1938, copy of which is attached, we expressed our willingness to participate in this convention.

I found that Mr. Burke was particularly interested in knowing whether the Treasury Department intended to send a representative to London. I said that we had discussed the same point last evening and, in view of the limited scope of the convention, had thought that if his division were sending a representative the representative could, after conferences in the Bureau of Customs on the customs point and the Bureau of Internal Revenue on the excise point, handle the matter in conjunction with our European customs representative, Mr. White. I found, however, that Mr. Burke had also reached the conclusion that the convention was not of sufficient scope to justify sending a representative from his division and that he was hoping to work out a team whereby he could have a member of the Embassy in London who was familiar with international negotiations join the Treasury representative. Upon learning that we had customs representatives abroad Mr. Burke thought that a good team could be worked out.

Since there seemed to be agreement in this respect, Mr. Burke asked if the Treasury Department would inform the State Department by letter within the next few days of the party whom the Treasury Department desired to designate. I told him that I would take the matter up with you immediately. Since customs is involved I assume that you will also want to discuss the matter with Secretary Gibbons and probably Under Secretary Hanes. This morning I discussed the negotiations with Commissioner Helvering and Mr. Bliss, Head of the

Miscellaneous Tax Unit, and we are agreed that both the internal revenue point and the customs point, which are practically the same in principle, can be handled by our customs representative. I might add that I met Mr. Waite aboard on several occasions and consider him well qualified to represent the Treasury in this particular negotiation.

If it is desired to designate Mr. Waite to represent the Treasury I assume that the letter now requested by Mr. Burke of the State Department will be prepared in the Customs Bureau but, if you prefer, and will so advise me or Mr. Bliss, it can be prepared in Mr. Bliss' division and routed through Customs. Also, if Mr. Waite is designated I think it is advisable that Mr. Bliss' division prepare a letter to Mr. Waite on the technical aspects of the excise tax point and its relation to the customs point. This letter can also be routed through the Customs Bureau on the way to Mr. Waite. If you desire, I shall be glad to take up with Mr. Bliss the preparation of such a letter.

Edmund P. King
Special Deputy Commissioner.

Nov 1 1938

My dear Secretary:

Receipt is acknowledged of your letter of September 28, 1938 (symbols IN 579.6 A K 1/9) in further reference to letter from your Department dated August 29, 1938, with which was enclosed copy of note from the British Embassy inviting this Government to participate in an international conference in London looking to the adoption of a convention for the exemption from taxation of liquid fuel and lubricants used in international air traffic, to which was attached a tentative draft of such convention as a basis of discussion between the powers participating in the contemplated conference. You request to be advised whether it is the view of this Department that this Government should participate in such proposed conference.

In reply you are advised that, as indicated in letter from this Department dated September 15, 1938, there are found in our existing revenue laws provisions for reciprocal exemption from excise taxes and import duties on liquid fuel and lubricants used in international aviation, which provisions parallel in principle those found in the tentative draft submitted with the note of the British Ambassador. It is, therefore, the opinion of this Department that there exists a basis upon which this Government may agree to a convention such as is envisioned in the note of the British Ambassador, and hence that from the standpoint of this Department this Government may participate in the proposed conference.

It is also the view of this Department that if this Government signifies its intention to participate in such conference it should be made clear that it reserves the right to suggest the amendment or modification of the tentative draft in any manner which appears to its representatives necessary or advisable. It is assumed in this connection that, in the event this Government decides to participate in the forthcoming conference, this Department will be consulted with respect to the scope and terms of the contemplated convention.

In the event further correspondence relative to this matter is necessary, please refer to IR:GC:A-320098

Very truly yours,

(Signed) John W. Hanes

(Acting) Secretary of the Treasury.

The Honorable,
The Secretary of State,
Washington, D.C.

DEC 8 1938

Original m. p. 35

Secretary Morgenthau

Herman Oliphant

There has been submitted to us for approval a proposed acceptance of an offer made by Homer S. Cummings to sell to the United States, for the sum of \$50,000, a tract of land to be used as an addition to the Stamford, Connecticut, Post Office site.

Without making any investigation of the circumstances in the matter, outside of what appears in the file, the following would seem to be the facts:

Mr. Cummings has owned the property at least since 1929. The H.O.L.C. has appraised the property at \$50,000. The property has an approximate frontage of 132 feet. The property between the present site and Mr. Cummings' property is also being purchased. The price proposed to be paid to Mr. Cummings per front foot is less than that proposed to be paid to the owner of the intervening parcel. The assessed value of Mr. Cummings' property is \$24,200.

The present Post Office site is in the middle of the block and the only other property available for the extension is the property on the other side of the Post Office upon which is located a Y.M.C.A. building, and the purchase of this property would entail a much larger expenditure than the property owned by Mr. Cummings and the adjoining property owner.

There does not seem to be any statutory prohibition against this transaction. Section 41 of the Criminal Code (act of March 4, 1909, 35 Stat. 1088, 1097) (U.S.C. title 18, sec. 93), which is the only statute applicable to sales to the Government by officials extends only to employees who are officers or agents of the seller and not to principals. The Comptroller General, in general language, has indicated that this act applies also to principals. However, such language may be disregarded in view of the express terms of the statute, which is penal, and has to be strictly construed. The Attorney General has held that such statute applies only to agents and not to principals.

Aside from any statutory prohibition, however, there is reason to believe that the Comptroller General, following decisions heretofore made, will hold that the transaction is void on the grounds of public

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policy. Before the site can be acquired and the check drawn for the purchase price, the warrant has to be countersigned by the Comptroller. Because of this the matter will be before the Comptroller prior to the closing of the transaction.

The Comptroller has held that the following transactions are void on the grounds of public policy:

1. Contracts by Government employees to rent automobiles to the Government, even though the employee is not the negotiating or contracting officer.
2. Contracts between a Public Health surgeon, who is the contracting officer, and himself, as proprietor of a private hospital, even though the hospital was the only one available in the vicinity.
3. Sales of tractors by an employee of the Virgin Island Government, after public advertisement, even though the employee was not the contracting officer and had nothing to do with the transaction in an official capacity.

A study has been made of the general law of public policy in so far as it is applicable to this type of transaction. Most of the authorities deal with the situation where the Government employee secretly, or otherwise, acts as agent for the contractor and while they do not cover our situation, they do contain general language as to the suspicion with which the law looks upon transactions between employees in their official capacity and acting in their own personal interest.

The nearest case to our situation is found in Mayor and Council of City of Macon v. Huff, 60 Ga. 221. In that case the City Council leased a piece of property to the then Mayor for a certain term of years and the Mayor as part of the consideration for the lease agreed to do certain things such as cutting wood and distributing it to the poor. After the execution of the lease there was a change in personnel in the City Council although the Mayor was reelected. An action was brought by the City against the Mayor to void the lease. The Court held that, even though the Mayor did not have the duty of negotiating and executing leases, he did have the general duty as Mayor of the City to see that agreements on behalf of the City were faithfully executed by the other parties to the agreement and that as part of his general duty he was required to see that the lease was properly performed. Because of this relationship, the Court held the lease void on the grounds of public policy.

In our case Mr. Cummings has nothing to do officially with the negotiation or execution of the contract. He has the duty, however, of certifying to the title under Section 355 of the Revised Statutes, as amended (U.S.C. title 40, sec. 255), and no money can be expended upon any site until the written opinion of the Attorney General shall be had

In favor of the validity of the title. In the closing of title it has been the practice of the Procurement Division that the vendor, after acceptance of the offer, furnish evidence of title to the United States Attorney or Special Attorney designated by the Department of Justice who examines the title and forwards his report to the Attorney General. The Department of Justice then furnishes a preliminary opinion signed by, or for, the Attorney General as to the state of the title. If the title is marketable the Procurement Division forwards the preliminary opinion of the Attorney General, the abstract, and supporting papers, to the General Accounting Office with the request that a check be issued for the purchase price and forwarded to Justice. The Department of Justice, upon receipt of the check, transmits it to the United States Attorney for the closing of the title.

If any suit is brought in the Court of Claims concerning the contract, it will be the duty of the Attorney General to defend the action and to assert any counter-claim available to the Government. This might involve a breach of warranty on the part of the grantor. The Department of Justice generally, under the supervision of the Attorney General, also will represent the United States in any other litigation in connection with the contract.

It is quite possible that a Court, following the decision in the Georgia case, cited above, might hold that the Attorney General had such an official interest in the contract as to render it void.

It is my judgment that the matter should be formally submitted to the Comptroller with a statement of all the facts in the matter, especially because it must be cleared with him prior to closing. The courts have permitted trustees of estates to deal with themselves individually upon a submission of all the facts to the Court for advance approval. It may be that this analogy may be used in submitting the matter to the Comptroller General.

(Initialed) H O

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE

DEC 6 -- 1936

TO Secretary Morgenthau
FROM Herman Oliphant

For your information

Judge Townsend in the opinion section of the Department of Justice called Cairns today and said he was preparing an opinion on the German matter and was inclined to agree with the Treasury's position. He wanted to see the press release of December 23, 1936 and our letter to the State Department of December 5, 1936, of which the press release was a condensation.

Cairns will take these documents to him in the morning and answer any questions he may ask. He will try to learn about when the opinion can be expected.



EDA

HANKOW VIA N.R.

Dated December 6, 1938

Received 7 a.m. 7th

Secretary of State

Washington

December 6, 9 a.m.

Hong Kong's December 3, noon, asking for comments on United States Government report that Yangtze River open to commerce and wood oil now on the way from Hankow.

Similar inquiries have been received from the United States by two leading American wood oil exporters here. The source of the report is attributed to the Department of Commerce by one of them.

The Yangtze River is not (repeat not) open to commerce. Inquiries among wood oil firms reveal that the Japanese have not acquired any stocks of wood oil at Hankow either by purchase or by confiscation. No foreign commercial vessels and no lighters with wood oil have left Hankow for down river since the Japanese occupied this center. While it is conceivable that a few tons of wood oil may have been found and confiscated by the Japanese military forces as they advanced along the Canton-Hankow Railway it is doubtful whether total could be more than

EDA - 2 - December 6, 9 a. m. from Hankow

than 50 or 60 tons, if that much. No positive information on this last is available yet.

Repeated to Hong Kong, Shanghai.

JOSSELYN

DDM :WWC

Confidential

P A R A P H R A S E

A confidential telegram (No. 579) of December 8, 1938, from the American Ambassador at Chungking reads substantially as follows:

On December 4 a member of the Embassy staff was informed by the Acting Director General of the Foreign Trade Commission that the exportation of bristles is proceeding normally by truck to Yunnanfu. With reference to the wool trade in the northwest, he stated that more than five thousand tons of wool had been carried to Soviet Russia by camel during the past year and that steps had been taken also to prevent shipments of wool from going into territories controlled by the Japanese. This official stated also that an average of twenty tons of tung oil is being carried each day by means of mule and coolie transport to Yunnanfu via Suifu. He declared that, although, of course, freight rates will be considerably higher, this means of transportation is being so enlarged as to preclude a shortage of tung oil in the consuming markets of the world.

The above-mentioned Foreign Trade Commission is an official organization which controls now almost all of the export trade of that part of China controlled by the National Government.

6001939/261

Handwritten initials



THE COMMANDANT OF THE UNITED STATES COAST GUARD

WASHINGTON

6 December 1938.

*Do the Secretary
you requested
written report of
this meeting!*
G.B.G.
12/9/38

MEMORANDUM FOR - The Secretary of the Treasury,
(via Assistant Secretary Gibbons).

Subject: U.S. Maritime Service - training.

On Monday afternoon, 5 December 1938, Assistant Secretary Gibbons called a conference in his office, at which were present, in addition to the Assistant Secretary: Assistant to the Secretary Herbert E. Gaston (who remained only during the early part of the conference); Mr. Gardner Jackson, an Advisor to the National Maritime Union; Rear Admiral R. R. Weesche, U.S.C.G.; Lieutenant Commander G. E. McCabe, Commanding Officer, Maritime Service Training Station at Hoffman Island, New York; Lieutenant Commander G. B. Gelly, U.S.C.G.; Mr. Jerome King, Secretary of the National Maritime Union; and Mr. Ralph Emerson, Legislative Representative of the National Maritime Union.

The conference was called to discuss certain changes in the regulations for the training of maritime personnel, proposed by representatives of the National Maritime Union. No difficulty whatever was encountered in coming to an agreement on the proposed changes.

Upon completion of this conference, Mr. King and Mr. Emerson of the National Maritime Union, and the representatives of the Coast Guard, met in conference at Coast Guard Headquarters, and remained together until detailed amendments to the regulations were written, satisfactory to both the Coast Guard and the National Maritime Union. These amendments, signed by the Commandant of the Coast Guard, were transmitted via registered mail today, to Mr. Jerome King, Secretary of the National Maritime Union at New York, and it is confidently expected that this will result very shortly in the officers of the National Maritime Union giving their approval to the training system of Merchant Marine personnel now being conducted by the Coast Guard.

As far as is now known, every objection made by the National Maritime Union to the training system has been satisfactorily met, and full cooperation between the union and the Coast Guard is expected in the future.

- #2 -

The Commandant is having lunch on Thursday, 8 December 1938, with Mr. Gardner Jackson, and will, thereafter, confer with Mr. Jackson from time to time, as may be deemed necessary, to insure full confidence and understanding in the training of Merchant Marine personnel.



R. R. WAESCHE
Rear Admiral, U.S. Coast Guard,
Commandant.

RECEIVED
OFFICE OF THE
COMMANDANT

DEC 10 11 15 AM '38

RECEIVED

December 6, 1938,
10:10 a.m.

Williams: Hello.

HMJr: Professor Williams.

W: Yes.

HMJr: Morgenthau.

W: Oh, yes, Mr. Morgenthau.

HMJr: How are you?

W: Fine. How are you?

HMJr: Well, I feel pretty good after yesterday's financing.

W: Yes, I should think you would.

HMJr: Mr. Williams, this so-called Fiscal/ Monetary Committee. and

W: Yes.

HMJr: They put up something to me yesterday which was prepared by the economists of the National Resources Board.

W: Yes.

HMJr: They set up this budget in a new way. It shows the inflation and deflation are the effects of -- on collection of taxes and on our spending.

W: Yes.

HMJr: Now, on the surface it looks awful good.

W: Yes.

HMJr: But it may be ga-ga, see? Now what I'm doing and what I'm trying to get -- it's a very complicated thing and they've got a lot of things -- these multiples which they use, and I'm trying to get you and Stewart and Viner to come down here Friday and Saturday, and to see whether this thing will stand up; because I don't want to show it to the President unless what I call my senior economists have looked at it, you see?

W: Well, I know something about it in a general way. I mean I know of those who have been interested in that point of view and some of their ideas, and I would like very much to go over it.

- 2 -

HMJr: Well, I'm really interested and bothered, and I've gotten ahold of Viner , he's coming.

W: Yes.

HMJr: It's really a two day's job, I think, and if you could spend Friday and Saturday here I'd appreciate it tremendously.

W: I think I could. I have to change my program around because we have a Seminar and we have a class on Friday, but I think I can arrange that.

HMJr: Well I'm going to try to get Hanson to.

W: Well, he's in the same fix as me. He's running a Seminar. We run it together.

HMJr: Would you ask him whether he could come also?

W: Well, if we are both away from that Seminar I don't know quite what we'll do.

HMJr: Gosh!

W: Suppose I talk it over with him and see what the possibilities are? He'd be free on Saturday, I think. The question is about Friday.

HMJr: What I was thinking was that you people could get these men. I told them -- I told White and Curry who are going to present this that they are going to be put on the spot and they say "Fine". What I thought is that if you fellows could just try to rip this apart, look at it and then I'd like to sit down with you Saturday, but I can't go into all the technical details behind it.

W: No.

HMJr: You see?

W: It wouldn't be possible for us to have a copy of it in advance?

HMJr: Well, no.

W: There is just one copy?

HMJr: There is just one copy and I'd send it up in a minute, but talk it over, and maybe one of you could come Friday and both of you be here Saturday.

W: I think that is possible.

- 3 -

HMJr: Will you call me back later on?
W: Yes, I'll call you back later in the day.
HMJr: Call me collect.
W: Alright.
HMJr: Will you?
W: Alright, I will.
HMJr: And then, will you speak to Hanson?
W: I'll talk to him right now.
HMJr: Thank you.
W: Alright.
HMJr: I make great importance on it because if it's alright then I want the President to use that philosophy and mention it in his budget message, but I don't want to present it to him until you fellows have used a can-opener.
W: Well, I'm awfully glad to be called on, because, as I say, I've been aware of some of the ideas and plans and I think it is awfully important.
HMJr: Well, I do too.
W: That we go into it thoroughly.
HMJr: Right!
W: Yes.
HMJr: Thank you.
W: Alright, good bye.
HMJr: Good bye.

December 8, 1938.
10:26 p.m.

27

HMJr: Hello.

Operator: Dr. Bowman. Go ahead.

HMJr: Hello.

Bowman: Good morning, Mr. Morgenthau.

HMJr: How are you?

B: First rate.

HMJr: Dr. Bowman, I got your letter and the statement for the money, and there is just this thing which has cropped up -- the first statement of a hundred odd dollars for work done by the National Geographic.

B: American.

HMJr: American -- yes, I haven't got the letter right before me. Well now that -- I don't -- there won't be any trouble about the Treasury paying for that. If my man may want to get in touch directly with them to have them break it down in the way the Treasury's red tape calls for, you see?

B: Yes.

HMJr: Another thing I find -- this man that you brought on at my request of the west coast -- he's not an American citizen, is he?

B: That's right.

HMJr: Well, then I'll have to -- I find I can't pay him on the Treasury so I'll have to pay him out of my own pocket.

B: Oh, you don't want to do that. Isn't it possible to shift that to some of the rest of the organizations?

HMJr: Well, I don't like to do that. So what I thought would be this -- if you could have him make out a bill, and I hate to bother you with this stuff.--

B: Well, I'll be seeing him day after tomorrow anyway.

HMJr: What his railroad fare was, and oh, we'll pay him for a couple of weeks or something like that, you see?

B: Yes.

- 2 -

HMJr: And then I'll make out a check to the University and the University can pay him.

B: Yes.

HMJr: Then you might give me a little estimate as to how long it will last.

B: That to I'll be able to learn from him day after tomorrow.

HMJr: Because I had forgotten all about this rule which was passed that you could only hire American citizens, and so -- I'd like to pay him his railroad fare and his work for oh, say, through -- up to maybe the fifteenth -- so -- I mean that he will be paid. Then let's figure how much longer after that he'd have to stay, you see?

B: Yes, yes, first rate.

HMJr: Pardon? And I've got McRaynolds here, my administrative assistant. Do you -- he is just raising a thumb -- what do you say Mac? (Talks aside to McRaynolds) -- Well, McReynolds says he thinks we can pay his railroad fare.

B: Yes.

HMJr: The Treasury Can,

B: I see -- yes.

HMJr: So that may help, but if the check could be made out, but I hate to bother you.

B: That's alright.

HMJr: Up to the fifteenth.

B: Yes.

HMJr: And then, let's find out how much longer it will take.

B: Yes.

HMJr: That would be helpful.

B: That will be fine. If you want to send that bill back I'll send it up to the Society and have them break it down any way --

HMJr: Well, I won't bother you. I'll have McReynolds -- I'll turn the bill over to him, and just let him deal directly with the Society, if that's agreeable to you. Is that alright?

- 3 -

B: Yes, that will be fine.

HMJr: Did you get anything out of Rosen?

B: Well, he wrote me about British Guiana -- that was after he called. He asked a number of questions. I found he was in possession of a copy of my letter to the President and the McBryant Telegraph.

HMJr: Yes, well, I want to explain that and that's one of the reasons I

December 6, 1938.
11:04 a.m.

30

HMJr: Hello.

Harrison: Good morning, Henry.

HMJr: Hello, George.

H: Henry, this thing is boiling down here still.

HMJr: Yes?

H: And it's going over tremendously. One thing is worrying us quite a bit -- it is the number of these thousand dollar subscriptions.

HMJr: Yes?

H: Which are being dreadfully abused in every way -- I mean, families, and clerks, and servants, all put in -- the boss putting in one check, his own check, and then individual subscriptions for all of his family, relatives and friends.

HMJr: That's the way they are doing it, eh?

H: Yes, and -- of course, there are a number who are legitimate subscribers for a thousand dollar bond, but I think that in view of the publicity in Scribners and elsewhere, about telling people how they can make a rake-off on this thing --

HMJr: In Scribners?

H: What?

HMJr: In Scribners?

H: Yes.

HMJr: Oh, I didn't see it.

H: OH -- it pointed out the whole way whereby you could by subscribing for five thousand dollars, how you could make seventy-five dollars in one day.

HMJr: I didn't know that. In Scribners?

H: Yes.

HMJr: I see.

H: And there has been a lot in the papers to so that we have already here about ten times as many one thousand dollar subscriptions as we ever get, and you will find probably

- 2 -

that it is more true in other districts where they have more thousand-dollar subscriptions than we do anyway, and what I was thinking was that you might get the Board, or you yourself, to ask the other Reserve Banks to compile for you the number of thousand-dollar subscriptions you are getting and keep you posted so that when you come to make your allotment you can determine what to do about that.

HMJr: Yes.

H: I feel -- frankly, as I see it now, I think the only way you are going to lick this thing is perhaps not to make any exemption at all, but to give these fellows their ten percent -- give them the hundred minimum for their hundred dollars.

HMJr: Well, not this time though.

H: Well, I think I did this time.

HMJr: Have we the authority?

H: What?

HMJr: Have we the authority?

H: Well, they tell me downstairs you have. You haven't committed yourself to allot up to a thousand.

HMJr: Yes.

H: Alright, now -- ah, I'm mentioning that ^{to you} to think about, but that's the way we all feel at the moment here, and if you talk to your men about it there and see whether you are sure about this, authority-- and I'm sure you have got it. It is on this theory that while you were out out, some legitimate investor for a thousand -- you could at the same time announce that those fellows that want to legitimately invest a thousand dollars can do better on a Baby Bond.

HMJr: That's right.

H: Because they get a better yield on a Baby Bond.

HMJr: That's right.

H: And the whole thing is that it is just a racket to try to make a rake-off, and you will find all these fellows spending their bonds again to take the premiums.

HMJr: You think we ought to have the other Feds figure up how many one-thousand dollar ones?

H: Yes, just make a special report to you --interim-report -- on the volume of thousand-dollar subscriptions as compared with previous issues.

HMJr: I'll do that right away.

H: I think it would be worth while and I think it would be interesting to you, because here, as I say, we are getting about ten times as many and it is due to all this fool publicity about how a fellow can make ten, or fifteen, or twenty dollars profit over-night.

HMJr: O.K.

H: O.K.

HMJr: Thank you very much.

Gambling in Governments

S. F. PORTER

AN INQUIRY into free riding in Government bonds . . . \$80,000,000 profits in half a decade . . . 15% in a week . . . the world's simplest, safest way to double money

EVERY so often the financial pages make casual reference to a practice called "free riding." To the uninitiated, this might mean anything from hitchhiking to snatching the brass ring on a merry-go-round. To those in the know, it stands for a simple, quick, and amazingly safe way to make money.

A free rider is a person or institution that subscribes for a block of new Government bonds and sells them at a profit before the date when full payment for the bonds is due. In the past six years there have been opportunities for thirty-four free rides in the Government market, reflecting the sale of nearly \$15,000,000,000 in new Treasury securities. The profits? Impossible to calculate accurately, but somewhere around \$80,000,000. The risks? Infinitesimal, for each of these thirty-four flotations was managed by the Government in such a way as to assure profits for the free rider.

This is how it works. The Treasury usually begins its preparations for a bond issue five or six weeks before it announces the terms of the new offering. Actually, it is preparing to borrow money. A man approaching his bank for a loan puts up a good front; he straightens out his financial records, talks big and confidently. The United States Treasury does the same thing on a larger scale. It releases some cheering news to stimulate the prices of prime-grade bonds. Both the Treasury and the Federal Reserve Banks are likely to borrow a few million dollars' worth of Government bonds to lift prices and give the market color and zip. Secretary Morgenthau confers with leading bankers and bond dealers to discover what interest rates and maturities would be best.

In short, the market is "dressed" and then, presto! comes the announcement. (September 8, 1938) "The Secretary of the Treasury . . . invites subscriptions, at par and accrued interest, from the people of the United States for 2½ per cent bonds of the United States, design-

ated Treasury bonds of 1950-52. The amount of the offering is \$400,000,000 or thereabouts. . . ."

Also in the announcement are details on the methods of subscribing; on the right of the Treasury to reject subscriptions; on the fact that banking institutions generally may submit for account of customers cash subscriptions without deposit. And there is one sentence which paves the way for the free rider: "Cash subscriptions from all others must be accompanied by payment of 10 per cent of the amount of bonds applied for. . . ."

When the Treasury offers new bonds it always allows a week to ten days to elapse between the date of offering and the date when purchasers of the obligations must pay up and take their bonds home. It is during this period that the free rider operates—a week during which, for all intents and purposes, he owns the obligations on a 10 per cent margin and during which they are being traded in the market just as though they had been outstanding for many years. Before that period is ended, the free rider sells his Government bonds to buyers who had wanted them all along.

II

HERE was the routine followed by a free rider—call him John Broadstreet—during the past September flotation.

Immediately after the disclosure of the terms of financing, Broadstreet (with funds and securities on which he could raise \$100,000 in cash for seven days) telephoned a dealer in United States Government securities and asked whether the bonds were worth more than the formal offering price of 100. He was told that the Treasury had been as generous as usual and that, according to the prices at which comparable outstanding Government obligations were selling, the 2½ per cent bonds were worth at least 101½, or \$1015, thus making the immediate profit to any buyer \$15 a bond.

Broadstreet, therefore, was ready to

proceed. He went to the New York Federal Reserve Bank and obtained the blank for cash subscriptions to the United States Treasury 2½ per cent bonds due in 1952. On the blank, he filled in the date, the space reading "Please enter my subscription for \$....." with the figure \$1,000,000, and signed his name and address. He then turned in the blank with his check for \$100,000—10 per cent of his total subscription—got a receipt for his money and went back to his business.

The first part of the free-riding transaction was finished.

Broadstreet had the entire day of September 8 to place this order. He might have waited until late evening and mailed his subscription directly to the Treasury Department. If he had lived in another city, he could have gone to the Federal Reserve Bank in his district, or, wherever he lived, he could have asked his bank or broker to place the subscription for him. And, of course, he might have ordered fewer bonds, depending upon the amount of cash he could raise.

At midnight, the Treasury closed the books on subscriptions to the new bonds, reflecting the fact that orders had been so overwhelming that it was unnecessary to solicit further orders. Two days later the Treasury revealed that it had received subscriptions of more than \$4,487,000,000 for its \$400,000,000 offering of bonds and that, therefore, subscribers would be allotted only 10 per cent of the total they had ordered. (Secretary Morgenthau added, however, that all subscriptions for \$1000 would be allotted in full and that the smallest allotment on any subscription would be one \$1000 bond. This, naturally, was a break for the smaller investors.)

Now comes the second part of the free ride. As soon as Broadstreet was notified by the Federal Reserve Bank that he had been awarded 100 bonds—10 per cent of a \$1,000,000 order—he prepared to

sell them at the market price. He telephoned his dealer again, learned that the new 2 1/2 per cent bonds were selling at 172 points over his purchase price and then, over the telephone, sold them. He told the dealer that the New York Reserve Bank would deliver the bonds to him on September 15, and he asked the Bank to deliver his bonds to the dealer specified.

On September 15, the dealer got Rosalston's bonds from the Bank and with him a check for his \$100,000 plus a profit of 1 1/4 per cent on each bond—or a total profit of \$1500. Although Broadstreet's deposit was tied up for seven days, he actually made his profit in less than an hour. He never had any intention of holding his bonds. He had bet on a sure thing.

Just to bring matters down from the \$100,000 class, I can cite my own experience. With only \$500, I took a free ride on the September offering. Knowing that the Treasury would not allot less than one bond on a subscription, I placed my order for one bond on a deposit of \$100 and used my remaining \$400 to place subscriptions for one bond each in the names of my aunt, my uncle, my cousin, and my brother. I went through the same procedure Broadstreet did: checked the profit possibilities with a bond dealer; went with my "proxies" to the Federal Reserve Bank and placed the orders; then sold my five \$1000 bonds at a profit of \$15 each. Altogether my free ride took about a half-hour. My profit was \$75 on an investment of \$500 for seven days.

There are no class distinctions in the free riders' fraternity. Speculators, big institutional investors, and just people with cash rub elbows at the Federal Reserve Banks on subscription day. I know of one man who figures that he has doubled his money by free riding. Early in 1931 he inherited \$50,000 and quit working so that he could manage his new fortune. Jittery about the normal risks in stock speculation, he spent most of his time worrying. Finally someone told him about free riding. He has taken a rule recovery cash issue of Government securities since 1934 and today is worth over \$100,000.

Another acquaintance boasts a 265 per cent capital appreciation through this maneuver. A third says he has increased his capital 480 per cent by free riding since 1933. And a well-known Wall Street house has met an expensive operating overhead from profits realized during free-riding periods.

Let anyone say the Government stifles initiative; consider the two young spec-

ulators who were so charmed by the trick that they went into free riding as a business. They put out a shingle announcing themselves as foreign-exchange dealers, although they hadn't the remotest idea of how to translate pounds into francs or marks into pesos. They simply knew how to catch a ride on new security issues and they used every dollar they could get for this one purpose. Later, when they decided they had used the foreign-exchange blind long enough, they moved to a new office, printed new stationery, and continued their operations. As far as I know they are still going strong.

It's also possible to be overenthusiastic. For some time before the December, 1936, bond issue was announced a certain broker had been busy collecting the names of friends and relatives that he could use to mask the extent of his operations. On subscription day he mailed to the Federal Reserve Bank order forms in the names of twenty-nine persons. In his haste and excitement, however, he made a sad error; he sent all the forms in envelopes bearing his firm's name. And an alert secretary at the Bank noticed the phenomenal duplication. The broker was called to the Bank, questioned, and sent away smarting under official reprimand. Even so, he was permitted to enter subscriptions for himself and his wife. During the next Treasury issue, he used blank envelopes.

III

THE question of risks involved in free riding is tied up with recent developments in the history of the United States Government bond market.

In 1836, the gross public debt of the United States amounted to only \$38,000. Today it is more than \$18,000,000,000, an increase of one hundred million per cent. From 1836 to 1918, there was no appreciable Government bond market. It really came into being with the World War, when the United States became a major nation, and a borrower with a \$26,000,000,000 debt. The prosperous period between 1918 and 1930, however, jacked up the Treasury's surplus and enabled it to pay off all but \$16,000,000,000. And then, in 1933, a new concept of government was born—one which held that the Government had a right and an obligation to feed and clothe its needy, to stimulate its industries. That meant borrowing again on a tremendous scale, and subsequent growth in the Government bond market which has made other exchanges look insignificant. To meet the vast deficits incurred in its spending program, the Roosevelt Administration had to have a special place

to borrow. It went to the banks—via its own market.

The success of the Administration's program during the past six years has depended considerably upon the good condition of the market. The Treasury has it completely in hand. With the billions of dollars at its disposal and with the help of the Federal Reserve System, it buys when prices weaken, sells when prices advance. In March, 1937, for instance, when the business slump was getting off to a fine start, the Treasury threw its support behind the Government market and picked up \$119,553,000 of its own bonds. In one week during August, 1934, when all world markets were suffering from the shock of Austrian Chancellor Dollfuss' assassination, the Treasury bought \$45,000,000 of its own securities for the "investment accounts" under its supervision. That's control on a scale stock manipulators don't dream of.

Free riders recognize this factor of Government support of the markets as fundamental. They know that successful financing deals are essential to the Administration and that, therefore, the Treasury will do its best to put the market in attractive shape just before security offerings. And, what is just as important, they know that since the Treasury "insures" the success of its offerings, there will always be hundreds of bona fide investors—banks, insurance companies, trust funds—that will want more securities than they are able to obtain from the Treasury in their own names. These bond-hungry investors create the free rider's market, for they are willing to give him his profit in order to get hold of his bonds.

Not once in the past six years have free riders failed to win. Every Government security sold has jumped above its original issue price immediately after the formal offering. Some of the issues have returned relatively large profits—\$17 and \$20 a bond—and some, tendered during unsettled periods, have allowed only a few dollars per bond. But each issue has been a success, for the Government understands full well the importance of keeping that market alluring.

Of course, it is possible to conceive of things which might spoil the pretty picture. A world war; a wholesale flight of capital from the country; the assassination of the President; a new wave of currency devaluations; an overnight reversal in Government financial policy designed to lift the cost of money-borrowing—developments of this sort might force Government security holders to dump their bonds on the market. And if

the market collapsed, trading might be suspended altogether, and the free rider caught short. But if such things happened, he'd probably be caught in one way or another anyway, and a free-riding loss would be the least of his headaches. To cite such catastrophes as the only probable causes for risk in free riding is no exaggeration. Even during a situation as hot as the March, 1933, crisis, when the nation's banks closed, the Treasury was able to sell an issue of notes that rose to a premium. The same thing was true in the September, 1938, financing, made at the time of the Central European crisis. The free riders could have sold their securities profitably at any moment during those periods.

few months. In 1935, for instance, close to 50 per cent of the outstanding debt was in the form of securities due within five years. In the fall of 1938, nearly 39 per cent of the debt represented obligations maturing before 1944. The Treasury Departments of this and future administrations, therefore, are faced with a serious problem of debt refunding. Borrowing at regular intervals by the country's fiscal authorities to meet the debt coming due and to raise new cash

is virtually assured during the remainder of this decade and most of the next.

Today, thousands of speculators are preparing to free-ride the Treasury's last financing of 1938, slated for mid-December. Another borrowing is anticipated for March, 1939, another for June, September, and a year from now. This short-term debt the Government has created is burdensome, even if not so dangerous as Administration critics insist. And for the free riders, that is a perfect setup.

If a free rider did get caught by a major catastrophe, he would have three alternatives: he could try to cancel his subscription, throwing himself on the mercy of the Federal Reserve Bank officials; he could ask his bank to carry him on a 10 per cent margin; or he could offer his bonds for whatever price they would bring, hoping to get out with only a minor loss.

The Government's attitude toward free riding is clear, but not frightening. It considers it disturbing to the market, harmful to the price level. In December, 1936, after a year in which free riders had run wild, Secretary Morgenthau exploded to reporters: "Free riders are chisellers who are trying to cheat their own government." He cited an instance of a bank which used its entire clerical staff to aid in its free-riding operations, and told of a man who had used the names of twenty-one members of his family to disguise his activities. The Treasury has taken some steps to get rid of free riders. It has raised the deposit requirements for subscriptions from 5 to 10 per cent, but that has not been prohibitive. Banks have been ordered to check on the credit standing of individual buyers, but that is too big a job. It is doubtful that the authorities could ever eliminate a practice so easy to understand and operate without doing the market more harm than good. Indeed, the activities of the free riders give the Government market a stimulation and excitement it could obtain from no other conservative source.

So much for the risks. They would not loom large to anyone who has the courage to ride in an airplane or cross Fifth Avenue at noon.

The future of free riding looks good. Since millions of dollars of the securities sold by the Treasury in recent years have carried short-term maturities, large blocks of the public debt mature every

December 8, 1938.
11:40 p.m.

HMJr: Hello.

Operator: Mr. Sproul.

HMJr: Hello.

S: Hello, Mr. Secretary.

HMJr: The President is very angry at me because I didn't get him any bonds.

S: Who is?

HMJr: The President of the United States. He says he thinks there is something the matter with a setup where you can't buy five thousand for your church.

S: Well, maybe there is.

HMJr: Well, how did she go?

S: Well, we've had -- after the first hour this morning when there was some selling of subscriptions to the long bonds of the whole long market was off, why, the market has gone very well.

HMJr: I see.

S: I'm selling tied up until eleven o'clock and since then the market has been strong all through, but particularly in the long bonds, and the gap which had developed between the rights, the new twos and the new two and three quarters has been pretty well closed up now.

HMJr: Good!

S: In the trading after the close this afternoon at four o'clock, the rights were quoted at one hundred and one twenty-four twenty-six.

HMJr: I see.

S: The new twos at one hundred and one twenty-four twenty-six, and the new two and three quarters at one hundred and one twenty-three twenty-five.

HMJr: Well, that's close enough, isn't it?

S: So they are pretty close together now and it looks as if either one might go ahead tomorrow, and I think it is in as good shape, or better shape, than it has been at any

- 2 -

time, and it has always been in pretty good shape.

HMJr: Well, it sounds very good. Now, has the system made up their mind what they are going to do?

S: No, they haven't. They are going to have a meeting tomorrow morning and decide.

HMJr: Yes, well, alright. I suppose -- I don't know when I make the allotments.

S: Well, I suppose in the ordinary course you would probably make them about Friday night.

HMJr: Oh, my heavens! As far off as that?

S: What?

HMJr: You fellows won't be ready until then?

S: No, to do even a half-way policing job I think we need until Friday night -- until Friday noon, say.

HMJr: Well, we ought to have it definitely by Friday night.

S: Yes, I should say so -- so that it would be out in the hands of the subscribers on Saturday, and they could begin -- they would get back in here on -- we could begin on Monday on the actual operations with the bonds.

HMJr: O.K.

S: Good bye.

HMJr: I am very much pleased.

S: Well, it looks good.

HMJr: Yes.

S: Alright.

TREASURY DEPARTMENT

25

INTER OFFICE COMMUNICATION

DATE DEC 6 1938

TO Secretary Morgenthau
FROM Herman Oliphant

There has been submitted to us for approval a proposed acceptance of an offer made by Homer S. Cummings to sell to the United States, for the sum of \$50,000, a tract of land to be used as an addition to the Stamford, Connecticut, Post Office site.

Without making any investigation of the circumstances in the matter, outside of what appears in the file, the following would seem to be the facts:

Mr. Cummings has owned the property at least since 1929. The H.O.L.C. has appraised the property at \$50,000. The property has an approximate frontage of 132 feet. The property between the present site and Mr. Cummings' property is also being purchased. The price proposed to be paid to Mr. Cummings per front foot is less than that proposed to be paid to the owner of the intervening parcel. The assessed value of Mr. Cummings' property is \$24,200.

The present Post Office site is in the middle of the block and the only other property available for the extension is the property on the other side of the Post Office upon which is located a Y.M.C.A. building, and the purchase of this property would entail a much larger expenditure than the property owned by Mr. Cummings and the adjoining property owner.

There does not seem to be any statutory prohibition against this transaction. Section 41 of the Criminal Code (act of March 4, 1909, 35 Stat. 1088, 1097) (U.S.C. title 18, sec. 93), which is the only statute applicable to sales to the Government by officials extends only to employees who are officers or agents of the seller and not to principals. The Comptroller General, in general language, has indicated that this act applies also to principals. However, such language may be disregarded in view of the express terms of the statute, which is penal, and has to be strictly construed. The Attorney General has held that such statute applies only to agents and not to principals.

Aside from any statutory prohibition, however, there is reason to believe that the Comptroller General, following decisions heretofore made, will hold that the transaction is void on the grounds of public

- 2 -

policy. Before the site can be acquired and the check drawn for the purchase price, the warrant has to be countersigned by the Comptroller. Because of this the matter will be before the Comptroller prior to the closing of the transaction.

The Comptroller has held that the following transactions are void on the grounds of public policy:

1. Contracts by Government employees to rent automobiles to the Government, even though the employee is not the negotiating or contracting officer.
2. Contracts between a Public Health surgeon, who is the contracting officer, and himself, as proprietor of a private hospital, even though the hospital was the only one available in the vicinity.
3. Sales of tractors by an employee of the Virgin Island Government, after public advertisement, even though the employee was not the contracting officer and had nothing to do with the transaction in an official capacity.

A study has been made of the general law of public policy in so far as it is applicable to this type of transaction. Most of the authorities deal with the situation where the Government employee secretly, or otherwise, acts as agent for the contractor and while they do not cover our situation, they do contain general language as to the suspicion with which the law looks upon transactions between employees in their official capacity and acting in their own personal interest.

The nearest case to our situation is found in Mayor and Council of City of Macon v. Huff, 60 Ga. 221. In that case the City Council leased a piece of property to the then Mayor for a certain term of years and the Mayor as part of the consideration for the lease agreed to do certain things such as cutting wood and distributing it to the poor. After the execution of the lease there was a change in personnel in the City Council although the Mayor was reelected. An action was brought by the City against the Mayor to void the lease. The Court held that, even though the Mayor did not have the duty of negotiating and executing leases, he did have the general duty as Mayor of the City to see that agreements on behalf of the City were faithfully executed by the other parties to the agreement and that as part of his general duty he was required to see that the lease was properly performed. Because of this relationship, the Court held the lease void on the grounds of public policy.

In our case Mr. Cummings has nothing to do officially with the negotiation or execution of the contract. He has the duty, however, of certifying to the title under Section 355 of the Revised Statutes, as amended (U.S.C. title 40, sec. 255), and no money can be expended upon any site until the written opinion of the Attorney General shall be had

in favor of the validity of the title. In the closing of title it has been the practice of the Procurement Division that the vendor, after acceptance of the offer, furnish evidence of title to the United States Attorney or Special Attorney designated by the Department of Justice who examines the title and forwards his report to the Attorney General. The Department of Justice then furnishes a preliminary opinion signed by, or for, the Attorney General as to the state of the title. If the title is marketable the Procurement Division forwards the preliminary opinion of the Attorney General, the abstract, and supporting papers, to the General Accounting Office with the request that a check be issued for the purchase price and forwarded to Justice. The Department of Justice, upon receipt of the check, transmits it to the United States Attorney for the closing of the title.

If any suit is brought in the Court of Claims concerning the contract, it will be the duty of the Attorney General to defend the action and to assert any counter-claim available to the Government. This might involve a breach of warranty on the part of the grantor. The Department of Justice generally, under the supervision of the Attorney General, also will represent the United States in any other litigation in connection with the contract.

It is quite possible that a Court, following the decision in the Georgia case, cited above, might hold that the Attorney General had such an official interest in the contract as to render it void.

It is my judgment that the matter should be formally submitted to the Comptroller with a statement of all the facts in the matter, especially because it must be cleared with him prior to closing. The courts have permitted trustees of estates to deal with themselves individually upon a submission of all the facts to the Court for advance approval. It may be that this analogy may be used in submitting the matter to the Comptroller General.



OFFICE OF THE DIRECTOR

TREASURY DEPARTMENT

PROCUREMENT DIVISION

WASHINGTON
December 6, 1938

MEMO. TO MR. MC REYNOLDS:

Subject: Public Hearing Temporary National
Economic Committee

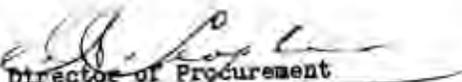
The fifth public hearing of the National Economic Committee was held in the Senate Office Building today at 10:30 A.M. and adjourned at 4:30 P.M.

Mr. Milton Tibbitts, Vice President and Patent Counsel of the Packard Motor Car Company of Detroit, Michigan was on the stand with respect to various phases of the use of patents by that company.

Mr. W. S. Knudsen, President of the General Motors Corporation, and Mr. James McAvoy, Director of the Patent Section of the same corporation were on the stand with respect to various subjects such as competitive use of patents; patents and progress; infringement suits; patent research; cross licensing; royalty fees; exchange of patents; patents in field of newer industries; basic and non-basic practices, and possible effects of revolutionary patents.

Next followed Mr. Charles P. Kettering, Head of the Research Department of the General Motors Corporation who was heard on various phases such as rewards for inventions; collective research; invention psychology; compensation patents; types of patents; patent licensing; technological problem; the patent system, etc.

Next followed Mr. James McAvoy, Patent Counsel of the same corporation on the general subjects of General Motor royalties; patent applications; and the patent office.


Director of Procurement

CONFIDENTIAL

C A B L E

From: Bankers Trust Co. of N. Y.
London Office

Date: December 6, 1938
Tuesday

#418. BRITISH CONTROL MADE FIRM STAND AS BUYERS OF DOLLARS AT 4.70. THIS FACTOR COUPLED WITH NEWS SMALL ANTI FRENCH DEMONSTRATION IN ITALY TURNED MARKET WANTED 'TILL RATE OF 4.69 REACHED AT WHICH RATE CONTROL WAS SELLING DOLLARS. FORWARDS AFTER OPENING OFFERED TURNED SLIGHTLY WANTED. REPATRIATION FRENCH FUNDS SMALLER AND FRENCH CONTROL OPERATING BOTH WAYS. FORWARDS STEADY.

DeCASTELLANE REPORTS CONTROL CONTINUED RECEIVE EXCHANGE THIS MORNING ESTIMATED 1,000,000 POUNDS. FOREIGN BANK NOTES ALSO BEING SOLD BUT LITTLE EVIDENCE SALE FOREIGN SECURITIES BY INDIVIDUALS. BOURSE STRONG INCLUDING GOVERNMENT BONDS. RATE TREASURY BILLS AGAIN LOWERED TALK FURTHER REDUCTION BANK RATE SOON. CALL MONEY EASY THOUGH MARKET LARGELY ARTIFICIAL. BANK DE L'INDO CHINE BELIEVES STERLING RATE WILL GO TO 175 BUT DeCASTELLANE DOES NOT AGREE THOUGH GENERALLY BELIEVED FRANC UNDERVALUED IN TERMS OF STERLING. NOW ANTICIPATED DALADIER WILL HAVE 60 VOTES MAJORITY POSSIBILITY MINISTERIAL RESHUFFLE AFTER VOTE.

December 6, 1938.

MEMORANDUM

At 12:40 this noon I again spoke with M. Cariguel of the Bank of France by long distance telephone in order that Secretary Morgenthau might have the latest information from Paris before lunching with the President. Cariguel told me that so far during the day he had acquired well over three million pounds. At around one-thirty P.M. he had been obliged to sell back a little sterling to the market, there having been a slight reaction, presumably due to the anti-French demonstrations in Rome. This movement had lasted only a little while; during the remainder of the afternoon the French Stabilization Fund had again acquired foreign exchange. Cariguel reminded me that the rate on French Treasury bills had again been lowered, this time to 1 and 3/4 per cent. He said French rentes and shares were strong, but that Paris was selling international securities, particularly gold mining shares. He said there was entire confidence that Daladier would obtain a majority in the session of Parliament which begins December 8. The spirit on the Paris market was quite good.

In answer to my inquiry as to whether the naming of Janssen as the new Minister of Finance in Belgium had caused any repercussions, Cariguel said he was not aware of any marked comment on this appointment. The belga had been weak the past few days, with Brussels losing gold to London, a little to Paris, and presumably some to the United States, but Cariguel could not in any manner confirm the present report which I mentioned as emanating from London to the effect that Belgium might cut the belga loose from gold and follow sterling.

H. M. C.
H. M. C.

December 6, 1938

Lunch with the President.

I told the President I was having Dr. Bowman do some work on exploring South Africa as a possible colony. He said that it was a waste of time to explore any country other than a British colony; that that territory was controlled from London and any country belonging to the Union of South Africa was out of the picture.

He then sketched his plan to me, which is as follows:

He first asked me how many people did I think there were to be taken care of. I said, I am not an expert, but, I said, Germany, 500,000; Roumania and Poland another 250,000. He said, Well, that just checks with the information he has. He said he had figured that it would take \$1,000 a person and I said I agreed with that, or \$500,000,000. He kept saying, always, "Do you think?" "Did I think if we could find a way to take care of 100,000 people for five years that that would be sufficient?" Would that answer the problem?

Well, I said, it is so much better than anybody has suggested that, I said, yes. He said, Well, what I am willing to propose is that, first, that of the \$500,000,000, \$300,000,000 be outright grants; the other \$200,000,000 to be subscribed to through selling of bonds as two-thirds ought to be recoverable. He said that he was ready to recommend that the United States Government contribute \$20,000,000 a year for five years, provided that all the other countries of the world would subscribe \$20,000,000 and that the \$20,000,000 was raised through private contribution. I told him \$60,000,000 and that \$40,000,000 should be raised through the sale of bonds.

He then outlined to me (and I thought he was going to give me the memorandum, but he didn't) where he thought people could be placed. He said he is willing to recommend that the United States take 20,000 Jews a year. I said, Well, that isn't the quota? He said, No, but the quota isn't exclusively

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for Jews. (Which, of course, is right.) He then put down Palestine for 15,000. He said, What do you think of that? I said, I thought that was low. And then he mentioned certain of the British colonies in South Africa and what he said was extra, extra secret: he hopes to get a few into the back country of Ethiopia, which he said is very good country. Altogether he had worked out that outside of the United States there would be room for 80,000 a year.

So I said, Well, what are you going to do with the plan? He said, That's what the meeting is for that follows you. There was Sumner Welles, Bullitt, Bill Phillips and Ambassador Wilson.

The President seemed very determined to do this and seemed to think, moreover, that it was possible.

I told him about my plan: that in my letter to Jones, from now on that the management of any bank to which we subscribe for preferred stock must be approved not only by Jones, but FDIC plus the Comptroller of the Currency and told him that for all the good banking reasons, the extra reason was I thought it was a mistake to let Jones have the exclusive right of going to the heads of these important banks during the next two years. He agreed.

The President said, Write that letter to Jones. He said, He will go up through the ceiling and then, he said, he will come and see me and I will say we won't do it the way Henry suggested, but you write me a letter, Jesse, but before you talk to the head of any bank at all it will first have to be O. K'd by the President of the United States and the Secretary of the Treasury and the Comptroller and the head of F. D. I. C., and, he said, if you write me such a letter than I will get Henry to withdraw his. But, said the President, I would much prefer to do it the way I suggest. I said, O. K.

I then had a minute to talk to him about Basil Harris, but only a minute, and he said yes; we needed a man like that. He said, "A man who would be good enough to sell bed warming pans to the Indians." (That's a hot country, you know.)

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He had a long telephone conversation while I was there with Jimmie Roosevelt and I asked three times whether I should not go out, but he didn't want me to. Needless to say, I was terribly embarrassed because it had to do with the position which he has just taken. (See note at end of dictation.)

I showed him the story of the low rental house at Fort Wayne left me by Stewart MacDonald and he was tremendously interested in it.

The President said, How is Hanes getting along with these taxes? I said, There is nothing to get along on because we are all waiting on you. So I said, Mr. President, your new Fiscal and Monetary Advisory Committee have worked out something which looks very important. I am having this group of economists come down Friday or Saturday to go over it to make sure it is sound. I named the economists. (Magill, Hansen, Williams and Walter Stewart.)

The President said, "Can't you let me have it before then?" I said, No, Mr. President, it's too important and I want to make sure it's all right. "When can I have it?" Monday afternoon. He said, Well, be thinking over how we should handle it publicly. He said, Can you guarantee that there will be no leaks on it? I said, Yes, I can. He said, Well, I will begin to see Jack Garner and the other leaders by the 17th of December and once I talk to them of course there will be leaks. He said, Think it over whether I should spring it before then or whether I should say nothing to them and keep it for my message. He said, From what you tell me, this sounds so important I may not put it in my budget message, but put it in my message to Congress and make it the principal thing. I said, Well, Mr. President, there is nothing that has come into my office that looks potentially as important as this. He asked me two or three times, Do you think you can guarantee secrecy? I said, Yes. (I hope I am right.)

I gave the President the report on Japanese discrimination against American commerce, which was prepared jointly by Harry White and the General

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Counsel's Office. The President said it was very interesting and that he will use it if necessary. The President said, "What will Hornbeck do if I use this?" and my answer was, "He will probably blow up and explode."

(I overheard the President say that Jimmie's new duties are to dig up historical scenarios and to keep his ears close to the ground to find out why certain stars are unpopular. He also overheard him say to his son, "How can you do this thing with a suit pending? What is the difference between a civil and a criminal suit? All I know is that you are working for a man who is fighting the United States Government.")

10:30 A.M.

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TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

TO Secretary Morgenthau

DATE: December 6, 1938

FROM M. A. Harris

Mr. Kilby tells me that there will be no report on cash subscriptions before this afternoon but would be glad to get a special report if you so desire.

The Federal Reserve Bank of New York has received so far in the over-night mail subscriptions amounting to \$514 million for the 2-3/4% bonds and \$300 million for the 1-1/8% notes. These figures are in addition to those given you by Mr. Kilby late yesterday.

Wall Street Comment

Reporting Banks

The contrasazonal increase of \$18,000,000 in the reporting New York bank loans to commerce, industry and agriculture in the week ended last Wednesday was not large enough to offset the \$19,000,000 reduction in the other reporting cities, with the result that total commercial loans for the 101 cities declined \$1,000,000. In other times than these, when term loans are beginning to get a good play with the banks, the advance that formed the bulk of the increase in commercial loans here would probably have shown up under the heading of investments. Holdings of direct government securities of the reporting banks in 101 cities decreased \$23,000,000, but the smallness of the rise in loans to brokers and dealers in securities left it doubtful whether dealers in government were stocking up heavily in the March notes in preparation for the quarter financing date. It is possible that loans to brokers and dealers' loans will be up this week, for the 2 per cent bond which the Treasury is offering, obtainable only through exchange of the March notes, has a special appeal to the banks, and dealers will be anxious to get the largest possible allotments. Demand deposits adjusted of the weekly reporting banks increased \$97,000,000, and so crossed the \$16,000,000,000 level for the first time on record.

Treasury Finance

Skilfully combining the investment and speculative features afforded by Federal issues of securities, Secretary Morgenthau yesterday was able to chalk up another outstanding success in deficit financing and refunding. With excess reserves at record levels, it was no great trick to float the new issues. The requirement was only that the terms be so adjusted as to attract bank insurance company and other institutional applications in volume. Mr. Morgenthau attended to this with his usual aplomb, and the market did the rest. With a premium of 1 1/2 to 1 3/4 points indicated on the new 2 1/2 per cent bonds, that portion of the flotation was in extraordinary demand. The new 1 1/2 per cent notes afford a premium of only one point, which means that applications will be more limited. The new 3 per cent bonds, available along with either of the other new issues to holders of March notes, were quoted on a when-issued basis at even figures with the outstanding notes, or from 101 25-32 early in the day to 101 20-32 at the close.

Free Riding

Extensive precautions were taken yesterday by the Treasury and the Federal Reserve banks against free riding on the new Treasury issues, but this feature nevertheless seems to become ever more prominent from quarter-date to quarter-date. Applications from financial firms were scrutinized carefully and pruned vigorously in many instances. The request was made that when-issued trading be avoided on the new notes and long bonds, but such trading was permitted on the new 2 per cent bonds, since the March notes afford the only access to that issue. Larger dealers were asked not to trade in allotments, and this request was observed where made. Some of the smaller outfits enjoyed good business in allotments, however, and the incident caused much discontent among larger houses. New York interests were mollified, on the other hand, by wire indications that the restrictions on the local market this time were applied with equal rigidity in all other districts.

French Gold

The foreign exchange market prides itself on its power of sensing disturbing events a long way off. One recent example of its prophetic claims is to be found in the fact that the foreign exchanges, prior to the September crisis in Europe, were showing anxiety over the course of events on the Continent for a long while before the securities markets became disturbed. The behavior of the foreign exchanges in this present unpleasantness between Italy and France is, therefore, all the more interesting. Sterling and French francs have been strong throughout the demonstrations in Italy for bringing Tunisia, Corsica, Savoy and Nice under Italian domination. The French fund has actually gained a fairly substantial amount of gold in the last week. It will take a few weeks of strong francs, however, before it can be said definitely that the foreign exchange market regards Italy's colonial ambitions as containing no imminent threat of military action.

Steel Production

The slight drop in the steelmaking rate for the third successive week merely confirms the opinion held by informed observers for some time—that if current prices were affirmed for the first quarter of 1939 there would be no inducement for consumers to buy in advance, resulting in a leveling-off of production schedules through the in-

ventory-taking period. In certain steel quarters there is a bit of apprehension that, because of assurance of low prices for products in January, February and March, consumer commitments may be so large during that period as to "borrow" from activity in succeeding months when, it is hoped, more profitable levels may be established. The general view, however, is that profits are secondary to putting any obstacles in the way of the still struggling industrial recovery.

International Nickel

One important consideration to stockholders of International Nickel Co. is the possibility that the company will remove its stock from listing on the New York Stock Exchange if the Securities and Exchange Commission demands that it disclose salaries and sales figures just as domestic corporations are required to do. However, despite this quite obvious fact, the company announced yesterday after a meeting of the board of directors that "the matter of the company's position under the United States securities exchange act was not dealt with at the meeting of the board today." Perhaps some purist dictated the statement who interpreted "dealt" to mean "disposed of" because there is no doubt that the major subject of discussion was what action to take with regard to the company's registration with the S. E. C.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE DEC 6 1948

TO Secretary Morgenthau
FROM Herman Oliphant

For your information

Mr. Foley held a conference this afternoon in his office to discuss the Chinese tung oil proposal with representatives of the State Department.

The conference was attended by Messrs. White, Foley, Johnson and Tietjens for the Treasury and by Messrs. Raymond C. Mackay and Frank X. Ward for the State Department.

The background of the proposal and some of its details were outlined for the benefit of the State Department representatives. No objections were developed at this conference which we had not considered when the objections of these officials of the State Department were first called to our attention. They ^{are not} were well taken. Nevertheless, Mr. Ward was of the opinion that the proposal could reasonably be objected to, under Article IV of the Treaty of 1844 between China and the United States, by powers entitled to most favored nation treatment by China, inasmuch as, in the absence of contrary evidence, it appears that the proposal would result in an exclusive agency being established by the Chinese Government which would have a virtual monopoly of the tung oil exports from China.

Methods of obviating this objection were discussed. It was suggested that the difficulty might be overcome if the contract to be entered into between the Chinese Government and the trading corporation

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would provide for the purchase of, say, 70 per cent of the tung oil produced in China rather than for the preferential sale of a stipulated amount of oil which might result in a corner on the available supply. It was also suggested that none of the powers who might object to the arrangement would be in a position to object if the Chinese first offer to sell tung oil to such powers upon the same terms as are being offered to the United States.

At the conclusion of the conference, Messrs. Mackay and Ward stated that they were not yet in a position to make any definite suggestions, but that the information they now had would afford a basis for further discussion of the proposal in the State Department.



PARAPHRASE OF TELEGRAM SENT

TO: American Legation, Bern, Switzerland
DATE: December 6, 1938, 1 p.m.
NO.: 62

STRICTLY CONFIDENTIAL.

Reference is made to No. 41 of August 30, 6 p.m., from the Department.

You are requested to see Mr. Royal Tyler, and say that Secretary Morgenthau would appreciate it if he would in the near future undertake a trip around Italy similar to the one he made around Germany early in September. On his return the Secretary of the Treasury requests that he submit a cipher telegram through the Bern Legation outlining his appraisal of economic and financial conditions in Italy. Mr. Tyler would receive from the Treasury compensation on the same basis as previously. Authorization is of course given to Mr. Tyler to inform Loveday in strict confidence of the purpose of his visit.

WELLES

Acting.

Note: See reply filed under date of 1/24/39



DEPARTMENT OF STATE
WASHINGTON

January 25, 1939.

My dear Mr. Secretary:

I enclose herewith one copy of paraphrase of a telegram sent at your request on December 6 to the American Legation at Bern asking Mr. Royal Tyler to take a trip around Italy, and a copy of paraphrase of telegram of January 24 from Bern transmitting Mr. Tyler's report.

Sincerely yours,

Herbert Feis

Herbert Feis,
Adviser on International
Economic Affairs.

Enclosures:

No. 62 of December 6
to Bern.

No. 7 of January 24
from Bern.

The Honorable

Henry Morgenthau, Jr.,

Secretary of the Treasury.

CORRECTION

JR

December 6, 1938

In telegram #1395, December 5, 6 p.m., from London "For Treasury", last figure in first line should read "4.68-1/8". Delete "(*)" there and also at end of message.

DIVISION OF COMMUNICATIONS AND RECORDS

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: December 6, 1938, 5 p.m.

NO.: 2060

FOR THE TREASURY.

Today the exchange and security markets were encouraged by good reports from most part of France on the labor situation, as well as by the conciliatory tone of the resolution which the general Confederation of Labor adopted yesterday to the effect that the Confederation was prepared to take part in any discussion which was likely to put an end to present difficulties.

Financial circles on the other hand are awaiting with interest but with no apparent misgiving the outcome of decisions which will probably be reached tomorrow on the question of what part of the agenda is to be taken up first when the Chamber meets on December 8. Parties of the Extreme Left insist that the 1939 budget be taken up first; they apparently hope that in this way they can place the Government in a difficult position on the decree laws, which would necessarily be linked with any discussion of the 1939 budget. If the electoral reform law is taken up first, and is voted before the decree laws are discussed, deputies who may otherwise be willing to risk unpopularity with their electors might be willing to give the Government their support regarding these laws.

The demand for the franc continued on an important scale in a quiet market, although it is our understanding

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that a slight nervousness was apparent on the market regarding the possible effect of the Italian incident on the international political situation.

It was again possible for the fund to obtain a large amount of sterling; at the opening it offered francs at 177.56 and gradually reduced the peg to .40, which is the rate at present. No premium was asked for one month sterling today. 45 centimes is the rate for three month sterling. Today the dollar was a little stronger than it was yesterday. There was pressure on the belga again today due, it seems, to an opinion that sooner or later the Belgian authorities will be obliged to link the belga with sterling.

On the security market there was a firm undertone and an improvement in rentes and French variable revenue securities.

There has been another reduction in the rate of interest on 75 to 105 day ordinary treasury bonds, the present rate being 1.75 percent (in yesterday's telegram I reported a rate of 3 percent).

END MESSAGE.

WILSON.

EA:LWW

PARTIAL PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, London, England

DATE: December 6, 1938, 6 p.m.

NO.: 1400

FOR TREASURY.

AA

One. Dollars opened offered at 4.70 the British fund buying dollars heavily until fixing when such rate was 4.69 7/8. 175 bars were sold at 148 shillings 1 penny giving a two pence premium. The British fund bought 75 of the bars sold and when this became known the rate went to 4.69 and later 4.68 3/4 with the British authorities selling some dollars at those levels. This afternoon the dollar has remained offered around 4.69 1/4, on a narrow market.

It is the belief of an exchange market source that after the fixing further small amounts of gold were bought by the British fund.

The one month forward dollar was steady around 13/16 premium and the three months which opened at 1 7/8 later went to 2-3/16.

The Bank of France bought sterling heavily starting at 177.82 and moving to .56 at fixing time. Later the French authorities sold some sterling but the franc was again bid and the Bank of France has continued sterling purchases closing at 177.42. The one month forward franc went to a premium of 1/32 franc but the three months

remains

- 2 -

remains around 3-1/4 discount.

Two. Sales by French holders of gilt edged and Kaffir stocks further depressed prices, war loan 3-1/2 per cent being down 1/4 to 98-7/16.

Three. The Chancellor of the Exchequer announced in Parliament today a temporary increase in the fiduciary note issue of 30,000,000 pounds to 230,000,000 pounds.

END MESSAGE.

KENNEDY.

EA:LWW

FEDERAL RESERVE BANK
OF NEW YORK

16

OFFICE CORRESPONDENCE

DATE: December 7, 1938.

CONFIDENTIAL FILES

SUBJECT: TELEPHONE CONVERSATION WITH

L. W. Knoke

BANK OF ENGLAND.

I called Mr. Bolton at 11:15 a.m. They were having a rather uncomfortable time, he said, sterling being under some pressure in two ways: (1) the continued repatriation of French money from the London market, and (2) a renewed French bullishness on the dollar and resulting transfers from London to New York. Generally speaking repatriation of capital to France continued and there was noticeable a considerable increase in confidence on the part of Paris. Daladier would most probably have a considerable favorable vote tomorrow when the Chamber meets. At the moment there was a mild reaction from this morning's firmness of the franc so that Cariguel just now had to support the franc but on balance he had gained about £2,000,000 for the day. The bulk of the London exchange operations, Bolton continued, came from Paris rather than anywhere else.

With reference to the gold coins and gold chips recently shipped to us, of which he had advised me a few days ago, Bolton requested that we melt them down on arrival and set the gold aside for him. He would let us know in due course in which account.

I asked a number of questions:

(1) The premium on forward gold?

This, Bolton said, was unchanged, that is, about 1 5/4d per month.

(2) What was the arrangement under which gold purchased in London could now be earmarked in South Africa?

There was no particular arrangement, he

FEDERAL RESERVE BANK
OF NEW YORK

OFFICE CORRESPONDENCE

DATE December 7, 1938.

RE CONFIDENTIAL FILES

SUBJECT: TELEPHONE CONVERSATION WITH

FROM L. W. Knoke

BANK OF ENGLAND.

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replied. South Africa would take gold in London and give the same amount in South Africa at a flat price but make a charge of 1 per mil for earmarking. No adjustment would be made in the price, that is, no allowance for the cost of shipping the gold between South Africa and London.

(3) Was it correct, as stated to me here in the market this morning, that the dollar bull position in London was by now mostly liquidated?

"Not anywhere near right," Bolton replied.

LWK:KW

REB

GRAY

London

Dated December 7, 1938

Rec'd 2:35 p. m.

Secretary of State,
Washington.

1406, December 7, 6 p. m.

FOR TREASURY.

The dollar opened at 4.68-13/16 offered and the British authorities sold dollars holding this position until the fixing when 264 bars were sold, 60 being supplied by the British fund. The price at 148 shillings 5 pence gave a premium of 2 pence. Since the fixing the dollar has remained around 4.68-5/8 on a narrow market with the British authorities apparently not operating.

The Bank of France bought a large amount of sterling this morning at 177.41 and .37 but this afternoon the franc was offered and the Bank of France sold a small amount of sterling at 177.42 the rate going in the late afternoon to 177.50.

The belga was heavily bid until the late afternoon with the three months forward discount moving from 35 to 13 but on rumors of the possible resignation of the Belgian cabinet the forward discount rose to 20 and the spot rate also moved from 27.77 to 27.85.

KENNEDY

DDM
RGC

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: December 7, 1938, 4 p.m.

NO.: 2069

FOR THE TREASURY.

This morning the upward franc movement continued with further important capital repatriation. However, this afternoon the tendency changed due it seems to short covering, to some hesitation and caution just before the day Parliament reassembles, and to continued nervousness regarding the claims against France on the part of Italy.

This morning at opening the fund entered the market offering francs at 177.41. It gradually permitted the rate to drop to 177.35, when the buying movement ceased.

Our market contact tells us that after obtaining about two million pounds the fund, in order to maintain around .42, had to turn buyer of francs and our contact estimated that the fund had probably paid out so far about one-half of the sterling which was acquired today. The spot rate for sterling strengthened, but the forward rate is about the same as it was yesterday.

In today's trading the belga showed slight improvement.

END SECTION ONE.

WILSON.

SECTION TWO.
PARAPHRASE OF TELEGRAM NO. 2069, DECEMBER 7, 1938, FROM PARIS

At opening the security market showed a good undertone. However, moderate gains in early trading have been practically wiped out since then.

The rate of interest on six months ordinary treasury bonds has been reduced to 2.50 percent; it was 2.75 formerly.

For the first ten months of 1938 the monthly adverse trade balance averaged 1,360,000,000 francs. For November the deficit is 812,000,000 francs, as compared with 1,552,000,000 for November of 1937. An increase in exports is responsible for the most part for the improvement.

A report in AGENCE ECONOMIQUE declares that in official quarters yesterday it was stated that Von Ribbentrop and Bonnet discussed at some length yesterday afternoon the subject of trade development between France and Germany. It was said that the German Foreign Minister had let it be understood that Germany would be glad to "soften" its autarchic system to some extent and that under appropriate conditions, and notably in the Balkans and Eastern Europe, the Reich would be prepared to collaborate with France.

END MESSAGE.

WILSON.

EA:LWW

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Berlin, Germany

DATE: December 7, 1938, 11 a.m.

NO.: 699

No. 36. FOR TREASURY FROM HEATH.

Yesterday I learned that Schacht had gone to London to talk with Montagu Norman; this is being kept secret here in Berlin, and I could not get any explanation of its purpose. Schacht said a few days ago that he hoped he would have an early opportunity to talk with Norman, since he had not seen him for several months.

GILBERT.

EA:LWW

REB

GRAY

London

Dated December 8, 1938

Rec'd 2:35 p. m.

Secretary of State,
Washington.

1413, December 8, 6 p. m.

FOR TREASURY.

The dollar opened bid at 4.77-3/8 and after touching 66-7/8 was 67-1/8 at the fixing when 178 bars were sold, 93 being married and 85 supplied by the British fund. The price was 148 shillings 11 pence and the premium 1-1/2 penny, so that all purchases were for hoarding. The British fund sold small amounts of dollars from time to time but the market was relatively quiet.

The Bank of France operated both ways, gaining on balance a fair amount of sterling.

KENNEDY

CSB

TREASURY DEPARTMENT

C3

INTER OFFICE COMMUNICATION

DATE DEC 7 - 1938

TO Secretary Morgenthau
FROM Mr. Oliphant

As you know, the newly-mined domestic silver Proclamation of December 21, 1933, as modified, is due to expire on December 31, 1938. Unless such proclamation is extended, beginning January 1, 1939 only silver mined prior thereto will be acquired by the Treasury under such proclamation.

The principal authority relied upon for such proclamation, as modified, is to be found in the provision authorizing the unlimited coinage of silver, contained in a paragraph of the "Thomas Amendment" of May 12, 1933, as amended, which paragraph also contains provisions giving the President power to fix the gold content of the dollar. These powers expire on June 30, 1939. Accordingly, if the proclamation is to be extended under this statute, the terminal date should be fixed not later than June 30, 1939. Moreover, it would appear that any such extension should make June 30, 1939 the final date for any deliveries under such proclamation, even if the silver be mined prior to that date.

Section 3 of the Silver Purchase Act of 1934 provides as follows:

"Sec. 3. Whenever and so long as the proportion of silver in the stocks of gold and silver of the United States is less than one-fourth of the monetary value of such stocks, the Secretary of the Treasury is authorized and directed to purchase silver, at home or abroad, for present or future delivery with any direct obligations, coin, or currency of the United States, authorized by law, or with any funds in the Treasury not otherwise appropriated, at such rates, at such times, and upon such terms and conditions as he may deem reasonable and most advantageous to the public interest: Provided, That no purchase of silver shall be made hereunder at a price in excess of the monetary value thereof: And provided further, That no purchases of silver situated in the continental United States on May 1, 1934, shall be made hereunder at a price in excess of 50 cents a fine ounce."

The Secretary of the Treasury would have the legal authority under this section of the Silver Purchase Act to acquire newly-mined domestic silver at a price in excess of the market price for foreign silver if he deemed the same reasonable and most advantageous to the public interest.

Herman Oliphant

December 7, 1938

This morning the Secretary called Miss Le Hand and told her that he had broken his toe and asked her whether the President had an extra cane which he might borrow for a couple of weeks.

At twelve o'clock the President called HM, Jr and the following is a record of their conversation:

The President: What are you kicking about?

HM, Jr: I am kicking the furniture about.

The President: Did you really lose your temper? Whom did you miss?

HM, Jr: I was just walking bare-footed across the room and ran into a piece of furniture.

The President: Is it your big toe?

HM, Jr: No, it's my little toe. I borrowed one of your big canes.

The President: Yes, I know you did. I picked it out myself for you and made sure it would be a comfortable one.

HM, Jr: Oh, thank you very much!

The President: How long before you will be all right?

HM, Jr: Oh, it will take three weeks.

The President: Well, can't you have a special shoe made or one with the toe cut out?

HM, Jr: Well, I am wearing a moccasin now.

The President: You can't come to the Diplomatic dinner and reception in a moccasin!

HM, Jr: Well, I promise to have it all healed by the time the King arrives.

The President: Mac says you had better have

-2-

it amputated. It will only take a week to heal.

HM, Jr: Oh, tell him to go to hell! Oh, is it Admiral McIntire or Colonel MacIntyre?

The President: It's Colonel MacIntyre. If it were the Admiral he would probably come over and amputate it himself!

HM, Jr: Oh! Thank you very much for calling me.

The President: I just cleaned up Danny Bell.

HM, Jr: Is there anything left of him?

I will be ready for you Monday afternoon with all the charts in the world. (The Ruml plan.)

The President: The Army budget without extras for the new National defense is only \$5,000,000 more than last year. We cut them \$25,000,000.

oOo-oOo

(The Secretary's comment to HSK: You know, I am just a baby about it. Part of the reason I sent for the cane was because I wanted the President to know that I had broken my toe.)

December 7, 1938

Mr. Oliphant told the Secretary today that this is what he gave Alsop in an interview yesterday.

December 7, 1938

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MORGENTHAU THE INNOVATOR

Tripartite Arrangement with England, France, Belgium, Switzerland, and The Netherlands.

Stabilization Fund.

Foreign Monetary Agreements: Mexico and Canada - silver.
China and Brazil (involving gold also).
Mexico and China - Foreign Exchange.

Devaluation of the Dollar and Maintenance of its Stability.

Coordination of Treasury Law Enforcement Activities.

Service Schools for Enforcement Agents, Including Arms Practice.

Efficiency Studies of Various Bureaus by Treasury Administrative Staff.

Coordination of Public Relations Policies.

Division of Laboratories for Entire Treasury.

Special Physical Laboratory for Currency Studies.

Furnishing of Psychiatric Diagnostic Services to Federal Courts.

Entrance of Vessels by Radio if no Disease is Aboard.

Internal Revenue Decentralization Plan.

Procurement Made General Purchasing Center for Government.

Creation of Architectural Advisory Committee, Coordination and Control of Building Design.

Treasury Art Project.

Identical Bids, Monopolies (tires, cement, etc.).

Reorganization of Research and Statistics.

Establishment of General Counsel's Office and Abolition of Solicitor.
New Section in Revenue - Reorganization, Receivership and Bankruptcy.

Richmond Self-Help Plan.

Statement on Prices.

United States Savings (Baby) Bonds.

December 7, 1938

Sumner Welles called at 11 o'clock. He raised the question was there any legal doubt as to the tung oil being in conflict with the nine-power pact of 1922. I told him there was none.

He said that he is ready to go ahead with it for one reason. Notwithstanding the fact that Mr. Hull has cabled that he is opposed to it, inasmuch as the President has given his word to General Chiang Kai-Shek, the consequence of the President's breaking his word is far much more important than anything else, so that he, Welles, is for it.

And the second thing he told me was that tomorrow, at Brussels, an inter-Governmental committee on refugees is meeting secretly with the Germans. He said he understood that the President approved the memorandum on German counter-vailing duties. I told him the first I knew about it was last night I learned, from a memorandum which Oliphant sent me, that the Department of Justice had this and were asking for additional information. Welles said, "For Heaven's sake, don't do anything before tomorrow because it would just kill this meeting." I promised I would not do anything until I talked it over with him again.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE December 7, 1938

TO Secretary Morgenthau
FROM Mr. Haas *HA*
Subject: Estimate of national income for 1939.

National income payments for the current year 1938 are expected by the Department of Commerce to total about 64 to 65 billion dollars. In estimating what they may be in 1939, it is necessary to assume certain levels of business activity and commodity prices. Business expectations for 1939 currently held by the Federal Reserve Board's research staff center around an average FRB index of 106 in that year, which seems to us a reasonable figure for use in estimating national income. The commodity price trend in 1939 will be so much affected by political developments abroad that prediction is very difficult. The trend of the BLS index of commodity prices continues gradually downward, and has as yet shown no signs of beginning an upturn. Currently the BLS index is around 77.3. A rise to an average of 80 in 1939, while not a forecast, may be taken as a basis for estimating national income.

Assuming an FRB index of 106 and a BLS price index of 80 in 1939, we expect the national income to show no substantial increase over this year's figure, probably not exceeding the current estimate of 64 to 65 billions by more than one billion dollars.

An important reason for expecting a relatively small change lies in the fact that national income payments do not respond immediately to changes in industrial production, but the various components of the national income lag to a greater, or less extent behind production. Employment and dividends, for example, may not respond for a number of months after business has turned upward. Owing to these and other lags, the national income in 1938 was held relatively high by the high level of business in 1937. Similarly, the national income in 1939 will be affected to an important degree by the low level of business in 1938.

Secretary Morgenthau - 2

The downward trend of commodity prices is a second important reason for being conservative in our estimate of national income for 1939. Commodity prices have not responded in a normal way to improved industrial demand, owing to unfavorable conditions abroad. This will strongly affect agricultural incomes, and will also be reflected in corporation dividends and in other components of the national income.

In 1937, the estimated national income of 69 billions was associated with an average FRB index of 110 in that year and 105 in the previous year, and with a BLS price index averaging 86.3. The national income in 1939 will be associated with an index of 106 (assumed) in that year and 86 in the previous year, and with an assumed BLS price index of 80. It seems apparent from such a comparison that the national income in 1939 cannot be expected to approximate that of 1937.

It should be kept in mind that the published figures on national income are no more than estimates, subject to frequent revision, and that they are based in part on estimates rather than factual data.

December 7, 1938.
2:40 p.m.

Operator: Go ahead.

HMJr: Hello,

Mariner
Eccles: Oh, hello.

HMJr: Mariner?

E: Yes, Henry.

HMJr: I don't know what -- if you've got something, when you're through I want to give you some information.

E: Oh, well, what it was -- was, I was going to call you at about twelve o'clock -- a little after twelve, and you were out, and then I went out. Maybe - I just wanted to tell you the way we were going to convert.

HMJr: Well, nobody has told me.

E: Well, now we decided thirty million of the notes; thirty-five million of the nine year two percent bonds -

HMJr: Thirty-five million of the nine.

E: Of the two percent.

HMJr: Yes.

E: And eighteen million of the two and three-quarters.

HMJr: I see.

E: It was a sort of a compromise.

HMJr: Uh-huh.

E: Some of them didn't think they should take any bonds -- That is, the long bonds.

HMJr: Yes.

E: And some thought they ought to take more -- I mean, you know, there was just a discussion -- and so this was sort of a --

HMJr: Compromise.

E: Yes. The question was pretty largely whether we should

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take forty of the notes instead of thirty; or whether we should take twenty or forty of the middle bonds; or whether we should take none of the long bonds; or whether we should go up to thirty of the long bonds.

HMJr: I see.

E: So it is thirty thirty-five and eighteen. It really doesn't make very much difference, I don't think, but it does put us in a position here to either increase the long if necessary or to have possibly some to sell.

HMJr: Right. Well thank you for telling me. Now this is what I would like to inform you -- the President is going to see this Fiscal and Monetary Committee most likely at two o'clock on Monday.

E: On Monday?

HMJr: Yes.

E: Uh-huh.

HMJr: And on this thing that they brought in that I call the Ruml plan -- Ruml doesn't like it, but I thought for lack of a better name we'd call it the Ruml plan.

E: Yes.

HMJr: I thought it would be good to have a dress rehearsal Monday morning.

E: Well, I think it is absolutely essential to have one.

HMJr: So shall we say 10:30 Monday morning?

E: That would suit me fine.

HMJr: Right.

E: Is it certain that it is at two -- that's tentative now, isn't it?

HMJr: Well, the President told me, but he would see us for two hours.

E: Well, Monday morning would suit me at 10 o'clock.

HMJr: 10:30.

E: 10:30.

- 3 -

HMJr: And with the President at two.

E: Yes.

HMJr: I've asked for two hours.

E: Yes.

HMJr: Maybe I will get an hour.

E: Well, I tell you, an hour isn't enough.

HMJr: I've asked for two and told him it wasn't any use to have less.

E: It wouldn't do him any good to go into this thing at all unless he is going to give enough time to understand it.

HMJr: No, I've asked him for two hours.

E: Is Ruml -- can Ruml come down?

HMJr: Well, I'm going to get word to him.

E: Um-hm.

HMJr: I'm going to get word to him

E: Well, that's fine -- I'll, I'll try to get -- I'm glad you notified me this far in advance. It will give me a little time to do some thinking.

HMJr: Well, I let you know just as soon as -- well, I knew yesterday afternoon.

E: Yes, well that's fine. Thanks.

HMJr: Thank you.

E: Alright, good bye.

TREASURY DEPARTMENT

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INTER OFFICE COMMUNICATION

DATE

December 7, 1938

TO Secretary Morgenthau
FROM Herman Oliphant

For your information

Bullitt came to my office at 4:30 today. I stated briefly the scholastic record of William Welles Robbins and said that it was far below the standard ordinarily applied in choosing men for the Treasury Legal Staff. He said that entirely satisfied him, and I did not need to say any more.

TREASURY DEPARTMENT

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INTER OFFICE COMMUNICATION

DATE

December 7, 1938

TO Secretary Morgenthau
FROM Herman Oliphant

For your information

Bob Kintner called me at 4:35 today and it turned out that Alsop was also on the line. He said that Hanes had told him that I had said to Hanes that someone had told me that Hanes had given the story to Bob Kintner about his handling taxes to the exclusion of myself. Bob said he just wanted to say that he had not got the story from him (Hanes), but that Alsop got it from me when I told Alsop that he wanted to see Hanes, not me, at the time he came in and wanted to talk to me about taxes. Bob then asked me who gave me this report and I declined to say.

When Alsop broke into the conversation, it became hilarious, and I asked him what the technique was for making the New York Times with his column. He said, "The prescription was simple—all I have to do is to either mention one of Sulsberger's favorite New York Jewish friends, who are also my closest friends, or merely hint that Sulsberger's taxes might be reduced."



TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE DEC 7 1938

TO Secretary Morgenthau
FROM Mr. Oliphant

To get your instruction

Another conference was held this afternoon in my office with Messrs. Hamilton and Ward of the State Department on the Chinese tung oil proposal.

We made a suggestion to meet what I understood was the objection raised by the State Department. The suggestion was that any arrangement entered into would provide: (1) that the amount of tung oil promised for American consumption would bear the same proportion to the presently available supply as the amount purchased for such consumption in 1937 bore to the amount produced in that year, and (2) that the period of the contract be extended to five years in order to lessen the maximum amount of oil undertaken to be delivered in any one year. The representatives from the State Department indicated that this would remove all objections which they had made under the Nine Power Treaty.

It developed, however, that they had a further objection directed to the Treaty of 1844. In order to overcome this objection, it appears that it would be necessary to remove the Chinese Government entirely from the picture.



*Rangoon. weekly cable
congrat
railhead. 77*

THE UNDER SECRETARY OF STATE
WASHINGTON

December 8, 1938.

*Haiphong.
S.I. Bank.*

Dear Henry:

I am giving you for your personal and confidential information a copy of an aide mémoire left with me this morning by the British Chargé d'Affaires.

Some time ago there commenced an off the record and unofficial exchange of views between this Government and the British Government with regard to the possibility that both Governments give consideration to retaliatory measures of a commercial or financial character that might be taken in view of the discrimination shown by the Japanese Government against United States and British commercial and financial interests in the Far East. This aide mémoire, as you will see, deals with this question.

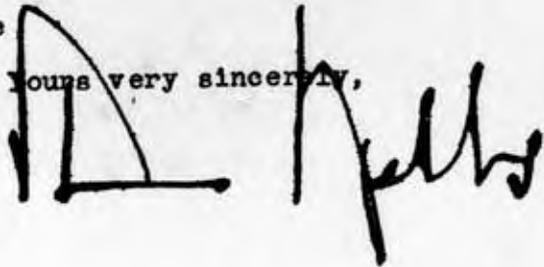
Will you let me have the benefit of your views with regard to the specific suggestion made in this communication from the British Government. What I would like, of course, particularly to know is whether this Government could take such a step as that proposed by the British Government without specific authorization from the Congress of the United

The Honorable
Henry Morgenthau, Jr.,
Secretary of the Treasury.

States.

Believe me

Yours very sincerely,

A handwritten signature in black ink, appearing to read "A. Kelly". The signature is written in a cursive style with a large, sweeping initial "A" and a long horizontal stroke extending to the right.

COPY

AIDE MEMOIRECONFIDENTIAL

Sir A. Cadogan informed the United States Chargé d'Affaires in London on December 3rd that to their regret His Majesty's Government were still not quite ready to furnish considered views in regard to possible punitive measures of retaliation or pressure on Japan. It had, however, occurred to them, he said, that third party interests in China might derive a certain measure of protection and benefit if, quite apart from economic and financial reprisals, steps were taken to support the Chinese currency. The Chinese Government had in fact recently requested that British banks should make a contribution of at least £3,000,000 sterling to a currency stabilization fund, an equal amount being put up by Chinese banks. A small committee of Chinese and British bankers would control policy and the operation of it through the two British banks i.e. the Hong Kong and Shanghai Bank and the Chartered Bank of India, Australia and China. The Chinese Government intimated unofficially at the same time that if foreign support could be increased to five or ten million pounds, the margin of safety would make the Chinese dollar impregnable over a long period.

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The United States Chargé d'Affaires was informed that His Majesty's Government were in fact considering a proposal to introduce legislation to guarantee a contribution of £3,000,000 by the Hong Kong and Shanghai Banking Corporation to the projected fund. Appropriate arrangements would of course be made to try to ensure that the fund if set up would be utilised solely for the purposes for which it was said to be necessary.

So far His Majesty's Government have reached no conclusion in the matter but their decision on the question of a contribution to a currency stabilisation loan would be greatly influenced by the knowledge that the United States Government were willing to take parallel and simultaneous action.

BRITISH EMBASSY

WASHINGTON, D.C.

December 7th, 1938

loaned to Foley 12/29
returned by Foley 12/30 80

December 8, 1933.

MEMORANDUM

TO: Secretary Morgenthau
FROM: Mr. Gaston

SUBJECT: Memorandum of November 23rd to the President from Chairman Eccles.

The general subject considered in the memorandum is the desirability of banking legislation and Chairman Eccles' personal views with respect to the nature of the legislation which seems to him desirable.

I. TIMING OF LEGISLATION - Chairman Eccles thinks there should be legislation at this session of Congress.

II. PROCEDURE - Chairman Eccles does not think it desirable that Federal agencies should agree upon a program of legislation to be presented to the Congress. Instead he would have the President make brief reference in his annual message to "the need for further constructive banking legislation," leaving it to Congress to conduct a disinterested inquiry and work out the legislation. He suggests that the Board of Governors in its annual report "make a reasonably complete statement of the existing conditions and express willingness to appear before Congress, if called, to advise upon appropriate legislation."

III. FORM OF LEGISLATION -

(a) Merger of Federal banking supervisory agencies to avoid conflicting jurisdiction. If called upon to testify Chairman Eccles would suggest that the Chairman of the F.D.I.C. be appointed to the existing vacancy on the Federal Reserve Board and that the Chairman of the Board of Governors be put on the F.D.I.C. to fill a vacancy that would be created by eliminating the Office of the Comptroller of the Currency. The Secretary of the Treasury would appoint the third member of the F.D.I.C. Board. The reorganized F.D.I.C. would take over all bank supervisory functions, leaving regulatory functions in the Federal Reserve Board. It is further suggested that the new F.D.I.C. be physically housed in the Federal Reserve building or in adjacent quarters. "This joint housing would in turn eliminate duplication of statistical and other functions."

- 2 -

(b) All insured banks should be blanketed into the Federal Reserve System.

(c) The Federal Reserve System should be "freed from private banker influence." To accomplish this bankers should be removed from the directorates of the Federal Reserve Banks, leaving three representatives of commerce, agriculture and industry to be elected by the banks; three others to be appointed, as now, by the Board of Governors and the seventh to be chosen from or by State bank supervisory authorities. The System would buy the stock in the Federal Reserve Banks now held by the banks and after accumulation of a sufficient surplus all earnings would go into the Treasury as a franchise tax.

(d) Federal Reserve System should have more power, specifically (1) Increased power to deal with foreign balances, particularly those of foreign governments and foreign central banks." (2) The System "should have restored to it the power to buy Treasury bills directly from the Treasury as can be done by every other central bank in the world."

(e) It is also highly desirable to discontinue purchases of silver which likewise further increase the excess reserves of the banking system. "That the silver policy is not even politically justifiable is indicated by the attached resolutions of the American Mining Congress."

IV. REASONS AND OBJECTIVES -

(a) "Our banking system remains fundamentally unsound. Responsibilities and authority are scattered among various agencies; there is much overlapping, duplication, conflicting jurisdiction; * * * efforts of the Treasury and of the Reserve System to carry out that (easy money) policy tend to be frustrated because some of the agencies pursue contrary practices or policies; * * * there are 'numerous paralyzing discriminations' as between different classes of banks; * * * enforcement of sound banking standards and the Government's ability to carry out national policy in the public interest become a mockery when banks may at will escape supervision by the Federal authorities. This makes for the competition in laxity which has long been a blot on the American banking system."

(b) Powers of the Federal Reserve System to cope with extraordinary credit developments such as "the fortuitous inflows of foreign capital and gold" are wholly inadequate "and the Reserve System is placed in the untenable position of having a tremendous responsibility which it is incapable of discharging because of lack of adequate powers and divided and conflicting banking authorities scattered among Federal and State jurisdictions."

- 3 -

(c) The present system leads to disputes over authority and "results in the frustration of monetary and credit policies by actions of supervisory agencies." Example - last spring's coordination of bank examination policy can not be applied in a sympathetic and understanding way because of "wide differences of interpretation and application." The effect of the easy money policy of the Administration "and the Reserve authorities" is largely nullified "when bank examiners following outworn methods entirely unrelated to monetary policy, criticize the banks for making the kind of loans which are required by the communities in which they operate."

(d) The Chairman would regard himself as remiss in his obligation to the President if he were "to let the impression stand that I felt that the banking situation was safe, and that no steps needed to be taken to safeguard it against the dangers ahead."

V. COMMENT (By H.E.G.) ON ECCLES RECOMMENDATIONS -

(a) Throw the fight into Congress. I could think of few things that could do more harm to the Administration than this, which calls for the airing of intra-administration squabbles and unwillingness by Chairman Eccles to submit himself to the regularly established channel for colation and appraisal of suggestions for banking legislation. It seems to me it would be a clear abdication of the President's responsibility. The only merit I can see to this suggestion is that there might be some sense in consulting a few responsible leaders of both parties on the Hill after some reasonable degree of understanding had been reached among the various agencies concerned.

(b) Extension of the Federal Reserve's power. Eccles proposes that the Federal Reserve Board shall have two out of three places on the F.D.I.C., which is to be responsible for all bank supervision and that the F.D.I.C. should be, to all practical effect, made an agency of the Board of Governors of the Federal Reserve System. The mere proposal is not to me so objectionable as the stated purpose for which it is to be done, which is to use the examining power as a control mechanism for relaxing and tightening credit. I don't think it is true that "our banking system remains fundamentally unsound" or that there is "a competition in laxity," or that other banking agencies are frustrating the policies of the Administration; or that there are "paralyzing discriminations" as between banks. The domination over the entire monetary and credit system of the country which Chairman Eccles seeks would, it seems to me, be far more perilous than any of the defects, or a combination of all the defects, of the present system. I doubt that the Congress would want to place in the hands of a continuing board such autocratic powers over the economic life of the nation or that any President would dare to recommend it.

Summary of memorandum to the President

1. Banking situation, dealt with on emergency basis, needs to be put on permanent basis before ending bank holiday.
2. Banking system should be integral part of Government mechanism to meet domestic or internationally created emergencies.
3. Government lacks power to cope with foreign capital; gold inflow of 7 billions in last 5 years; multiplication of Federal agencies; conflicting jurisdictions; discriminations against member banks; competition in laxity inevitable when banks can at will escape supervision; Government cannot make policy effective; easy money policy frustrated by contrary examination-investment policies.
4. Need for simplification greater than ever due to increase in Federal agencies; precedents in Farm Credit Administration; Home Loan Bank Board. Chart.
5. Inadequate power to absorb impact of foreign capital, except as Treasury sterilized; unpopular; would increase interest rates, add to public debt.
6. Stop silver purchases; Mining Congress resolutions.
7. Bank examination and investment policy contrary to easy money policy; agreement of last spring requires sympathetic administration; these policies must be closely integrated with monetary policy.
8. Action needed at this session; grave risk to let situation go until after 1940; give opposition issue.
9. Procedure; President's message; Reserve Board should report facts; this approach preferable to attempt to get agreement of Federal agencies; Congress jealous of prerogatives; prearranged Administration bill might provoke partisan attack; better to put responsibility up to Congress which will be to blame if it fails to act; Administration would get credit for legislation if Congress acts.
10. Form of legislation; transfer Comptroller's and Reserve examining functions to FDIC; interlock FDIC and Reserve Board, giving former supervisory and latter regulatory powers; cover all insured banks into Reserve System, abolishing membership as such but requiring insured banks to carry reserves with Reserve banks, exempting from insurance assessments; take bankers off Reserve bank boards; abolish stock, letting System build up capital out of earnings, surplus to be paid annually into Treasury.
11. Would also recommend power to deal with foreign government or central bank balances; restoration of power to buy Treasury bills directly from Treasury.
12. Important thing is to solve problems; if better way available than foregoing, ready to accept; would not wish to go contrary to President's wishes, but would like moral support.
13. Retention of Reserve System probable; adequate facilities, staff, personnel; Board named by President; have responsibility without power; untenable position.
14. Chairman's obligation to make facts known to President; question of reappointment; failure to report situation to Congress would imply ignorance or fear to do so.

November 25, 1938.

MEMORANDUM:

TO - The President
FROM - Chairman Hoopes

Need for banking legislation

In March, 1935, you declared a National Emergency. It should be terminated before your term expires. Yet it cannot be safely terminated until a banking system has been created which can withstand the impact of changing economic conditions, and a coordination of Federal banking supervision has been established that will be capable of exerting its influence towards the control of an inflation or towards cushioning a deflation when either of these conditions becomes dangerous to the national economy.

The Administration's courageous and effective actions in dealing with the most acute banking collapse in history have evoked universal commendation. The restoration of confidence in the banks and the subsequent recovery, however, have tended to obscure the fact that our banking system remains fundamentally un sound. It has been dealt with on an emergency basis. It needs now to be dealt with on a broader, more permanent basis

- 2 -

of reconstruction so that it can function effectively as an integral part of the Government's mechanisms for coping not only with potential future emergencies of inflation or deflation but also with an emergency that might be created by the international situation. The effective organization of the banking system is a basic and essential part of any comprehensive program of preparedness.

The system is not now so organized. Responsibilities and authority are scattered among various agencies; there is much overlapping, duplication, conflicting jurisdiction; there is lack of uniformity both in practices and in policies so that, as for example in connection with the Administration's easy money policy, efforts of the Treasury and of the Reserve System to carry out that policy tend to be frustrated because some of the agencies pursues contrary practices or policies; the system is characterized by numerous paralyzing discriminations as between member banks of the Reserve System, insured banks and State banks not under Federal supervision; enforcement of sound banking standards and the Government's ability to carry out national policy in the public interest become a mockery when banks may at will escape supervision by the Federal authorities. This makes for the "competition in

larity" which has long been a blot on the American banking system.

Because of the multiplication since 1939 of Federal agencies either with supervisory or lending powers, or both, the situation has become even more unsatisfactory, and the need for reorganization, consolidation and simplification the more urgent. An excellent precedent is to be found in the Administration's bringing together under the Farm Credit Administration of the scattered authorities that previously were divided among the Federal Farm Board, the Federal Farm Loan Board, the Reconstruction Finance Corporation, the Department of Agriculture and the Treasury Department. As the President declared, this reorganization of the farm credit powers was "to eliminate overlapping, prevent duplication, settle conflicting jurisdictions--in short, to provide a more efficient, logical and consolidated credit service for the farmers at low cost." The same general reasons apply with even greater force to the banking situation today. Another precedent is to be found in the Administration's merging in the Home Loan Bank Board supervision of the operations of the Home Owners' Loan Corporation, the Home Loan Bank System, the Federal Savings and Loan Associations and the Federal Savings and Loan Insurance Corporation.

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In striking contrast, the attached chart portrays the disorganized, complex and irrational structure of the Federal banking agencies.

Beyond these conspicuous structural defects, however, the banking system is in no position today to withstand another severe inflationary or deflationary crisis, and the Federal authorities are without adequate means of exerting a control over the vast and volatile credit reservoirs, swollen by the fortuitous inflows of foreign capital and gold, nor has the banking system any adequate means of protecting the domestic economy from these foreign movements.

If the Federal Reserve System, with its nation-wide organization, extensive equipment and trained personnel, has any basic justification for existence it is to exert an influence towards greater economic stability and to mitigate speculative credit excesses and inflationary or deflationary extremes. Yet while the Congress has vested the Reserve System with certain powers to cope with such credit developments, these powers today are wholly inadequate, and the Reserve System is placed in the untenable position of having a tremendous responsibility which it is incapable of discharging

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because of lack of adequate powers and divided and conflicting banking authorities scattered among Federal and State jurisdictions.

In the past five years there has been an addition of seven billion dollars to the monetary gold stock of the country, resulting principally from a flight of capital from Europe. On the basis of reserves created by this gold there could be a credit expansion that would wreck our economic machine. Yet there is no power in any agency of Government to take action to control these reserves, except the power of the Treasury to do so by increasing the public debt. This is politically difficult and would result in a rise in the cost of borrowing. If the Treasury had to borrow a constantly increasing amount for the purpose of sterilizing present excessive gold stocks, as well as future inflows, the result would be an increase in the interest cost not only on the amount borrowed for this purpose but also on all borrowing that the Treasury had to undertake. Some method other than this must be devised for discouraging the inflow of foreign capital and gold and for controlling the effects on our economy of the gold that has already come to this country and that may come in the future.

It is also highly desirable to discontinue purchases of silver which likewise further increase the excess reserves of the banking system. The silver program is an unnecessary and useless one for monetary and credit purposes and serves solely as a subsidy to silver producers. That the silver policy is not even politically justifiable is indicated by the attached resolutions of the American Mining Congress.

Results of present organization of Federal authorities

Not only does the present set-up foster inefficiency, but it leads to disputes over authority and results in the frustration of monetary and credit policies by actions of supervisory agencies. As a recent example, at the President's request last spring a conference of the Federal banking agencies was called under the leadership of the Secretary of the Treasury for the purpose of better coordination of bank examination policy. After extended discussion and compromise, an agreement was finally reached, coupling with it a modification of the Comptroller's Regulation. Sympathetic and understanding administration is necessary to carry out the purpose and spirit of the agreement in practice. Such administration is not to be expected when there are wide differences of interpretation and application of the terms of an agreement representing a com-

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premise of widely divergent views.

Outworn examining practices have not only frustrated Administration policy which the Treasury and Federal Reserve have sought to carry out, but have served to accentuate deflation on the downswing and to encourage over-expansion and speculation on the upswing. Congress has recognized by legislation and the Reserve authorities are endeavoring to follow the principle of taking monetary action so as to reduce the violence of both inflation and deflation. Both the Administration and the Reserve authorities have consistently followed an easy money policy designed to encourage bank lending and investment so as to stimulate business, which, in turn, would relieve the Government of a corresponding amount of public borrowing. The effect of these policies and actions is largely nullified when bank examiners following outworn methods entirely unrelated to monetary policy, criticize the banks for making the kind of loans which are required by the communities in which they operate.

Old-fashioned bank examination methods, still being pursued, attempt to force banks to liquidate on the downswing, thereby accentuating deflation and undermining the banks' loans

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and investments. This not only discourages the banks from making new loans at the very time the Government is attempting to encourage them to do so, but it places additional burdens upon the Federal budget by requiring the Government to set up Federal agencies to supply the credit which the banking system is thus discouraged from supplying, and to expand the supply of money and put it into circulation through relief and other programs because of the deficiency resulting from bank liquidation and the failure of private credit to expand.

The time for improving the quality of bank assets is under boom conditions. That is when banks make loans and investments that later get them into trouble. However, this is the very time when bank examination policy fails to discourage unsound loans and investments because it persists in measuring value by the artificial yardstick of ticker quotations, which are likely to be as unrepresentative of true worth in a speculative period as they are when all prices are abnormally depressed.

I have set forth the foregoing at some length not only as an example of conflicting policies, due to the existing diffusion of authority, but because this case particularly reflects the necessity for close coordination of bank examination

- 2 -

and investment policy with Government monetary policy.

Authority over monetary policy is largely useless unless such authority is closely integrated with bank examination and investment policy. In principle, authority over all these functions should be vested in one agency, but, in any case, should be vested in closely coordinated agencies.

The situation calls for action at this session of Congress

These problems should not be left for consideration later than this winter inasmuch as a year from now the country will be on the eve of a presidential election. The banking holiday should be terminated before that time. To leave the situation until after 1940 would involve a delay that might prove disastrous in the face of future speculative and inflationary potentialities and taking into account world conditions together with the exposure of our credit system to foreign influences.

To let the situation drift would not only indicate unawareness or unwillingness to face it, but would give the opposition an opportunity to make an issue of it in the 1940 campaign. If the Administration were to put the responsibility up to Congress at this session, not only would there be no

opportunity to make such a case against this Administration, but responsibility for future consequences would be upon the shoulders of the Congress.

The procedure

It would be desirable if the President in his message to Congress would in a paragraph or two indicate in a general way the need for further constructive banking legislation to enable the banking system to deal more effectively with the present situation and future developments. Then, in its annual report to Congress, the Board of Governors, it seems to me, should make a reasonably complete statement of the existing conditions and express willingness to appear before Congress, if called, to advise on appropriate legislation. Or, should the Board for any reason not see its way clear to make such a report, then the Chairman at least should do so.

This course seems to me to be far preferable at this time to attempting to bring about an agreement among Federal banking agencies upon a specific piece of legislation, which would be regarded as an Administration bill and would be almost certain to be attacked on partisan grounds. Moreover, as you are aware, the members of Congress are jealous of their pre-

regulatory and essential at having any one agency present undried legislation for passage. If the President requested Congress to assert this prerogative and to work out necessary legislation, hostile members of Congress would not be able to side-step the responsibility, and all agencies interested in the legislation would have an equal opportunity to present their views.

If legislation results, the credit would redound to the Administration. Whereas, if Congress fails to act after having been requested to do so, the onus will be on the Congress or on the groups that blocked action. Instead of leaving an issue for the Republicans to make much of in 1940 and against which the Democrats would find it difficult to make a defense, those responsible for blocking the legislation will be on the defensive.

Form of legislation

I believe that Congress would be willing to initiate a program bringing about a merger of Federal banking supervisory agencies that would largely avoid conflicting jurisdictions and effect a much better set-up of the Federal agencies.

The Comptroller of the Currency is almost entirely today an examining agency for national banks, the other functions

of the office being minor. The Federal Reserve System examines State member banks. The Federal Deposit Insurance Corporation examines State insured banks that are nonmembers. It would seem to me to be politically feasible to obtain legislation which would merge the examining functions of the Comptroller's office and of the Federal Reserve System with the Federal Deposit Insurance Corporation, whereas any other method of complete consolidation of these functions would, in my opinion, be impossible to obtain from Congress. This would be logical because all of the banks now examined by the various Federal agencies are insured banks. This would place in one agency all Federal examination, supervisory and chartering functions, while there should be consolidated in the Reserve System all of the regulatory functions, thus eliminating the numerous discriminations now existing between member banks and nonmember banks. Attached is a memorandum showing the many existing discriminatory provisions of law.

If this were done, it would be important, however, to have examinations, chartering, supervision of trust departments, and other supervisory functions carried on with close

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coordination with the Federal Reserve. To bring this about, I would suggest, if called upon to testify, that the Chairman of the FDIC be appointed to the vacancy now existing on the Board of Governors and that the Chairman of the Board of Governors be put on the FDIC to fill the vacancy on that Board which would result from merging the office of Comptroller. I would suggest that the third member of the FDIC be designated by the Secretary of the Treasury to represent him on the FDIC Board and to serve at his pleasure. The effect of this would be to have on the FDIC Board two out of three members who are also members of the Federal Reserve Board. This would afford an excellent opportunity to work out a harmonious and co-operative program of relations and of integrating examination with monetary policy. In the new Federal Reserve Building there is considerable available space and there is also an adjoining vacant building lot for future expansion of all the offices required by such a merger. This joint housing would, in turn, eliminate duplication of statistical and other functions.

I mention the foregoing possible solution of the organization problem, but should some better set-up be devised, or should you prefer some other course, I would naturally wish

to defer to your judgment. My own guiding view is merely that the present set-up is unsound and impractical, and I am not wedded to any one solution but only to the necessity of getting some solution. The most practicable compromise, I think, would be the plan suggested, calling upon both the Reserve System and the Comptroller's office to give up their examining functions to the FDIC, then coordinating the FDIC and the Reserve Board so that policies, now and in the past repeatedly in conflict, may be harmonized.

An important part of this pattern, I think, would be to do away with the existing legal barriers to membership in the Reserve System, and, in fact, to scrap altogether the restrictive membership requirements, by blanketing all insured banks into the System and requiring that they carry their reserves with the Reserve banks, at the same time, of course, being entitled to all of the privileges of the Reserve System. One provision that I favor, which would, in my judgment, make this proposal more attractive to the insured banks, would be that they be relieved of paying insurance assessments on the funds they carried with the Reserve banks as reserves. This would also have the desirable effect of tending against the

over-concentration of correspondent bank balances in the large money centers, chiefly in New York. It would have an incidental effect of serving to put a bottom of 1/12th of 1 per cent on interest rates.

I would also recommend, if asked, that the Federal Reserve System be completely freed from private banker influences and made unequivocally a public body. While the truth is that the system is not banker dominated, it has been much criticized by Fetsman, Coughlin and others because private bankers are on the boards of the twelve Federal Reserve banks and because member banks hold stock in the Federal Reserve banks, on which stock they receive a 6 per cent dividend, a rate that is out of line with current returns.

I, accordingly, would recommend that bankers be removed from the directorates of the Federal Reserve banks; that such directorates consist of three representatives of commerce, agriculture and industry who would be elected by the banks; that three others representative of the public interest be appointed, as now, by the Board of Governors, and that a seventh director be chosen either from among or by State bank supervisory authorities. This would reduce the number of directors from

also, as at present, to seven, and would give the Board an equal number with those elected by the banks, while the State banking authorities would be represented by the seventh member.

I would also recommend that the Reserve bank stock be done away with entirely, as it is not necessary. I would suggest that the Reserve System be permitted to accumulate in its capital account out of earnings a sufficient amount to offset the loss of capital due to paying off the stock, but all earnings in excess of such amount to be paid into the Treasury each year as a franchise tax. These two changes would remove two principal, though exaggerated, complaints against the present set-up of the System.

It is also important that the Reserve System be given increased power to deal with foreign balances, particularly those of foreign governments and foreign central banks. Likewise, the Reserve System should have restored to it the power to buy Treasury bills directly from the Treasury as can be done by every other central bank in the world.

There are various other recommendations I would make, if called upon, which I feel would strengthen and simplify the existing banking system, but the foregoing are the principal and most important ones.

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It would be very helpful to me to feel that I had your moral support in connection with remedying the banking situation at this time. I would not want to make recommendations contrary to your wishes, if I should be asked to testify before Congress. The steps I have outlined would, I think, meet with a minimum of political resistance, while accomplishing desirable results.

Retention of Reserve System

Since no modern economy can get along without a central banking organization, I have assumed the continuance of the Reserve System in any plan of reorganization. The Reserve System, created nearly a quarter of a century ago, performs numerous essential functions for the banking system, and if abolished would have to be replaced by some other system to perform the same functions. The Reserve System has an extensive physical plant, consisting of the 12 Federal Reserve banks with their 24 branches and agencies, located in principal cities throughout the country, and the Board of Governors in Washington occupying a recently constructed building with ample facilities to accommodate all existing Federal banking functions, and with material savings in the elimination of duplication. All of this represents a large investment in property. In addition, the Re-

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serve System has a continuing and trained personnel both in the field and in Washington.

The Board of Governors of six members now—seven required by law—has its own trained staff of lawyers, examiners, statisticians, economists, etc., the personnel in Washington numbering more than 550. Under the law the Board is a continuing agency, and it is able to contribute that expertness which follows from continuous service. It is able to devote its full time and resources to the single purpose of dealing with banking and monetary matters. The present Board was selected entirely by this Administration. It is one, therefore, in which the President can have confidence. Under existing circumstances, the Board is in the unenviable position of lacking authority to discharge the responsibilities imposed upon it by law, and I question whether the Board can hold or continue to attract the services of public-spirited men if this situation is not remedied.

Speaking for myself, I would not wish to continue in the Chairmanship of a System which in the minds of the public and of Congress is charged with great responsibility for exercising controls over domestic credit and monetary conditions,

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when, in fact, as it exists today, the System's powers and authority are largely limited to the performance of mechanical functions.

In conclusion

Without venturing to speak for other members of the Board, I, as the Chairman, find myself in the situation where I would be open to the charge of failing in my public duty, and I feel that I would be equally remiss in my obligation to the President, if I were to let the impression stand that I felt that the banking situation was safe, and that no steps needed to be taken to safeguard it against the dangers ahead. My term expires a year from February, and I have no right choice, it seems to me, except to bring to your attention well in advance of the end of my term the necessity for remedial action before the problems become acute, and there is a flare back of criticism. Otherwise I would be justly charged either with not knowing the facts or withholding them for some reason. While my reappointment, a year from February, may be out of the question for other reasons, in any case, as I view it, I should not put the President in the position of considering for reappointment an official who had so far failed

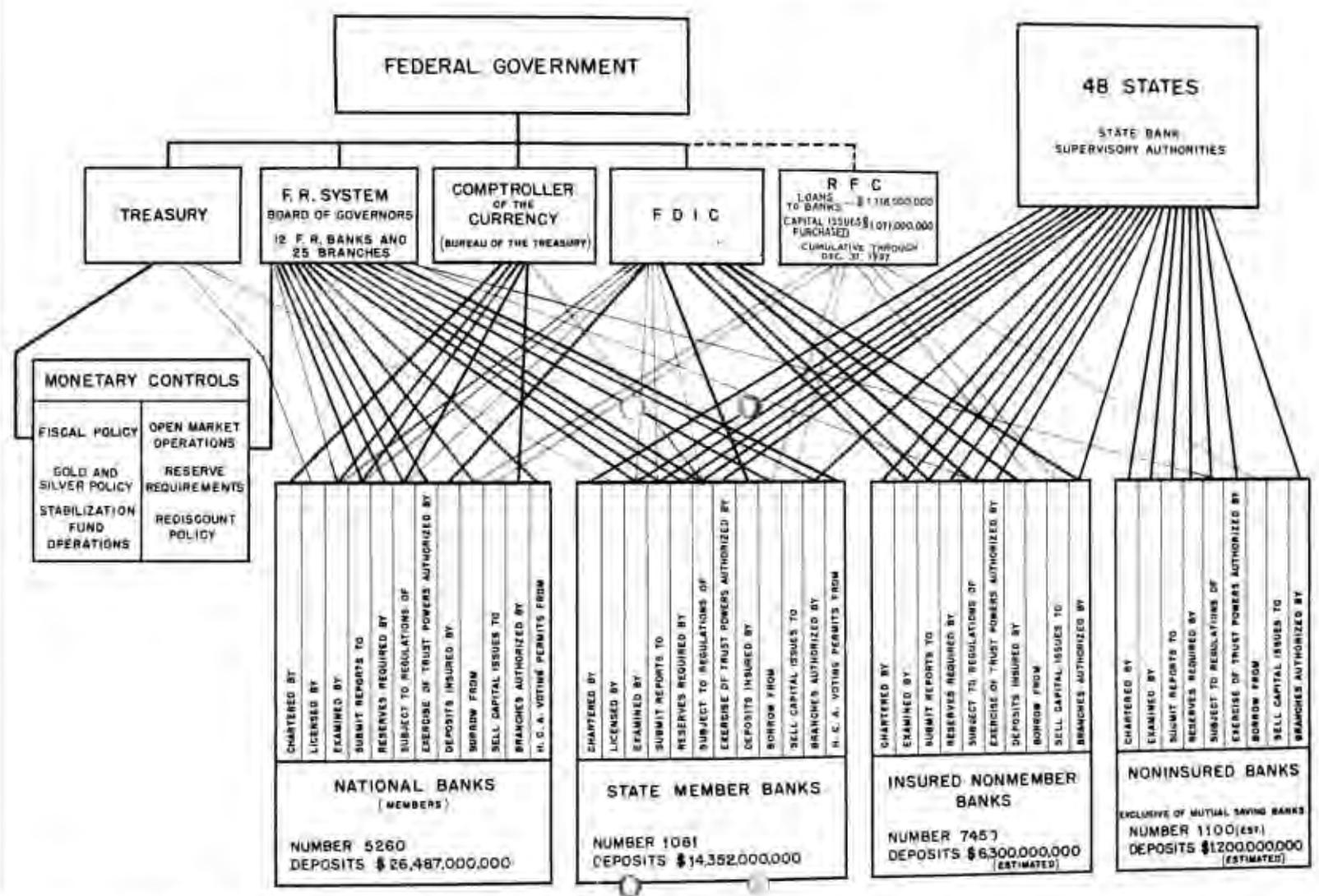
- 20 -

in the discharge of the responsibilities of his office.

I think it is clear that, as Chairman of the Board, I have a responsibility to bring these general considerations to your attention so that, if you consider it appropriate to do so, you may include in your message the request that the Congress take cognizance of the situation with a view to providing the necessary remedies and safeguards. Thereby, I feel, the Administration will have done its part, and the responsibility for action will be clearly upon the Congress.

Attachments.

PRINCIPAL BANK SUPERVISORY RELATIONSHIPS



———— MAJOR SUPERVISORY RELATIONSHIPS
 - - - - - INCIDENTAL SUPERVISORY RELATIONSHIPS

NUMBER AND DEPOSITS AS OF DEC. 31, 1937.

DISCRIMINATION IN FEDERAL BANKING LAWS

In addition to laws peculiarly applicable to the National Banking System, the Federal Reserve System or the Deposit Insurance System as such, Congress has enacted many laws for the general purpose of preventing unsound banking practices and requiring banks to operate in a manner conducive to the public interest.

It would seem that laws of the latter class should apply uniformly to all banks subject to the jurisdiction of Congress; but they do not do so. Some of them apply only to national banks, most of them apply to all member banks of the Federal Reserve System, but only a few apply to nonmember insured banks.

This is not the result of deliberate policy or design but of fortuitous circumstances incident to the gradual development of Federal supervision of banking.

From 1863 to 1913 Congress assumed jurisdiction over no banks except national banks; and the Federal banking laws enacted during this period naturally were made applicable only to national banks.

In 1913 Congress extended its jurisdiction to those State banks which chose to join the Federal Reserve System and extended some, but not all, of the general regulatory provisions of the National Bank Act to them.

Practically all remedial or regulatory banking laws enacted from 1914 to 1933, inclusive, were made applicable to all member banks, State and national alike.

-2-

In 1933 Congress extended its jurisdiction to all State banks which chose to have their deposits insured by the Federal Deposit Insurance Corporation; but it was not until 1935 that it started extending its regulatory provisions to them; and so far only a few of the general regulatory provisions of the Federal banking laws have been extended to them.

The result is shown in the attached table, which disregards laws peculiar to the organization of national banks, membership in the Federal Reserve System, or the insurance of bank deposits and relates only to general regulatory provisions which could properly be made applicable to all banks subject to the jurisdiction of Congress.

A glance over the table will disclose that these laws leave State member banks more freedom than national banks and leave non-member insured banks much more freedom than member banks.

Stated differently, it discloses that although the Federal Government has assumed the responsibility for insuring the deposits of all insured banks, it has not thrown the same safeguards around the transaction of the banking business by non-member insured banks as it has with reference to member banks.

In view of the facts that all national banks are required to be member banks, all member banks are required to have their deposits insured, and member banks pay approximately 85 per cent of the assessments to support the deposit insurance system, the result seems not only nonsensical but unjust.

-3-

In order to remedy this situation it is not necessary to require that all insured banks be national banks or to require that they all be member banks. It would be sufficient to extend to all insured banks those general regulatory provisions of law which Congress deems necessary or desirable for the purpose of preventing unsound banking practices and requiring the banking business to be conducted in a manner conducive to the public interest. To do so would reduce the risks of deposit insurance, eliminate unfair discrimination between different classes of insured banks, and require all insured banks to operate in the public interest.

On the other hand, if any of these general regulatory laws are too strict or are not necessary or desirable in the public interest, they should be modified or repealed and should not be left on the statute books to hamper member banks alone.

COMPARISON OF FEDERAL STATUTORY PROVISIONS
REGULATING AND RESTRICTING THE BUSINESS OF
DIFFERENT CLASSES OF BANKS

Type of Statute	Applicable to		
	National Banks	State Member Banks	Nonmember Insured Banks
Restrictions on real estate loans.	Yes	No	No
Regulations governing exercise of trust powers.	Yes	No	No
Restrictions on acting as insurance agent.	Yes	No	No
Restriction on acting as real estate loan broker.	Yes	No	No
Prohibition against holding "other real estate" for more than five years.	Yes	No	No
Limitation on indebtedness which bank may incur.	Yes	No	No
Restriction on loans to executive officers.	Yes	Yes	No
Restrictions on dealings with directors.	Yes	Yes	No
Prohibition against paying preferential rate of interest on deposits of directors, officers, etc.	Yes	Yes	No
Restrictions on interlocking directorates between bank and other banks.	Yes	Yes	No
Restriction on interlocking directorate between bank and securities companies.	Yes	Yes	No
Prohibition against securities affiliates.	Yes	Yes	No
Prohibition against acting as medium or agent in connection with loans to dealers in securities.	Yes	Yes	No
Prohibition against affiliation with other corporations.	Yes	Yes	No
Limitations on loans to affiliates.	Yes	Yes	No
Limitations on investment in bank premises.	Yes	Yes	No

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Type of Statute	Applicable to		
	National Banks	State Member Banks	Nonmember Insured Banks
Minimum capital requirements.	Yes	Yes	No
Prohibition against loaning on or purchasing own stock.	Yes	Yes	No
Restrictions on withdrawal of capital and payment of unearned dividends.	Yes	Yes	No
Prohibition against impairment of capital.	Yes	Yes	No
Requirement that reserves specified in Federal Reserve Act be maintained.	Yes	Yes	No
Prohibition against making loans or paying dividends while reserves deficient.	Yes	Yes	No
Restrictions on purchase of investment securities and stock.	Yes	Yes	No
Limitations on acceptance powers.	Yes	Yes	No
Limitations on loans to one borrower.	Yes	Yes	No
Limitations on loans secured by stocks or bonds.	Yes	Yes	No
Minimum capital for branches.	Yes	Yes	No
Restrictions on establishment of branches.	Yes	Yes	Yes
Restrictions on payment of interest on deposits.	Yes	Yes	Yes
Prohibition against loans or gratuities to bank examiners.	Yes	Yes	Yes

EXCERPTS FROM DECLARATIONS OF POLICY
ADOPTED BY THE AMERICAN BIRING CONGRESS
RESPECTING THE AMERICANIZATION PROGRAM.

September 26, 1935, at Chicago, Illinois, the Eastern Division of the American Biring Congress adopted a Declaration of Policy containing the following:

Constitutional Government

* * * * *

The present the attitude of many in authority in our Government who seek by specious use of words, phrases and interpretations to nullify the plain intent and spirit of our Constitution. We look forward with confidence and faith to the time when the Supreme Court again will declare in language unmistakable that its provisions, made for the preservation of individual liberty and freedom of action, are yet valid and binding. (Underlining supplied.)

* * * * *

Bureaucracy

Bureaucracy has grown to such an alarming extent that industry is now faced with a government, not by a system of checks and balances through legislative, judicial and executive branches, but a government by politically appointed commissions and administrators. Three-quarters of a million persons are employed by the Government, not counting the legislative and judicial branches, the Army and Navy, and special agents of the Department of Agriculture. Bureaucraticism is reaching out to every phase of our American life. (Underlining supplied.)

* * * * *

Palming the Deficit

Our Federal public debt is now in excess of thirty billions of dollars, and the appropriations made by the twenty-fourth Congress were in excess of ten billion dollars. No government can go on year after year spending more than it receives, and piling deficit upon deficit. Such a course inevitably destroys the currency, and leads to inflation and repudiation. Our Government should, therefore, take immediate steps to balance the Federal Budget by strict limitation of

B.

"governmental expenditures. Taxes should be levied only to provide necessary revenue, and not to effect social reforms, or to carry out schemes of redistribution of wealth. (Underscoring supplied.)

* * * * *

"Money

* * * * *

"To expose what is commonly known as 'managed currency,' (Underscoring supplied.)

* * * * *

"Government in Business

* * * * *

"Government, by its very nature, cannot conduct business efficiently; its invasion of business destroys individual enterprise, injures all citizens by unfair competition, and dries up the source from which its revenue is derived. We condemn and oppose such invasion.

"Labor

* * * * *

"We condemn the attempt on the part of Congress to set up an outside political body to intervene between employers and employees in their industrial relations.

"Relief

"We favor direct relief at subsistence rates rather than work relief administered by Federal agencies."

* * * * *

January 15, 1936, at its 38th Annual Meeting, the American Mining Congress adopted a Statement of Principles containing the following:

"Bureaucracy

"Check bureaucracy, abandon government by men and return to government by law."

October 1, 1938, at Denver, Colorado, the Western Division of the American Mining Congress adopted a Declaration of Policy containing the followings:

Taxation and Finance

• • • • •

"Amend the Federal tax laws to reestablish the flat rate of corporation tax, to restore the right to make consolidated returns, to remove the tax on dividends received by corporations, to permit business losses of one year to be deducted from future income, to provide full allowance of capital losses, and to permit annual declaration of value for capital stock taxes, particularly in case of mining properties in the development stage."

• • • • •

Extension of Federal Government

"We deplore the tendency to center supervision of business in the Federal Government.

• • • • •

"We oppose the growth of bureaucracy, and urge a return to government by law instead of by executive order or administrative decree.

• • • • •

Reciprocal Trade Agreements

"Changes in tariff rates should not be made through trade agreements with foreign countries without specific approval of such changes by Congress after public hearing."

September 10, 1937, at Salt Lake City, Utah, the Western Division of the American Mining Congress adopted a Declaration of Policy containing the followings:

Taxation

"The mining industry views with concern the continuation of excessive and unnecessary expenditures by the Federal Government.

• • • • •

"We recommend the reestablishment of the flat rate of corporation tax, the restoration of the right to make consolidated returns, the removal of the tax on dividends received by corporations, the carrying forward of business losses of one year to be deducted from future income, and the unlimited deduction of capital losses.

* * * * *

"Extension of Federal Government

"We deplore the growing tendency to regulate business by the Federal Government.

* * * * *

"We oppose the growth of bureaucracy, and urge a return to government by law instead of by men through executive order or administrative decrees.

* * * * *

"Labor

"The essential interest of employe and employer is to obtain efficient production through the cooperative efforts of labor, management and capital. Government interference with such cooperation should be avoided."

October 27, 1958, at Los Angeles, California, the Western Division of the American Mining Congress adopted a Declaration of Policy containing the followings

* * * * *

"Taxation

"Consistent with our belief of many years, we view with ever-increasing apprehension the continued unbalanced national budgets with mounting expenditures and progressive deficit financing made necessary thereby. Sound and proven theories of Government finance demand that the control of these expenditures MUST be returned to Congress. There alone, as the Constitution provides, responsibility for Government revenues can be united with responsibility for Government expenditures. Having properly resumed its

5.

"constitutional powers in this respect, Congress, if it would preserve the Nation from the financial catastrophes which have enveloped so many countries, should and must limit Federal expenditures to an amount which can be covered by taxation yield."

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TREASURY DEPARTMENT
INTER OFFICE COMMUNICATION

DATE December 8, 1938

TO Secretary Morgenthau
FROM Mr. Oliphant

For your information -

I talked at some length this morning with Mr. Lawrence Morris (who represents the Chinese delegation) and Ed Foley about the Chinese loan, with particular regard to some of the objections raised at the conference yesterday by Messrs. Hamilton and Ward from the State Department. Morris pointed out that it would be possible to rearrange the Chinese program to suit any formula acceptable to us.

At 2:15 this afternoon, the three of us met with Mr. Hanes in his office. Hanes agreed to extension of the period of the loan from three to five years, a formula for the apportionment of the supply of tung oil, the substitution of a Chinese private corporation for the Chinese Government as the procuring agent for the tung oil in China, and a guarantee of the loan by the Bank of China in lieu of a guarantee by the Chinese Government. Hanes expressed himself as being opposed to the use of any of the tung oil loan proceeds for war materials. Lockheed was called in and said that a condition to this effect should not create any insurmountable obstacle since the Chinese trading corporation would have other moneys to spend in this country, and by segregation of accounts could use the tung oil loan money only for the purchase of non-belligerent materials and other funds for the purchase of munitions. Mr. Chen was then called in and he verified Lockheed's statement. He

- 2 -

also reiterated in substance what Morris had told us as to their willingness and ability to meet any reasonable formula we proposed. Hanes then expressed himself as being satisfied, and at his suggestion I called Sumner Welles at 4:20. I recited to him the substance of our conversation with Messrs. Hamilton and Ward, whom he had sent over for me to talk to yesterday. I stated that they had expressed themselves as entirely satisfied with the following changes, which would remove any objections on the score that we were countenancing a Chinese monopoly or seeking to get more than our share of the tung oil production. These changes are:

(1) The period for the delivery of the 225,000 tons is to be lengthened from three to five years, thus further reducing the amount deliverable in any one year even further below recent production figures.

(2) That there will be no obligation to deliver to the United States a greater percentage of what they actually have for delivery to anybody than the ratio of last year's delivery to the United States to last year's total production.

I then mentioned to Welles the further objection of Messrs. Hamilton and Ward, that the Government of China was appearing in the transaction as such. This objection, I said, would be met by the organization of a new corporation in China by private individuals, which would deal with the American corporation. I mentioned that somewhere back of such private corporation would, of course, be the Foreign Trade Commission, and Welles said that that would be entirely satisfactory.

- 3 -

He then interrupted to state the thing which had given him "grave perplexity", namely, that since we were coming to square issue with Japan on whether the Nine Power Pact was still in force, he didn't want Japan to have any violation on our part to point to.

I then asked if I might go over the whole matter again with him so as to be sure he had it entirely in mind. I then recited:

(1) That no monopoly law had been passed, or would be passed by China.

(2) I repeated the double change, i.e., extending the period from three to five years and fixing a ratio to measure the supply to be made available to the United States, to meet the objection that we were grabbing more than our part of the tung oil.

(3) I again stated that the new corporation was to be formed by China and that back of it somewhere would be the Foreign Trade Commission.

(4) I then said that the loan would be guaranteed by the Bank of China, not by the Chinese Government.

(5) I mentioned that all the proceeds of the loans were to be spent in the United States and that none were to be spent for belligerent materials.

He then said, "It is entirely satisfactory with us over here that the thing go through on this basis. Would you be good enough, when it has been drafted, to send me a copy personally?"

- 4 -

I repeated that I understood on the basis stated it was entirely satisfactory for the loan to go through and he again said it was, and thanked me rather profusely for having given the matter so much attention.

Samuel O. ...

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

M 120

DATE December 8, 1938.

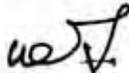
TO The Secretary
FROM Mr. Taylor

As I told you over the telephone, at the Export-Import Bank meeting I gave final approval to the I.T. & T. financing. This involves ten-year serial maturities with a $4\frac{1}{2}\%$ coupon and a purchase price of approximately 95, which averages out to about a $5\frac{1}{4}\%$ basis. A group of banks, including Guaranty, National City, J. P. Morgan, and others, will take five million. The Export-Import Bank will take ten million. This financing will clear up all current indebtedness of the I.T. & T., with the exception of ordinary commercial Bills Payable, and, in the opinion of those familiar with the situation, will put them in good shape, as after paying off their debenture issue which matures on January 1st, with the proceeds of this financing and cash which they have accumulated to meet the maturity, they will have no other maturities prior to 1952. No publicity will be given out until an agreement on the publicity has been reached between the banking group and the Export-Import Bank. On the whole, I think it will be fairly well received as it combines the banks' taking ten-year loans with cooperation on the part of the Government to help finance industry on a long-term basis.

In addition there was some discussion of the Portuguese Bridge proposal. It appears that in order to get the business we will have to raise our ante from five million to slightly over six million -- if it is good at all, six million ought to be as safe as five. This proposal is not in final form but we will have to give an answer fairly soon.

- 2 -

I also had an extended conversation with Mr. Bursley, who handles the Mexican end of the State Department, Cairns and Johnson, in connection with sending an investigator to Mexico to clear up the suspected dumping aspects of certain oil sales which are being made through Eastern States Petroleum. We are writing the State Department a letter asking for their help in arranging for the visit of our investigator, as State thinks that the situation is so delicate that if one of our men started investigating this particular case without the advance permission of the Mexican Government, that the public reaction might be unfortunate.



Kunming, Yunnan,

8th December, 1938

The Honorable

Secretary Henry Morgenthau, Jr.,

Department of Treasury,

Washington, D.C.

Dear Mr. Secretary,

I attach reports typed from notes sent me by Dr. Buck
from Chengtu.

Respectfully,

Enid Saunders

Enid Saunders
Secretary to Dr. Buck

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TREASURY DEPARTMENT

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Chengtu, December 1st, 1938

To Secretary Morgenthau

From J. Lossing Buck

INTERVIEW WITH GOVERNOR WANG CHAN-HSU OF SZECHUEN

"In the name of the people of Szechuen I express thanks for all the help from America in this war. We still need more assistance in the form of military supplies and we hope and desire this help from America.

"We do not fear a Japanese attack in Szechuen as we have made preparations. We have recruited and are giving training to 800,000 new soldiers. We have plenty of men and the recruiting has had no adverse effect on our economic life as we have taken those without important work to do.

"The Chinese Communists are not a problem in Szechuen. They are fighting wholeheartedly with the Central Government against Japan. They are not a large group and China has nothing to fear from them.

"Russia wants China to fight Japan as it is for her protection. We accept Russia's help but not her political doctrine. In China we have and give our allegiance to only one party, the San Min Chu I (the three principles of the Kuomintang Party).

"We are giving urgent attention to transportation and are building a narrow gauge railway from Szechuen to Kunming to be completed in two years.

"We are pushing gold mining to increase gold production."

Note: Governor Wang, a military general, is a native of Szechuen and very loyal to the Generalissimo. He is stated to be a straight forward type of person, but with limited ability. He often rides to the office on horseback to save gasoline. I gained a favorable impression of him.

Chengtu, December 2nd, 1938

To Secretary Morgenthau

From J. Lossing Buck

STATISTICAL DEPARTMENT, SZECHUEN GOVERNMENT

The Statistical Department of the Szechuen Government has an ambitious plan under way for obtaining various detailed statistics from each hsien; and the outlook, judging from the staff, is promising. One of the men is a former student of mine, who has had good training at the University of Nanking.

Chengtú, December 5th, 1938

To Secretary Morgenthau

From J. Lossing Buck

HIGHWAYS, SZECHUEN

The Commissioner of Highways of Szechuen states that the new road to Kunming, connecting with the Chungking-Chengtú highway at Lungchong, is passable in the Szechuen portion, but not fully completed. He is uncertain about the exact progress of the Yunnan portion.

A limited amount of highway construction is carried on in the nature of extension of existing roads and their improvement.

Chengtu, December 5th, 1938

To Secretary Morgenthau

From J. Lossing Buck

INTERVIEW WITH MR. KAO

CHIEF SECRETARY, COMMISSION OF FINANCE, CHENCTU

The Commissioner of Finance has been ill for some time, so my interview was with his chief secretary, Mr. Kao. The revenues of the province are 50,000,000 yuan, chiefly from land taxes, but one-fifth is from goods tax in transit. Szechuen being a rich province does not feel pinched for revenues as do the provinces of Kweichow, Kansu and Tsinghai. However, during this war the province is feeling the need for additional income.

Mr. Kao states that Central Government notes are in circulation in every hsien, and only in the distant hsien is the circulation of silver dollars still practised. Collection of silver is still taking place. Gold production amounts to over one million ounces annually, and some effort is being made to increase the production.

Chengtu, December 2nd, 1938

To Secretary Morgenthau

From J. Lossing Buck

CHENG TU

Adequate pursuit plane protection for Chengtu is in the process of realization. One hundred and fifty Russian pursuit planes and thirty bombers, some of which have arrived, are to be stationed at the Chengtu and other airfields in Szechuen. One airfield at Chengtu is to be given over to the Russian training force, and the other kept for the strictly Chinese training force. Mr. Schultze of Central Aircraft states the Generalissimo is cautious about having too many Russians in Szechuen, as he does not want too much Russian influence.

New forces are at work in Chengtu. Streets are kept very clean and policemen check up and see that sidewalks and pavements in front of each doorway are kept clean. Yesterday I saw a policeman admonishing a storekeeper for the mess in front of his shop, which was a strong contrast to the otherwise clean street.

The movement to save gasoline is effective and now one does not see wives of officials riding about in their husbands' cars, or such cars parked in front of theatres and restaurants.

Chengtu, December 1st, 1938

To Secretary Morgenthau

From J. Lossing Buck

CENTRAL AIRCRAFT COMPANY

The Central Aircraft Company has decided to build its plant near the Burma border along the Kunming-Burma road, rather than at Kunming. It will turn out two bombing planes per day. Protection will be afforded by their own men and their own pursuit planes. The location appears excellent, as Japanese pursuits cannot accompany their bombers that distance.

Mr. Schultze, a Curtiss-Wright man in charge of Central Aircraft's repair shop at Chengtu, speaks well of the ability of the Chinese to learn the art of plane manufacture and of past accomplishments. At Hangchow the company was turning out eighteen bombers per week, all manufactured there except engines and a few other parts.

The activities of Curtiss-Wright in China are a good illustration of how many types of American business could assist China and at the same time make reasonable profits.

Chengtu, December 1st, 1938

To Secretary Morgenthau

From J. Lossing Buck

INTERVIEW WITH DR. Y.G. CHEN, PRESIDENT OF UNIVERSITY
OF NANKING AND MEMBER OF PEOPLE'S POLITICAL COUNCIL

"At the meeting in November of the People's Political Council, Dr. Kung referred to the help of the U. S. Treasury, and to the favorable outlook for some type of credit from the United States. If this further assistance is not forthcoming it will affect Sino-American relationships, because the Chinese may feel forced to apply for more help from Russia on her own terms. We do not want the same feeling to develop toward America as has occurred toward England on account of the method of Czechoslovakia's settlement and her apparent willingness to compromise at China's expense in the Sino-Japanese issue.

"As long as England and the United States help both sides, Japan and China, and Russia helps only China, we Chinese are bound to feel more friendly toward Russia." (There is strong feeling in regard to the continued sale of war supplies by the United States to Japan. Chinese cannot understand how Americans, if they are friendly to China, can continue to permit such sales. J.L.B.)

"On December 15th the Kuomintang Party leaders are meeting to discuss further the question of peace possibilities and foreign policy. In January the People's Political Council will meet again. At the last meeting, in November, the attitude was that this is an unfavorable time to consider peace terms."

Chengtu, December 2nd, 1938

To Secretary Morgenthau

From J. Lossing Buck

INCOME TAX

When in Lanchow I talked with Mr. Wu, who has charge of income tax collection for the provinces of Kansu, Ninghsia, and Tsinghai. The collections from these three provinces are exceeding the estimated collection, and since January 1st have amounted to 50,000 yuan. It is expected that the collections next year will amount to 800,000 yuan.

Kunming, Yunnan,

8th December, 1938.

The Honorable

Secretary Henry Morgenthau, Jr.,
Department of Treasury,
Washington, D.C.

Dear Mr. Secretary,

I attach a copy of a message sent you by Dr. Buck, through
Mr. Campbell, on December 2nd, 1938.

Respectfully,

Enid Saunders

Enid Saunders
Secretary to Dr. Buck

Chengtou, December 2nd, 1938

To Secretary Morgenthau

From J. Lossing Buck

COPY OF MESSAGE SENT THROUGH CAMPBELL

Several of my Lanchow reports have been delayed in the mails. One important general predicted a Japanese attack on communications west of Lanchow via Mongolia or Ninghsia, and believes it can be successful, although he declares a more vital blow to China would be a successful attack on Tungkwan and thence to Hangchung in Southern Shensi. Japanese test of Tungkwan defences have found Chinese defences strong and situation there is still favorable to Chinese. Chinese fear Japanese attack will be greatly assisted if Yellow River freezes. Szechuen loyal and Governor expresses confidence of Szechuen defences, although more foreign assistance war supplies urgently needed. Governor expresses thanks for all American help to date, but states hope that still further assistance possible.

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 TREASURY DEPARTMENT

PARTIAL PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Berlin, Germany

(part air)

DATE: December 8, 1938, 3 p.m.

NO.: 704

No. 37 FOR TREASURY FROM HEATH.

The concern of the Reich Government over the export and foreign exchange situation has recently become more acute as evidenced by the export conference presided over by Funk the first of this month and the latter's announcement that export orders must have primacy. The Economics Ministry has been trying not to increase export subsidies but recently reports of several cases of increased bounties were received as well as cases where Hamburg exporters have through the intervention of the Ministry of Economics forced reluctant German manufacturers more interested in the profitable internal market to give preferential attention to the manufacture of export goods. While the October foreign trade figures for greater Germany show an increase of imports over the disturbed month of September of 34 million marks to 526 million marks and an increase of exports of 48 million marks to 490 million marks there is still a trade deficit of 36 million marks which, however, is less than the 51 million excess of imports in September and the 84 million excess in August. For the first ten months imports of greater Germany totaled 4,983 million marks and exports 4,637 million marks leaving a trade deficit of 356 million marks as compared with a surplus

- 3 -

of exports from Germany amounting to 362 million for the first ten months of 1937.

Statistics of gold imports and exports are available only for old Germany. During the first seven months of the year, despite the trade deficit, there were net gold imports of 94.5 million marks lending support to an authoritative statement to me that German trade statistics tended to over-value imports. In August there were net exports of gold of 13.5 million, in September of 91 million, and in October 41 million marks. These shipments have had little reflection in the published gold reserves of the Reich. The Reichsbank's disclosed reserve has remained constant around 70 million. The Gold Discount Bank's October statement, however, showed a decrease in its gold stock from 47 million to 40 million marks.

The Reich's debt statement for October shows an increase of 1,849 million marks ^{during the month} ~~(omission)~~ to a total of 25,076 million marks. The increase was entirely due to the issue of long term bonds. There was a net decrease of 45 million marks in the disclosed short term debt due to the maturity of three and six months treasury bills. The controlled financial press had predicted there would be a substantial decrease of short term debt during October and to the extent of 45 million marks, this was achieved.

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- 3 -

The undisclosed debt consisting mainly of "special bills" is of course not included in the debt statement. Re my telegram of July 9, 11 a.m.: the British Financial Attache is still of the opinion that this unrecorded debt runs from 18 to 20 billion marks. He believes that about 6 billion marks of this is held by industry, and about 12 by the banks. He believes, too, that the net aggregate bill holdings of the Reichsbank, the Gold Discount Bank and all private banks which on the thirty-first of October amounted to 15,275 billion marks - not including single bills of the Gold Discount Bank - are made up of commercial bills only to the extent of 2 1/2 to 3 billion marks, and that indefinitely renewable Government "special bills" make up the balance of this total. A few months ago it was stated in the Financial Press that private banks had in their portfolios no more "special bills", but there is good evidence that such is not the case. For the past two or three months, it is known, German industry has been becoming ~~more~~ progressively less liquid and the banks have been taking up its holdings of "special bills". It is also known that it is the tendency of the Reichsbank to pass on "special bills" which it has accepted for discount to the private banks. So far it has not been possible for me to get any reliable estimate as to what
part

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part of the bill holdings of banks is composed of "special bills" and what part is commercial paper. During the year 19²⁸(~~emission~~) - a period corresponding in activity with the present period - commercial bill holdings of German private banks were about 4 billion marks; those of the Reichsbank were about 2 billion. Because Government orders make up a greater part of the present economic activity, it is to be assumed that there has been a decrease in the proportion and amount of commercial paper, but that it is down to 2 1/2 or 3 billion seems doubtful.

During the first seven months of the fiscal year which began April 1 there has been a net increase in the Reichs debt of 6,578 million marks. With the last loan of 1500 million (payments for which do not begin until January) Government borrowing for the current fiscal period will presumably be in excess of 8 billion marks unless important economies should be effected which no one in the Government with whom I have talked expects. Semi-official forecasts are for tax and miscellaneous revenues of 17 billion marks making a total Central Government budget of 24 billion marks or a third of the national income. The Government's borrowing of a billion marks compares with estimated money capital formation of 7 billion marks during the calendar year 1937. Money savings during 1938 will doubtless show an increase over 1937 but industry has been relatively "starved" in favor

- 5 -

favor of Government borrowing notably the Reichsbahn has had to put off orders for new rolling stock. For the first nine months of 1938 only five private industrial bond issues totalling 158 million were permitted as compared with private bond issues of 307 million in 1937. To be sure share issues total 698 million marks for the first ten months of 1938 (1937, 333 million marks) but more than half of this was for the Reich owned Hermann Goering works. The Government seems able to borrow without difficulty however. Recent issues of Treasury bills bear slightly less discount than those of last summer when certain issues went to 3 5/8. January bills were offered at 3 3/8% and later maturities at 3 7/16 to 3 15/32.

In public and in private Schacht insists that as long as the Government meets its deficits by long term bond issues, inflation is automatically checked. So much confidence is not felt by other observers in the Government. I was told by one well-placed source that while the price stabilization control of the Reich has been remarkably administered, gradual hidden increases are not being prevented. Despite the statistics, he insists, a very slow but merciless decrease in the real wages of the individual workman is taking place, as well as a decrease in the standard of living. Judging from his own contacts
and

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and experience, he does not expect that there will be any real slackening of the "must" orders for ambitious party plans, for the four-year plan, and for the military in order to increase the output of consumption goods. In his opinion the cartelized industry will be able to repulse additional taxation and will be successful in opposing inertia against efforts to lower costs and prices for consumption goods. In his opinion no successful measures will be taken to halt a very gradual inflation and a deterioration of the workman's real wages and standard of living. Unless some unforeseen event takes place, however, he does not think that the grumbling of the working and other classes will break through the present discipline sufficiently to bring about a change in the present program of the Government. Those here who have knowledge and experience of the situation have the general feeling that there is a gradual continuing economic deterioration and strain. However, not many believe that this deterioration and strain or the dissatisfaction evoked by it will have any early decisive outlet or results on the present Government's political or economic organization.

The projects and organization of the party are costly, and such actions as racial persecution have their effects on foreign trade; however, these observers believe that despite these facts, and barring some decisive miracle,

it

- 7 -

it will be possible to maintain the "discipline" of the workers and other sections of the population against a considerable restriction of living standards. They also believe that it should be possible for the highly competent bureaucracy of the Treasury, the Economics Ministry and the Reichsbank to makeshift to keep the economic machine running for a considerable time without actually breaking down, although dislocation and deterioration will be apparent.

END MESSAGE.

GILBERT.

EA:LWW

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: December 8, 1938, 5 p.m.

NO.: 2079

FOR THE TREASURY DEPARTMENT.

Transactions on the exchange market here today were on a moderate scale under erratic and cautious conditions, pending the result of the vote in the Chamber.

We have been told by our market contact that there is no serious doubt that Daladier will be successful. He also says that in financial circles it is apparently believed that he will have between 50 and 100 votes for a majority. Sterling has alternatively been bought and sold by the fund, at rates varying between 177.50 and 177.75. Francs are being offered now at 177.60 by the fund. It is thought that a slight amount of sterling has been gained on balance. Sterling forward rate about 15 centimes for one month; for three months about 50 centimes.

END SECTION ONE.

WILSON.

EA:LWW

PARAPHRASE SECTION TWO, NO. 2079 OF DECEMBER 8, 1938
FROM PARIS

At opening rentes were lower, but they improved later on to about the closing point yesterday.

Today's JOURNAL OFFICIEL published the decision canceling the designation of Jouhaux as a member of the Bank of France's General Council.

Today's Bank of France statement (as of December 1) shows that gold reserves increased by 204,000 francs. The commercial portfolio decreased 1,200,000,000 francs and note circulation increased 2,650,000,000 francs. Deposit and current accounts decreased 2,600,000,000 francs. Gold cover percentage declined from 60.21 to 60.17.

END SECTION TWO.

WILSON.

PARAPHRASE, SECTIONS THREE AND FOUR OF TELEGRAM NO. 2079
OF DECEMBER 8, 1938, FROM PARIS

The press today carries a semi-official statement that Reynaud told the Finance Committee of the Chamber last evening that on December 15 or 16 he would be prepared to open discussion of the 1939 budget. Furthermore, for the month of November the budgetary revenue was 175,000,000 francs over and above estimates, and since the beginning of November 6,000,000,000 francs were repatriated. Reynaud is also reported to have said that Treasury requirements were such that it would not be possible for the Government to envisage a diminution of the yield of measures embodied in the decree laws recently issued.

In today's AGENCE ECONOMIQUE there is a report from its correspondent in Amsterdam that next week there will be a meeting of officials of Mendelssohn and Company and other Amsterdam banks for the purpose of undertaking a conversion operation of the 7 percent Moroccan Railway loan into a thirty-year loan at 5 percent. The new loan would be issued at 98.

END MESSAGE.

WILSON.

EA:LWW

145
December 8, 1938.
4:48 p.m.

HMJr: Hello.

John
Hanes: Hello.

HMJr: Johnny?

H: Yes, sir.

HMJr: Am I making a record of this?

H: Wait just a minute -- yes, O.K., Henry.

HMJr: Who's with you?

H: Nobody now.

HMJr: All right. Well, I wanted to tell you this -- the President just called me.

H: Yes?

HMJr: And he said that a "little birdie" told him that if I would see young Giannini to talk with him, that everything would be all right. So I said, "Well, Mr. President, let me tell you what the present situation is." I said I just got through talking to Johnny Hanes who had a meeting at the Comptroller's office at which I believe Eccles and Jones were present. Am I right?

H: Mr. Eccles was not there - Mr. Jones and Mr. Crowley were there.

HMJr: But not Eccles?

H: No.

HMJr: And I said they got along beautifully, and I said that -- that on everything except the question of putting in new capital, but I said they are going to meet again tomorrow and they are making excellent progress. I said, furthermore that my understanding of Preston Delano is that he is keeping me as an ace in the hole, and that he is only going to come to me after they come to an agreement, and that if and when they do make such an agreement, I'll walk across the street, if I can still walk, and see you.

H: Yes.

HMJr: And I said with this plan working, I said, don't you think it would be a mistake for me to see Giannini? He said

"Oh, absolutely!" He said what information I had was brought to me last night.

H: Yes.

HMJr: So he said, "That's simply fine." So I wanted to give it to you, and having nobody to dictate to, I wanted to make a record of it, you see?

H: Sure.

HMJr: And I wanted to let you know so that you know that just -- so when you carry the ball, and if the coach is giving me some signals from off the benches, I want you to know what they are.

H: Yes, sir. Well, I'm glad to get that. That may explain in some way the attitude that I reported to you earlier -- you know, the friendly attitude that was taken there this morning -- that may explain it, don't you think?

HMJr: I don't know. What I imagine is -- I should imagine -- was that Jesse saw the President.

H: Yes.

HMJr: Why wasn't Eccles there today?

H: Well, I don't know why he wasn't there. Well, now wait a minute -- wouldn't that be -- wouldn't it be natural that Eccles would not come to this thing since he might be drawn into later as -- later as a judge in the case? Wouldn't it be out of place for him to come?

HMJr: Well, if I might make this suggestion -- I think it would be better to invite him and let him turn it down, but you can think that over, so that he can't again say the way he said in the case of Douglas, that he didn't know anything about it.

H: Well -- well, we've got a record of that I think that covers that point alright -- because Preston showed me a letter that he had from Marriner this morning --

HMJr: Yes.

H: In which all these points were taken up and I think that covers it. However, I'll go down to Preston's office and look it up right now and see that -- that -- and if it doesn't cover it, and I think you are right, we should at least notify him that we are carrying on.

HMJr: And does he want to come?

H: And does he want to come. All right.

HMJr: Or does he want to send his chief bank examiner?

H: All right.

HMJr: Folger.

H: All right.

HMJr: Now the only other thing - the President said, "How are you getting along on the Anglo California" -- so I said that we -- that you took the letter over and spent a couple of hours with Jesse, the result of which was that he wrote me a letter including the paragraph that the bank management would be satisfactory to us.

H: Yes.

HMJr: And he said, "Well, that's really fine," he said, "You had better knock wood you seem to be getting along so well."

H: Yes.

HMJr: And he was very jolly -- and, -- and, very much pleased.

H: Good!

HMJr: But I wanted to get that to you so that you -- to let you know that's just the way I'd play it, that's all.

H: Yes, sir. Well, now do you feel like spending five minutes with me if I come to see you?

HMJr: Well -- well, I'm not -- what time would it be?

H: I was just going on by to say "hello" to you and just drop -- just drop this Chinese thing.

HMJr: Well -- I'm -- I'm not --

H: You're not up to it?

HMJr: I tell you -- I really would -- I'd love to see you, but if I stay home tomorrow, I'd like to ask you to come.

H: Right! Well, I was only coming if you wanted me now, and -- because I just didn't want to -- if you wanted to talk all right, if you didn't, I didn't have a thing in the world on my mind. I told you everything that is going on.

HMJR: Well, that's darn nice. I'm -- I'm -- I'm so uncomfortable.

H: Yes.

HMJR: So that --

H: Well, let's -- I won't come, and we'll -- if you want me for anything why you know how to get me.

HMJR: If I'm home -- ah -- I have to stay home tomorrow, then I'll ask you if you would come up.

H: I'd be delighted.

HMJR: Are you home tonight.

H: Yes sir. I'll be at home tonight. I'm having dinner with Douglas tonight at home on a situation, so -- I hope he's coming. I'm not sure yet.

HMJR: I appreciate it, but I think I'll postpone it until tomorrow.

H: O.K. Fine, and if you want me you can get me.

HMJR: And you've got this thing of the President which doesn't change it, other than it just means that somebody has been talking to him and my guess would be that it was

H: Alright.

HMJR: And it's alright.

H: Yes, don't you think so?

HMJR: Don't you think so?

H: Yes -- yes, I don't see anything wrong -- I don't -- of course I haven't had time much to think about this -- I don't know if it is he. I don't think it was he.

HMJR: You don't think it was?

H: I don't believe it was. He was with me all night last night.

HMJR: And did he say --

H: No -- no, he didn't say -- he didn't mention anything about it to me all evening.

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HMJr: How was he, anyway? Well, you can tell me about it when I see you.

H: Alright -- I'll tell you the whole conversation when I see you.

HMJr: Alright.

H: It is interesting.

HMJr: He -- He -- how shall I put it? He's no less friendly towards the Treasury.

H: No -- no -- it couldn't be better.

HMJr: I called him up to try to get him to have lunch with me today -- that was yesterday.

H: He -- he told me that you did, and he said that he was sorry that he had another engagement. He wanted to see you.

HMJr: It turned out I couldn't have seen him anyway.

H: Yes.

HMJr: But he is no less friendly?

H: Not a bit in the world. No. No. He is in good shape, I think.

HMJr: Well, Johnny, if I'm home tomorrow, I'll see you.

H: O.K. Fine.

HMJr: Good night.

H: Good night, and thank you.

TREASURY DEPARTMENT

Washington

FOR IMMEDIATE RELEASE,
Friday, December 9, 1965.

Press Service
No. 15-65

Secretary of the Treasury Morgenthau today announced the subscription figures and the bases of allotment for the cash offering of 2-3/4 percent Treasury Bonds of 1960-65 and of 1-1/8 percent Treasury Notes of Series B-1943.

Reports received from the Federal Reserve banks show that cash subscriptions for the offering of Treasury bonds aggregate \$5,732,000,000 and for the offering of Treasury notes aggregate \$3,646,000,000. Subscriptions for the bonds were allotted 7 percent, and subscriptions for the notes were allotted 9 percent. No preferred allotment was given, and subscriptions for both issues were allotted on a straight percentage basis, with adjustments, where necessary, to the \$100 denomination.

Further details as to subscriptions and allotments will be announced when final reports are received from the Federal Reserve banks.

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RE FEDERAL BUDGET AND RECOVERY
(Meeting at 2211 30th Street)

December 9, 1938.
5:15 p.m.

Present: Mr. Hanes
Mr. Taylor
Mr. Bell
Mr. White
Mr. Stewart
Mr. Williams
Mr. Viner
Mr. Currie

H.M.Jr: Well

Stewart: Here we are.

H.M.Jr: Are you fellows "learnt"?

Stewart: We've been doing our best to learn.

H.M.Jr: Uh-huh.

Bell: Burnt.

H.M.Jr: Learnt.

Bell: Burnt.

H.M.Jr: No - learnt.

Stewart: We've had a full day seminar.

H.M.Jr: Did you? Well, it's terribly nice of you to give it all the time; but it is awfully important if it's right, and it's more important if it's wrong.

White: It's very much more important.

H.M.Jr: Well, which one of you gentlemen wants to

White: I can just probably start it off; then they can speak for themselves individually; because we didn't have a great deal of time to sum up the views.

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We started with an agenda and moved through it, discussing questions of what the national income would be and what the budget might be, and then went on to the specific problems that you were interested in. And I think it's the feeling of the men who were there that that approach as a method of either determining what changes to make in the budget or as a method of presentation is quite unsatisfactory, and that there wasn't enough time to see whether any positive contributions might be made either in the direction of suggesting specific changes in the budget or specific measures outside the budget; that would be a matter for subsequent discussion.

Now, with that very preliminary cursory observation, I think they each ought to speak for themselves, express their own views on the subject.

H.M.Jr: Shall we go around the way you're sitting? Jake?

Where's Professor Hansen?

White: Well, Professor Hansen wasn't able to attend all day. He started in, had a half hour; then he sent word through John Williams that something very important to him had come up in the Social Security Board and he couldn't get away today.

H.M.Jr: Fine.

Williams: Some question that he was expected to declare himself on today.

H.M.Jr: I see.

Williams: He had agreed to come down for that.

H.M.Jr: Jake?

Viner: Why, what I got that was positive is the desirability of studying both the revenue and the expenditure aspects of the budget to see whether you can select certain items and say those items would be - are most - let's say on the revenue side, are most hurtful to business recovery, and those that are

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less; and that if you can make any shifts, the shifts should be from the former to the latter. Similarly in the expenditures, that some could be selected as more stimulative to business recovery and others as less, and that the expenditures should be shifted as far as possible in the direction of the former and away from the latter, in so far as other considerations don't stand in the way.

On the method of presentation there, aside from the logic still, mere mode of presentation, I feel myself that you mustn't use any figure unless you are prepared or have somebody else prepared to explain in pretty specific terms just how you reasoned it; that you can't defend a budget in terms of

Bell: Talking about the multiplier now.

Viner: Yes.

White: Several possibilities; not only the multiplier....

Viner: ... but the percentage of expenditures which get into consumption. If they ask you the question "How do you get that figure?" you must be able to answer it; if you can't answer it, you mustn't use the figure.

If you could come to a pretty definite consensus on the arranging of the items, it might be worthwhile to put them in an order - say, A, B, C, D, E - not use any ratios, but put them in an order of desirability, which is just another way of saying you're going to compare the merits of the various items, say "this is more or less bad than that." I wouldn't go any farther than that; I mean as far as figures are concerned, in order of rank is as far as I'd go, and I'm not sure that you can safely go that far.

H.S., Jr: May I ask you a question? Is it true... - or maybe I could either - need to ask either White or Currie - ... that those multipliers were arrived at by figuring the things backwards?

White: I suspect that those multipliers were arrived at by

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merely a preliminary estimate on the basis of what Jake has just said: saying that "these are high, these are low, and these are about medium"; and then there have been some studies and a lot of writing with respect to the rank of multipliers done in theoretical work, and that he had some familiarity with that work....

H.M.Jr: Pardon me - who is "he"?

White: Sanford, whatever his name is, at the New York Bank.

... and that he said, "This is the high multiplier; we'll use the figure $3\frac{1}{2}$. This is a low multiplier; we'll use a figure of 1. This is somewhere in between; we'll use 2 or $2\frac{1}{2}$."

I suspect that that was the way it was arrived at.

Williams: I think we ought to say, as long as Sanford's name has been mentioned, that he was pulled in on this job.

White: I don't know anything about his merit.

Williams: He has no conviction about it. He was asked to do it.

H.M.Jr: Mr. Vice President, it's no reflection on your bank.

Williams: I wanted to make the point clear.

H.M.Jr: Even though I'm a little wrong here, a little wrong there, I've still got my sense of humor.

White: I still - John, I didn't say the Bank of New York.

Williams: Nor even Sanford.

H.M.Jr: Just the reason I raised the question at this time - in discussing this with some Treasury people, the only way they could arrive at it is that they had the expenditures and they had the collections and they had the national debt figure and they just worked it backwards and arrived at the multipliers and then arranged them accordingly. I wondered whether that was what

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- White: I don't think that was done. Oh no, what they did was not a substantial violation of the logic. I think you probably would find agreement here that the range of what they were driving at - what they called the multiplier - was about two and less than four, whatever you call it; and that there would be some order of high, low, and middle. And once having granted that you would get variations and that the variations, the relative movements, would not be greatly different, so with different points of view you might get one way or the other. But I don't think they attempted to fix up the multiplier in order to make the end result come out, because it wasn't necessary and they wouldn't have gotten anywhere substantially even if they tried to do it.
- H.A.Jr: Shall I go on to Professor Williams?
- Viner: I'm through.
- Williams: Well, I thought he had done a good job in arranging these multipliers, though I agree he did it in this general way: The range is in here somewhere, and here's a tax that affects consumption a good deal and here's one that probably affects it very little. Well, you get your extreme, then you fit them in the best way you can. But I don't feel that you can do much with that approach. That is, we all know, we knew before, that taxes have a certain impact; some bear on consumption, some on investment, some on savings. Similarly with expenditures. I don't feel that we know any more about it now than we did before, and that the real problem is just about where it was before, and I should think we'd have to go at it in other ways than this one.
- H.A.Jr: You wouldn't go as far as Viner: that we could, for instance, arrange them in their order of - let's say, A, B, C.
- Williams: I think it would be very desirable to arrange them in this order internally, that is, to say, within the Treasury, and to give thought to it and perhaps change the order as you got more light. But I should think it would be very undesirable to publish any such list. I think we're not sure enough of our ground to do that.

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- H.A.Jr: Well, do you feel that there is, for instance, a difference as one is to three between some kinds of taxes? Is there that much difference?
- Williams: I think probably so. I can't see it clearly, talking in terms of one and three; I prefer to say that some taxes have a very great effect on consumption, others have very little effect. I don't know what the figures are; I don't believe anybody does.
- Taylor: Might even be more.
- Williams: Might even be more.
- Taylor: Yes.
- H.A.Jr: Stewart?
- Stewart: I think the question partly is whether or not this is a promising approach to a problem, with enough promise so that in the near future it's going to have practical value. I should doubt whether you'd be able to agree among yourselves as to the order of the incidence of each item.
- Part of the idea is a very simple idea. We have always known that taxation of various kinds has had varying effects on consumption, and so forth, but when you get to determining the precise amount, undertake to assign a figure, I don't think we know enough or anybody knows enough at the present time to do any such thing at all. It struck me, as I said at the meeting, as just assigning numbers rather than giving any sort of statistical figure for it.
- So it doesn't strike me really as a promising line of inquiry for any practical effect.
- H.A.Jr: Not enough for the present to philosophize about it.
- Stewart: It's in the field of abstract ideas. Then the question is whether or not in the field of abstract ideas, and in the hope you'll get more figures in more time, it's worth while working at. That's a separate question.
- Viner: Do you mean by that, Stewart, that you wouldn't say as between two taxes, that in a given stage of a

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business cycle, one was a more preferable form than another in its effects on the economy?

- Stewart: question of ranking the whole group is what we were talking about; and even as between one and another, I think it would be awfully difficult to do.
- Williams: The extremes are pretty easy.
- Currie: Actually I think all that's necessary - there's only a few things which offer a possibility of change, and there your investigation could be concentrated.
- Williams: Having in mind, too, the administrative difficulties; it is very difficult to treat these things flexibly, it seems to me, especially on the revenue side. If you know your extremes, know a few instances where you are fairly sure of your ground, that may be very useful in thinking about the problem and preparing tax measures or passing upon new tax proposals. It might be useful. But as for setting it up as a general framework of attack on the problem, particularly publicly - that would seem to be a very great mistake, to me.
- H.M.Jr: Well, I'm going to be terribly frank, the way I always am when you people come down to advise me. As Secretary of the Treasury, not as chairman of this other committee, I just want to ask Currie and White: supposing I decide that this thing is not practical and I don't want to recommend it; what are the chances, do you think, that they'll go around me anyway and get it to the President?
- White: No, no, not one chance in a thousand.
- H.M.Jr: Are you sure?
- White: Positively.
- Currie: I know that Chairman Eccles has grave reservations along the lines that have been expressed.
- H.M.Jr: Really?
- White: And there were in the Industrial Committee. You see, what we did, Mr. Secretary, was try two other approaches which were less undesirable, let's put it,

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then that original one, and seeing whether we could save out of that some concept which would enable a presentation possibly in the forms of high, low, and middle, or more or less of each desirable, or in some rough quantitative forms of the other. But I know that the criticisms and suggestions which they had to make will be given consideration, so that if there is conviction that the thing doesn't work there, I would say there isn't a chance in the world that they'll go around. But there are certain other aspects of it that possibly present two points of view that go to little more fundamental issues about which there will have to be further discussion. But none of it will emerge until that's discussed with you. I'm positive of that. Wouldn't you (Currie) say that?

Currie: Oh yes.

White: Nothing I could be more positive of, because there would be just hell to pay; because we know how the technical men feel about this thing.

Currie: Yes.

H.M.Jr: Well, you people - how shall I say - who are presenting the evidence, so to speak

Currie: As you know, I had no responsibility for this method of approach, and I felt just as Mr. Viner has put it, that it's perfectly valid as a qualitative matter. We all have, I think, a firm conviction that certain types of taxes are more repressive than others and that certain types of expenditures are more expansive than others. But when you start to apply a definite figure to any individual tax receipt or tax expenditure, then I think you expose yourself to attacks on that definite figure - "How did you arrive at it?" It might be this; it might be that. We're not in a position statistically, in quantitative terms, to defend that figure. I'll maintain that practically all W.P.A. figures will stimulate consumption - very stimulating. But if you'd have to put a percentage - very difficult.

H.M.Jr: Well, may I just keep on the tax and revenue thing

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thing for a minute. I'm not digressing, but I'm coming over now into - you know, I can't emphasize how confidential this is, but here's the thing that's placing Bell, Hanes and myself - this is the thing. We've really got only from now until Monday night. I see it's out in the paper now that the President is going to see the leaders, the Vice President and the rest of them, the 17th; so between now and the 17th, he's saying to us, "Well, if you've got something, give it to us." I don't know whether he said that to you (Bell), but he said it to me. So I stalled him until Monday afternoon so I could get you people down to look at this thing.

Now roughly - Dan, you bring me up to date - the next budget that we're working on, without the additional things, planes, anything over and above, just the way we stand tonight - the expenditure's around nine billion, isn't it?

- Bell: Yes, that's right; they're under nine billion, they're high in the eights.
- Hanes: Eight six.
- H.M.Jr: What?
- Hanes: About eight six.
- H.M.Jr: How much?
- Bell: That much if you consider about a billion and a half for WPA.
- H.M.Jr: There you are. You're getting the very inside. Billion and a half for relief brings it up to eight six. Nothing in there for planes.
- Bell: Nothing for the new program. The old plane program is in there.
- H.M.Jr: And if you put in the new plane program, it might be 500 million to a billion.
- Bell: That's what they're talking about. I don't think they can spend that much money.

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- H.M.Jr: Anyway, it's between 500 million and a billion. So the program on the expenditure side is roughly eight six ...
- Bell: ... without - yes.
- H.M.Jr: Without the extra planes. And the other thing might be 500 million to a billion. But I haven't talked to the President in two weeks, so I don't know where he is after two weeks. I don't know whether you (Bell) have.
- Bell: No, I haven't. I don't think he knows. He's waiting for a definite program from the War Department.
- H.M.Jr: From the War Department.
- Bell: That's right.
- H.M.Jr: And if the present tax base is not changed and if business - George Baas says the national income for the next calendar year will be about the same as it is this year; quoting Currie and his people, they think it will be about five billion more, or around 68 billion. Right?
- Currie: 68 as compared to 62 this year.
- H.M.Jr: And George says it will be
- Currie: Income paid out will be the same.
- H.M.Jr: If it stays at 62, then, as I say, we take in about five billion dollars next year.
- Bell: Roughly, yes.
- H.M.Jr: And if he's (Currie) right, we'll take in about five and a half billion.
- Hanes: Nearer six.
- Bell: Really?
- Hanes: I think so.
- H.M.Jr: Well, let's split the difference and say that our income for next year - and that's only for six months of it - is five and a half billion; let's be

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on the conservative side. And let's say that we're going to spend 500 million for planes. Let's say it's going to be nine billion dollars, see? So the deficit is a difference between five and a half and nine, or ...

Bell: Three and a half.

H.M.Jr: Three and a half. Right?

Bell: Right.

H.M.Jr: And it might be even more - four. And the deficit - it looks to us like a deficit of between three and four billion.

Viner: Is that eight six figured on the basis of appropriations or on the basis of expectations, or on - as to what they'll actually spend?

Bell: That's an expenditure figure, but it's very rough, because we haven't had the final figures, in any case. But I can't see any material difference between next year and this year, including WPA.

Viner: What's it going to be this year?

Bell: Be around eight nine.

Viner: Eight nine.

Bell: Probably a little higher because of the additional requirements for WPA, but not much over nine.

Viner: And the revenues?

Bell: Revenues were last estimated at five billion. That hasn't been changed.

H.M.Jr: Am I right that it will be between three and four billion?

Bell: I think that's a conservative estimate.

Hanes: I didn't hear the first part of it.

H.M.Jr: I said the deficit, as of tonight - between three and four billion.

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Hanes: Yes.

Bell: That's right.

H.M.Jr: Somewhere, depending on where the national income goes and how much extra for the planes, between three and four billion.

Taylor: In terms of a net contribution, would it be that, or is that an accounting job?

Bell: That's the budget deficit.

H.M.Jr: Now here's the thing: what can we do about it? See? I mean that's our problem.

White: Mr. Secretary, most of the discussion, practically all of it, relates to - their opinion is pertinent merely to that form of presentation on these other issues; as to what can be done on the outer budget, investments, and so forth, ...

H.M.Jr: I know.

White: ... they didn't have much time.

H.M.Jr: I know, but as long as they're here I'm going to give them the works. I mean there's no use having part of the picture. They might just as well have the whole picture and get part of my headache.

and the reason for the - now, one of the suggestions was made, and that comes back to this thing. And the President liked it, and he's in that mood. I have never seen him in the mood where he really is more anxious for constructive suggestions than he is now. I mean he's hungry for some of us to tell him what to do. And he's very anxious to keep the budget deficit down to at least - what did he say, a billion and a half or two? Two, wasn't it?

Bell: No, he was talking first about the two and a half billion figure that we took him.

H.M.Jr: Then he wanted to cut.

Bell: He wanted to try not to increase it beyond that,

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find some way of financing the additional expenditures that would increase that deficit.

H.A.Jr: Now, the simplest way is the suggestion - after all - was that if you take the present War Department and Navy Department budget, it comes to approximately a billion one.

Bell: That's right.

H.A.Jr: And then you add as much more as he decides and Congress decides for the planes. I mean it can be - whatever it is - but - and the thought that we went to him with - and that comes back to this thing, you see - was the possibility of a national defense tax, with some kind of a stamp - battleships, airplanes - so everybody knew, whatever the thing was, that was it. Of course, the easiest thing you think of is a sales tax, and we got some figures out on from one to five percent on the sales tax; a one percent tax produced \$308,000,000.

Bell: 277, wasn't it?

Hanes: Well, it was about - you've got to figure that out a little differently than we did before, because it depends so much on whether you cancel the present excise taxes, which yield about \$380,000,000 a year.

H.A.Jr: That's the figure I had in mind.

Hanes: The present excise taxes, which are sales taxes, yield about \$380,000,000. Well, if you're going to - of course, this wouldn't be done, because certain of those excises would not be changed; for instance, your tax on tobacco would certainly not be reduced. Therefore, you've got to eliminate the tobacco taxes, for instance, which yield about \$400,000,000. But leave that out. That'll make a big hole in your 380 million.

H.A.Jr: But new?

Hanes: The new taxes would yield about \$230,000,000 per cent.

H.A.Jr: Per cent. That's the easiest, and that's why I'm coming back to this multiplier business. A person could very easily raise another billion dollars with

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a five-cent

Bell: Four-cent

H.M.Jr: ... four-cent sales tax. Now, in recommending that - let's say that the Treasury and I decided to recommend that, and are we recommending something which is more deflationary than any other tax, you see? I mean that's - and if that's correct and there isn't - I'm convinced that there is very little chance of cutting down on the expenditure side - what other form of taxation can we suggest to keep this deficit within reasonable bounds? And that's, Harry, you see

White: That's the problem.

H.M.Jr: That's why I figured - I mean you people are too valuable to me to give you just a piece of the picture. I've never done that. I've always given it to you all. You've always kept the confidence. Therefore, I want you to have the whole picture. I think in five minutes I've given it to you. If I haven't given it to you, question me. But there's the picture.

The easiest thing is the sales tax. Now, for the first time since Roosevelt's been President, he didn't throw us out of the office when we suggested the sales tax. He liked it, and I think he'd take it. But, on the other hand, you people may say, "Now wait a minute, that's falling too hard on the consumer classes, and that isn't - something else." But there you are. Should we go, can we go through another year with a three to four billion dollar deficit, or should we make the extraordinary effort to cut down, or should we try to do it through revenue? Now, there's the picture.

And I don't expect you to give me an answer like that. But I'd be more than pleased to have you cross-examine me and Hanes and Bell. Have I stated it about right?

Bell: That's about right.

H.M.Jr: Dan?

- Bell: That's all right.
- H.A.Jr: Anything happened since to change it?
- Bell: No.
- H.A.Jr: John?
- Hanes: No, that's about the story.
- H.A.Jr: Well, there you are.
- Stewart: You estimate that from a four percent sales tax you might get a billion dollar yield, is that it?
- Bell: On Mr. Hanes' estimate, 230 million at one percent, you get about 920 million, somewhere between 900 million and a billion dollars.
- White: Mr. Secretary, without their acceptance of any such concept as an exact multiplier, they still might agree or might not - at least it's a basis for discussion - that the effect on the income stream and on consumption and on business of attacks of that kind might be much worse than some other place, and that the net effect on the addition to this, that or the other thing So the mere fact they've discarded this approach doesn't mean that the underlying concept doesn't play a role in their determination and decision as to whether this is a good or bad thing.
- H.A.Jr: I said that. That's why I'm raising it. I say the only one that we've been able to think of, where you can get it fast and get it, is this one. But as I say, in view of what we've done and what I've listened to, maybe this would be the worst tax I could suggest.
- Viner: I'd certainly say the rapidity with which you could collect it is a disadvantage rather than an advantage, because the offsetting expenditures will be delayed, and on past precedent they will be delayed even beyond the program.
- White: Not only that, but even if they were not delayed, there may still be added to the income stream less than what you take out.

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- Viner: That's another question. I'm talking now about the rapidity of the tax itself. I'd say on that ground alone, if you were going to finance it by a sales tax, I might enact it but I would delay it for perhaps six months after you thought the expenditures were booked really to start.
- Bell: You mean they'd be delayed beyond the time when the particular expenditures took place for which they were levied.
- Viner: Well, I'd certainly delay it until not earlier than the time at which the expenditures would actually take place in the form of disbursements to the public.
- Bell: You mean for the national defense program.
- Viner: Yes.
- Williams: How would Congress receive the suggestion about a sales tax?
- H.M.Jr: Well, I can only tell you what I think. I think I'm correct in this, and you better go back - a little bit of history. I think that Jack Garner has always been for this when he was Chairman of the Ways and Means. I think he always was a sales tax man.
- Bell: I really don't know. I would have said the other way.
- H.M.Jr: I think that's right.
- Gaston: I think he proposed it once and then withdrew it.
- H.M.Jr: Well, my impression is that he is a sales tax man.
- But I'm just bringing this up, having that chart in mind. The sales tax, under that, would have a very high multiplier. And is it the worst kind of suggestion? And here you've got this thing and we're right up against the gun. And I don't blame myself and my associates for this, because as I told publicly the press conference, we've just been sitting here waiting until the President told us what the figures

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are, and we don't know. And you might say, "Well, why the hell call us down on Friday to give you an answer Monday," when the answer is that, without breaking any confidence, Danny was over this week on the War Department thing

Bell: Yes, sir.

H.M.Jr: ... and you don't know what the answer is tonight, do you?

Bell: No, sir, not on the new program.

H.M.Jr: I mean, so there you are.

Williams: My feeling is it would be a bad tax under these conditions, when we are still hoping for a real recovery and where it looks as though the national income wouldn't be much above what it is now next year; to throw a thing like that in would be putting something on the wrong side, I think.

H.M.Jr: You do?

Viner: I would say that I'd find a little difficulty in finding a worse tax under these circumstances. I think I could find a worse one.

Taylor: Well, how would you compare that in effect - I mean this is just guessing - with a tax on bank deposits?

Viner: You mean on idle ones?

Taylor: Well, don't care whether they're idle or not; it's the same kind of a thing. I mean you can

Viner: Also on Government money.

Taylor: Yes.

White: Have to do a lot of other things. Have to put it on short-term bills.

Taylor: I wasn't advocating it.

White: You'd be able to sell short-term bills for a hundred and whatever the tax was.

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- Viner: Keynes came in with - that was his solution, in the middle of 1934.
- Waite: Fellow worked - this fellow Danberg in a book last year took all the ramifications of it.
- Williams: He's an old student of ours in Cambridge; I don't know whether you remember him.
- Hanes: What's the experience in Canada with the sales tax?
- Viner: Their sales tax is now eight percent, which is a huge sales tax - eight percent on manufactured sale prices. But they tried to adjust it so there shouldn't be pyramiding, but there is some pyramiding. It amounts to 5.2 percent of the value of retail sales in Canada. And there are a lot of exemptions - foodstuffs, groceries, and agricultural implements. Lots of things are exempt for the farmer, and some foodstuffs. But it produces 5.2 percent; an eight percent tax produces 5.2 percent of the total retail sales in Canada.
- Now, a lot of that tax never gets into retail sales. It gets into sales of services. For instance, maintenance of buildings - that shows itself in rent, you see.
- But I don't know how you reached your estimates. Did you base it on retail sales?
- Hanes: These were the estimates that we prepared - were translated into somewhat later terms, because these were only at the time, you remember, back in 1932 ...
- Viner: Oh.
- Hanes: LaGuardia and Bob Doughton fought the battle on the floor of the House and defeated what then looked to be like a program for the sales tax; and the Treasury apparently was called on at that time to make estimates as to what they would produce based on 1931 total sales volume. Now, we took those figures just as they were worked by the Treasury - we didn't rework them, but as they were worked by the Treasury at that time, and translated them into 1935, figuring

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that 1935 was a year comparable with 1938 and 1939. We translated those figures into the volume of '35, and that's the way the figures were arrived at.

Viner: I must say that the Canadian tax - it's eight percent, but it's eleven percent on imported goods. You see, they collect the eight percent plus a special three percent, which you may say is simply additional to the tariff, although they call it a sales tax.

Administratively it works surprisingly smoothly; and the public, because it's a manufacturers' sales tax and is often levied several stages before it reaches the consumer and a long way back - the consumer is scarcely conscious of it. But it is a stiff tax on the lower classes.

And I'd say here that from all the evidence I know our tax system is certainly sufficiently stiff on the poor. I think it is sufficiently stiff on the poor, it is deadening to investment and enterprise on the very rich, and that it's the \$2,500 to \$10,000 income people who are so well off in this country, as compared to almost anywhere in the world; unbelievable they've been left alone as much as they have. I'd say if you're going to tax in terms of equity, there is the untouched tax capacity.

White: There are two alternatives. That was one - not twenty-five to ten, but twenty-five, I think, to a hundred thousand, somewhere in that neighborhood, in which these items, the surtax proposals which they had, would yield approximately \$400,000,000 - the surtax proposal which the Tax Research has gotten up.

Williams: How much?

White: The other alternative was the estate and gift tax, which they hope would be 350 - about 750 between them, those two taxes.

Henes: Estate and gift taxes were higher than that - about 480 million.

White: You mean the proposal - that would mean about eight or nine hundred million on both, which would be pretty substantially - don't know how much the expenditure

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would be. And then that would have several advantages as against the other. In the first place, right along the principles which we were discussing - it would fit that; and that really lies behind in part your own conclusions as to the desirability of the tax.

Then, it would avoid the difficulty you (Viner) suggested, which is a real one: getting the money before you spend it, which would be highly deflationary; whereas, that kind of a tax would probably postpone that particular thing, if it became effective.

Viner: You should do that with any tax. You ought to be careful as to that with any tax. You could do it with the sales tax by enacting a tax now to take effect at a certain future date. I'd say that you ought to watch that you don't collect the revenues before you start the expenditures.

White: Then, a sales tax of that magnitude would have a terrible effect anyway.

Viner: A one percent sales tax, I'd say, isn't worth collecting, doesn't produce enough revenue; it isn't worth collecting.

Williams: Wouldn't the tax measure be under discussion during the winter - wouldn't it - if you were going to do anything about it?

H.J.Jr: I would be surprised if the tax thing would come up much before March. And of course, if I could write it - I've said so; I'd say it again - I don't think the tax bill should be passed until the last piece of expenditure legislation is passed. I think that you should get all the expenditure legislation and keep your Ways and Means Committee back as a club and say, "Now, we're not going to pass any tax legislation until we hear the last appropriation bill is passed."

Dan and I have talked this, haven't we? I mean I think that's the thing to do, and of course to hold it back just as long as possible. But what we have to do for the President in his budget message is to indicate the sources of revenue. We always have, haven't we, Dan?

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- Bell: Well, sometimes we have. But it's required in the Act; the budget and accounting Act requires him to state how the expenditures will be financed.
- Williams: I feel that one of the important things that came out today was - well, first, that there would be no great increase of national income next year; and then, more particularly, that the first quarter would be down. I don't know myself whether that's so or not, but I think that's the opinion here in Washington among the economists. And if that's true, then I think it becomes a very serious question whether any kind of tax increase wouldn't be unfavorably received and might not have a bad effect.
- H.M.Jr: Pardon me - you mean for the first quarter of the next calendar year?
- Williams: Yes. If you could tax idle savings and be sure of doing it, why, I think I would be in favor of it. But I think it is really very difficult to do that without repercussions on sentiment and incentive to investment and all that sort of thing. And if that's the case and if the national income is not going to be much above what it is now, I myself would be inclined to justify another deficit. If it is felt that for military reasons we must increase expenditures, and if as a consequence of that we're to have a deficit of the same general order of magnitude as we have had, I would take that line on it, I think, rather than try to increase the revenue; that's always calculated, I think,
- H.M.Jr: Well, I think - I mean we all agree that the kind of taxes we have and the new taxes to be imposed would have a definite influence on how much recovery we're going to have.
- Williams: I should think so.
- H.M.Jr: And I don't think that this Administration has paid enough attention to that in the past.
- Williams: Uh-huh.
- H.M.Jr: I mean - what? I think they get all....

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- White: That's the basis of discussion: as to whether that can be presented.
- H.M.Jr: Again in this room, I think too much attention has been paid to the social effect and not enough to how much income it will generate or
- Viner: ... suppress.
- H.M.Jr: Suppress. And I don't think we've approached it enough from the standpoint of the net result in terms of national income, and that is - I think maybe out of this chart will come that, and if we could get.... What I'd like to do, gentlemen, is this, and I think I'm right on this. I'm terribly anxious to get the President to talk in terms of national income as an objective. I'm terribly anxious to have him so minded that when anybody brings anything to him he will say, "Wait a minute, will this increase or decrease the national income?" He's never done that before. I think he is receptive to that if we can get him to do that and express that philosophy, if we're sure we're right. I'm pretty sure myself that that's right and that that will be a big step forward. I don't know how you feel.
- Williams: Oh yes.
- H.M.Jr: Now, we've never done that. Just say to anybody that comes with a scheme, "Now wait a minute, gentlemen, when this is through will this add or subtract to the national income?"
- Viner: Put in other words, that's the old issue of recovery versus reform.
- H.M.Jr: Well, all right, let's go that far, Jake.
- Viner: Oh, I'm for it; I always was.
- White: Of course, you used the word "reform" just a moment ago.....
- H.M.Jr: Just a moment; knowing my President
- Viner: I think it's reform....

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- H.M.Jr: Just a minute.and knowing myself, that doesn't mean I'd be for giving up old-age pensions and stuff like that. See what I mean? I mean I think what we've got, that sort of thing, we ought to keep. Don't you?
- Viner: Why, sure. I played some part in their having it. Can't take that away from me, Harry.
- H.M.Jr: So I think there's a big job that we can do, without using multipliers.
- Williams: Yes.
- White: You (Viner) spoke of taxing the poor too much. That's what made me think of that.
- Carrie: I think anything that decreases consumption next year, when your plant is working at a low degree of capacity, will be very deflationary. I think we should avoid every possible way of decreasing consumption. In fact, I think what we have to aim for before we expect really substantial volume of capital investments - that you have to increase consumption sufficiently to more or less utilize the existing plant before you expect to get any substantial volume of new capital investment.
- H.M.Jr: Now, I just - and I know Jake likes to have fun - I don't think it's a question of being against - I don't think you have to weigh recovery and reform.
- Taylor: No, not at all.
- Viner: No. Of course, my position has been all along that if you don't get recovery, you can't get reform.
- H.M.Jr: You can't hold reform unless you get recovery; can't hold what we've got unless we get recovery.
- Viner: I hadn't thought of it from that angle, but there's a lot in that, too.
- H.M.Jr: We can't hold reform unless we get recovery.
- Viner: I think that's probably true.

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White: I take it Jake agrees that the criterion of a tax should not be sociological.

Viner: The things that I thought stood in the way were punishment taxes and punishment activities and threats on alleged reform grounds, and my point was that those things were probably causing more damage to the classes they were supposed to help by retarding recovery than they were certainly bringing benefit in their moral satisfaction or otherwise.

White: Couldn't we pursue Jake's line of thought and possibly come out with something of that sort instead of attempting to give any quantitative figures on it: merely allocate the kind of taxes which we're likely to alter - don't have to go through the whole list, because some we're not going to change anyway - and say they're high, low, or medium, or some other such qualitative terms; and, using that as the sort of a symbol for the effect on the national income of the specific tax under specific conditions which we're envisaging, we can label these taxes as high, low, medium or what not, and their effect on national income.

Viner: On some of them I think you may.

White: This particular tax. We're not concerned with some of them. There's no use talking about the effect of paying interest on the public debt; we're not going to stop paying interest, and we're not going to pay more interest. But we may alter the estate taxes, may alter the excise taxes, and those we can label with some degree of unanimity in qualitative and quantitative terms.

Stewart: I should be doubtful about that as far as I'm concerned, because I don't know enough to know what the shifting and incidence of taxation is - shifting and general incidence of taxation. I'm not confident that we know enough about its bearing on national income.

The criterion of taxation that appeals to me first as a measure of desirability is that - my first ranking is that of simplicity. When you pass from that and say, "How does it bear on different classes

in the community?" I am affected by the advantages that come from not impairing the income of the lower groups in the community; that is not with reference to total national income, it is because I believe in progressive taxation and so on. When I begin to figure out what is the effect as a stimulus on the business community and therefore upon the national income of a flow of consumption and a flow of investment, and the influence upon enterprise, and so on, I'm extremely doubtful in the whole field.

Willis: I agree.

Stewart: I should be most hesitant to arrange this thing in an order which would say, "This is the way in which the national income is going to be affected."

Waite: About that there is a very definite cleavage of opinion, Mr. Secretary. And I think that what I said earlier in the evening about there being no danger of anything being put over on you - that presupposes that there would not be further discussion about this angle and that it would not have your acceptance and approval. I mean about that point and not about the earlier discussion; but about the ability to label a specific tax proposal such as a sales tax as adding or subtracting from the national income stream, I think there is a definite difference of opinion which would have to be trashed out.

Currie: I don't think, Harry, there really is a difference of opinion. I think we'd all agree that a sales tax now would probably be the most repressive type of any tax you'd impose.

Waite: I didn't know.

Currie: and that more taxes in the middle income brackets and the estate taxes would be less repressive.

Viner: On the shifting and incidence, I'd say I'd be perhaps, from the business cycle - the effect on the income stream, I think I'd be more opposed to a sales tax if I thought it weren't shifted to consumers. And I'm opposed to a sales tax, that is, a new sales tax, until the shifting

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process has been solved, because its first impact is to just slice profit margins.

Williams: Isn't this our idea: that we all agree that certain taxes would affect consumption in deflationary ways? We're all agreed on that. And where the question comes in is, what's the effect of taxes on investment and incentive to invest on idle savings, and that whole area. I'd find very much more difficulty

Waite: It was in regard to the first one

Stewart: I doubt whether you're going to raise a billion dollars of additional taxes without some deflationary effect.

Viner: Sure you can't.

Stewart: When you go to that step, then you begin to consider alternatives; when you begin to consider alternatives, then you've got a combination of the human feeling about the lower income classes of the community, combined with the fact that the man who has the larger income is usually the man who functions as an entrepreneur, who hires people, and you affect employment by affecting the incentives of the man to employ somebody. In that field I'm vague. I think Viner is much better prepared to discuss this than I am. The reason I make an exception is, I don't feel sure how these things work out. I think there is always a risk about a scheme that recommends itself on simple grounds and discarding it because it isn't clear - an idea which isn't very clear and which seems to have some disadvantages. I don't say I'm for a sales tax; I'm just not clear, so I don't really want to take a position.

H.M.Jr: You're not either for or against.

Stewart: I just don't want to commit myself.

H.M.Jr: You also don't want to take the position - just a little hint that Williams dropped - whether we should attempt to raise the tax base at all.

Excuse me. I've got a couple doctors here. I'll

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be back in a couple minutes. When I come down I'm going to take an entirely different angle, and I want to talk about expenditures. I want to talk about - excuse me a minute - I want to talk about expenditures.

(Secretary leaves room. Informal discussion in small groups continues for ten or fifteen minutes until Secretary returns)

H.M.Jr: Do you mind - is this a pause?

Viner: It's a pause.

H.M.Jr: Well, the way I see this thing heading up is this:
1. Should we increase the tax base? 2. If so, what kind of taxes? Huh?

Viner: Well, I don't think the basic question has yet been answered as to whether you should increase taxes at all.

H.M.Jr: Has it?

White: No.

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

Viner: Tax base - I thought he meant the income tax base.

Gaston: He means the structure.

H.M.Jr: I say: 1. Should we increase the total amount of taxation - the tax structure? 2. If so, what should we do?

Now I want to talk a minute on the other side. I'm going a little bit out of my field. Bell's got to help me. We haven't talked anything about expenditures. The biggest single item after national defense is agriculture. And the agricultural appropriation is well over a billion dollars. Hanes - I haven't had a chance - he's got the thing; they're all fussing about a processing tax.

But again very much in the room, the one philosophy

that Wallace has had that has stuck to him is that if the manufacturer is protected by a tariff, the farmer should be protected by the same amount, and therefore he's entitled to something to take the place of the tariff; and in addition the city man is being taken care of by a billion and a half for unemployment, which he charges up to the city - the unemployment load, plus the tariff load, and he says the farmer should have his.

well, if you examine that, there is in that field there well over a billion dollars which is going to them, and - it will take me a couple minutes to do this thing - we're finding ourselves rapidly - very, very rapidly getting into a much worse position than the Farm Board ever was, with the technique of always spending more money on top of more money on top of more money to hold the price. We have now got loans on or control ten million bales of cotton. And as one very able farm economist told me the other day - he's a really sincere person - he said, "I'm not sure that all the money and everything that you're doing on cotton isn't simply aggravating the situation, as long as you keep building up the amount of cotton which the Government owns."

I'm not going to try to solve the agricultural problem, but I'm talking in terms of big expenditures. And you talk about getting money, Currie, outside the budget - I mean look at the money that we've got tied up in crops.

Viner: Is that in the budget?

H.S.Jrs Yes.

White: Past budget.

H.S.Jrs But it will take me a couple minutes, if you'll be a little patient with me.

As I say, that's the one thing that Wallace has been consistent on. That's one thing we've averaged one-seventh of the expenditure on, and I'll say in this room I don't think we've gotten - ever gotten our money's worth.

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I think that as we go along and struggle, try to raise two, three, four hundred million dollars more money, we should in that struggle also look at big expenditures - now, we went all through this thing last year - and also weigh them as to their effect on the prices. I'm particularly talking about agriculture, because I'm convinced that the biggest drag on recovery now is commodity prices, and I can't see anything that Agriculture is suggesting which is going to get us out of this situation. And I think - I'm very much afraid that in the next two years we're just going to get deeper and deeper, and it all comes out of the budget, and we're piling up these vast quantities of commodities which are just depressant on the market. I'm talking in terms of recovery, talking in terms of the budget; and I think when we look at this thing we can't just overlook an expenditure of a billion two - what is it?

- Ball: About a billion dollars. Billion two if you include roads.
- H.M.Jr: Well, including roads, a billion two.
- Vinert: You can't include roads.
- H.M.sr: Pardon?
- Vinert: You can't include roads.
- H.M.sr: Let's call it a billion dollars, and put roads where it belongs, as a part of public works.

When the other thing on the expenditure side which I think ought to be weighed - I mean there is certainly - there is nothing which is pressing down more, and we can worry about sterling and everything else, but just as long as we have these huge stocks of commodities, increasing hourly, and all coming out of the budget - I don't know anything which is more deflationary than that. And the great trouble is, again digressing a little bit, that what bothers me the most is that the schemes, which are half-baked, are more and more coming out of Agriculture in order to kind of patch over this situation rather than face this situation just coldly - I mean in a cold-blooded way. I mean they're more - every day I get things from the President which I know come

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from Agriculture, which have nothing to do with agriculture, but are right in my shop, in order to kind of patch over this situation.

Then the other thing which I think on the expenditure side - if we go into five hundred million or a billion more money for national defense, plus all the snips of the Maritime, everything else, I think we've got to make up our minds that we've got to take care of so many unemployed until we get this machine going much faster than it's ever gone before. Until we get up around 150 in the Federal Reserve index, we're not going to do anything, we won't reach a point where we can absorb the employables. At least that's the way I feel. And how much on the expenditure side will national defense do in taking care of the unemployed, and if the President decides to spend, say, two billion dollars for national defense, does he still have to spend a billion and a half on the unemployed? In other words, all I'm suggesting is that we kind of take a look on the expenditure side and just don't say, "Well, that can't be touched," because I don't think that that's correct, particularly when you take a look at agriculture.

And I'd like to see you people - very friendly and don't mind a little punishment - I'd just like to throw that at you, I mean, as well as the other thing.

Stewart: The billion dollars represents the annual expenditure for the accumulation of surplus products?

Taylor: No.

Stewart: What's the billion dollars?

Taylor: That's the total agricultural program. That includes various things.

Bell: That includes the AAA program.

Taylor: Regular expenditures of the Department, and so on.

Stewart: Decreasing production.

H.M. Jr: But it all goes out of the budget.

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- Viner: But doesn't include R.E.A. and doesn't include Farm Credit appropriation.
- Bell: No.
- Viner: Does it include rural relief?
- Bell: Yes, it includes the Farm Security Administration, which is part of the Agriculture Department.
- White: What was that R.E.A.?
- Bell: Rural Electrification Administration. Does not include that. They're spending this year a hundred million dollars. They'll drop a little next year, unless Congress increases it.
- Taylor: I've got a bad thought to give you, Henry. We passed him the other day - and service on the public debt.
- H.M.Jr: We passed?
- Bell: Agriculture.
- Taylor: Caught up. I hate to bring that up, but I mean it's
- H.M.Jr: Doesn't bother me.
- Viner: It seems to me back in '34 and '35 we were figuring the same way, and you were discussing the Department of Agriculture appropriation as the measure of the agricultural expenditures, and there were scattered things outside which brought it up to 30 percent. In other words, there are other things which go to the farmer. Your figure is the Department of Agriculture figure.
- Bell: That's right. There are other expenditures such as the R.E.A.
- Viner: I think there's something to be said for getting them into a gross figure.
- H.M.Jr: I wasn't trying to - I was thinking in terms of expenditures which are deflationary.

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- Currie: I think in those terms, Mr. Secretary, putting aside the questions of justice or equity, that that type of expenditure - probably any reduction in that would be, as far as I'd be concerned, the same as the equivalent reduction in housing expenditure, something like that, from the point of view
- Bell: In other words, that has a high multiplier.
- Currie: That has a high multiplier. I'd say the money that goes to the farmer in benefit payments is almost entirely spent.
- Bell: That's like a WPA expenditure.
- Viner: Well, if the farmer is paying his debts
- White: It's not the same.
- H.M.Jr: Just a minute, I want to ask Currie - I wouldn't argue with you a bit that the check which goes to the farmer to reduce his acreage in cotton - that the actual check that he gets - that that particular check he spends and it will help the stores; but look at the purpose.
- Currie: Well, there again, Mr. Secretary, it seems to me like so many of these problems - the railway problem, farm problem itself - and it must be inevitably a program of patching unless we get up the national income. 75 percent of farm income is derived from dairy, livestock, fruit and vegetables sold to urban workers; we really can't solve the farm problem until we get the urban income up; and apart from that it seems to me we'll just continue to patch.
- Williams: But wouldn't it be better to hand out straight relief to him and avoid - and not give it to the rich farmer, the prosperous farmer?
- Taylor: That's something else again.
- H.M.Jr: I'm talking about the technique.
- White: Jake's point is that some portion of that is used to pay off debts and it's not in the same class with the

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Viner: Don't be too sure.

Taylor: How do you know some of these other boys don't

White: The sharecropper doesn't get any of his check, to speak of.

Viner: Thing may be different now, but the sharecropper was the one fellow that didn't get anything out of it, and he'd be the one fellow that does spend it.

Bell: He gets loans from Farm Security.

Viner: Now. But he got nothing before; he got kicked off his farm.

White: He's getting it now.

Currie: There's some offset in the rural rehabilitation loans; part of that will be recoverable, and I think they're a little different - in a little different class from the benefit payments to the farmers. In my own mind, I'd put them a little ...

Bell: Initially they can be put in that class; eventually they can be put in the WPA class, I think, the greater majority of them.

Currie: I don't know. The collections haven't been bad, have they?

Bell: Well, pretty low.

Currie: Everything's low.

Taylor: While you're on this subject, why, everything that you said about the sales tax applies equally to the processing tax, doesn't it?

Viner: Oh, it is a sales tax.

H.M.Jr: Check and double-check.

Taylor: Well, I would like to emphasize that, because ...

H.M.Jr: You know how I feel about the processing tax. What? You know how I feel about the processing tax.

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- Taylor: Oh, absolutely. But I know John's going to be up against a lot of this processing tax business, and everything that applies to the sales tax applies to that. I mean the complete impact
- Currie: Even more force because of the basic nature of the items taxed, whereas in a sales tax at least you get some luxury expenditures.
- Viner: And as that actual processing tax worked, there was really a terrific lag between the levying of the tax and the disbursement of the benefits to the family - six or nine months, as I remember.
- H.M.Jr: Would you gentlemen be willing to do this for me? For the rest of the time that you're here - I don't want to push you too hard - see, the thing - it divides itself into three things: 1. To go after more taxes. 2. If we do, what kind of taxes? And 3. Is there anything that we can do on the expenditure side? Right? Isn't that the way
- White: 4 - Is there any method of selling any one of those ideas that they can think of?
- H.M.Jr: Or anything else they think of. But that's the problem that we have, isn't it, Dan?
- Bell: That's right.
- H.M.Jr: What?
- Bell: Yes, sir.
- H.M.Jr: And right now I never was harder pressed for an answer. I have no answer.
- White: Did you give some indication of what you thought the military expenditures would be next year?
- H.M.Jr: Yes. Ask Bell.
- Bell: Well, I think the only thing you can do is give a range of somewhere between 500 million and a billion....
- Viner: in excess of

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- Bell: ... in excess of the present.
- White: That would be the appropriation for the fiscal ...
- Bell: All depends on what is appropriated. If there is an authorization for a billion and a half, say, in airplanes, I don't think they can spend a half billion in 1940; but if that program is spread over the entire Army as a billion and a half program - other things except airplanes, in addition to airplanes - then they might spend a half billion dollars.
- Currie: and about a quarter of a billion, perhaps, for the Navy, additional?
- Bell: Navy hasn't been mentioned in this program, because they've got a program going of - they'll have eight battleships laying down next year.
- Currie: But that will be an increase in spending over this year - actual expenditure.
- Bell: If the present program is continued, yes.
- Currie: About 200 - 150.
- H.M.Jr: Well, Currie, the Army and Navy, as it is tonight, is about a billion one. Isn't it?
- Bell: That's right - annual program.
- H.M.Jr: And on top of that you've got to add somewhere between 500 million to a billion, on top of the billion one.
- Currie: My only trouble, Mr. Secretary, is that it is really a billion one for this fiscal year - Army and Navy - isn't it?
- Bell: It's contemplated to be about a billion one for 1940, without any new program.
- Currie: So if you attribute all this additional stuff to Army, you're not attributing any additional expenditure to Navy for the next fiscal year.

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- Bell: You've got it wrong. The billion one I'm speaking of is the normal program.
- Currie: But we're trying to get the additional after this fiscal year.
- Bell: Well, as it is, the additional will be somewhere between 500 million and a billion. So if you spend 500 million of that program next year, you'll have a billion six instead of a billion one, see, for national defense.
- Viner: That means half a billion
- Currie: ..addition over this year.
- White: Not allowing any increased expenditure on the Navy.
- Currie: That's what I was trying to get at.
- Bell: Except what it takes to clear up contract authorizations on building contracts.
- Currie: Will that be lower than this year?
- Bell: Not over 50 million or 100 million.
- H.M.Jr: Well - I'm sorry, I'll wait.
- Currie: I think perhaps Harry had the same thing. The other thing, the question mark, was the Social Security program. I know that the Council - of course, you people all know this too - is going to recommend that the benefit payments, and more generous benefit payments than now provided for in the Act, be commenced at the beginning of 1940.
- Bell: Fiscal '40.
- Currie: Is that included?
- Bell: No, that's not.
- Currie: Little more expenditure - perhaps 100, 150 million.
- H.M.Jr: I wasn't aware of it, were you, Dan?

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- Bell: Well, I've heard rumors but I haven't had any program.
- Viner: But if I remember rightly, though, the budgetary treatment of Social Security, you can fix it up there by re-estimating the ultimate obligations on the Treasury.
- Currie: You're quite right, Jake, that will not increase the budget expenditures.
- Viner: Not if you follow the practice of setting off as a liability just what you estimate your revenue is going to be.
- Bell: That all depends on what you're talking about. If you're talking about advancing the date when they pay benefits under the old-age provision, then it makes no change in your budget, because you just cut down on your investment of funds for that account; but there is a scheme to increase the grants to states for those who will not come under the old-age provision. I understand there is a scheme to increase the grants to states by about 100 or 150 million dollars. That's an actual cash outgo.
- Currie: Then there is
- Viner: But you've got some leeway on your investment figure, haven't you?
- Bell: Not for that purpose.
- Currie: That's one of the places where you can increase expenditures without increasing the deficit, as it is set up.
- Viner: Where in the earlier years Dan Bell increased the deficit without increasing expenditures.
- Currie: Yes.
- Bell: On what?
- Viner: Why, by setting up as a liability a larger amount than you were collecting as revenue.

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- Bell: I set up the same amount as an investment that we had in revenue, so it had no effect whatever on the deficit.
- Gaston: Not in fiscal '37, Dan.
- Viner: Not in fiscal '37.
- Gaston: Your transfers to the fund were greater than your tax receipts in fiscal '37, I think, substantially greater.
- Bell: Oh yes, we did that for a reason - yes.
- Viner: Well, you can do it the other way now.
- Bell: But it wasn't large.
- White: If you just convinced him out of that - took two years to get him out of that.
- Taylor: Wasn't large; but it's flexible.
- Viner: It's flexible. There's a law there, but the law as any two men read means two different things.
- White: You (H.M.Jr) had a second point.
- H.M.Jr: Yes, it isn't a point, but I wanted to get this over. If you agree that we should have additional taxes, is there any nice package which we could wrap up in pink ribbons and say, "Gentlemen of the United States, here is your national defense tax, and this is the nice pretty picture on it."
- White: Smells good, looks good, and it ain't good.
- H.M.Jr: Is there such a thing that we could take it and
- Currie: There has been a proposal for just upping the corporation tax rate, because - partly on the ground that that's easy and simple, and also it bears on the beneficiaries of an armament program.
- Viner: I'd say that's all wrong, that there oughtn't to be any rise in corporate taxation at all.
- White: Well now, there's disagreement on that point.

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- Viner: If you want a tax on incentive to invest, that's where you can be sure of it. You'll be getting right in a bad spot.
- H.M.Jr: I want - may I draw on the charity of you gentlemen, can I draw on it for another day? Take pity on this poor Secretary of the Treasury and sweat with me for one more day.
- (Several nod acceptance)
- White: Mr. Hansen said he would be able to devote tomorrow morning.
- H.M.Jr: Well, I'd be in touch, and when the atmosphere clears, why, I'm available any time; just get in touch. What?
- White: If you could begin at 9:30 - 9:30 tomorrow
- Stewart: 9:30.
- White: ... then you can have at least three or four hours. And if you (H.M.Jr) will be available ...
- H.M.Jr: I only have one appointment, to go to the doctor, at 12:15; but outside of that I have no appointments.
- White: I think on that discussion - I think that all the men who are available, Wayne Taylor, Johnny Hanes, could spend - because that kind of discussion is
- Hanes: I haven't got anything.
- H.M.Jr: You (White) mean sit right in.
- White: I think so, if they've got the time.
- Taylor: I'm fine all day tomorrow.
- Hanes: Sunday too, for me, if you want me.
- H.M.Jr: Magill will be here. You're (Bell) on call?
- Bell: I'd hate to spend all day, but I'll be available.
- H.M.Jr: You're available. And then when they come to see me you're available.
- Bell: Yes, sir; I'm really in a terrible hole, but I can run out for an hour or so.