May 6, 1939

To: The Secretary

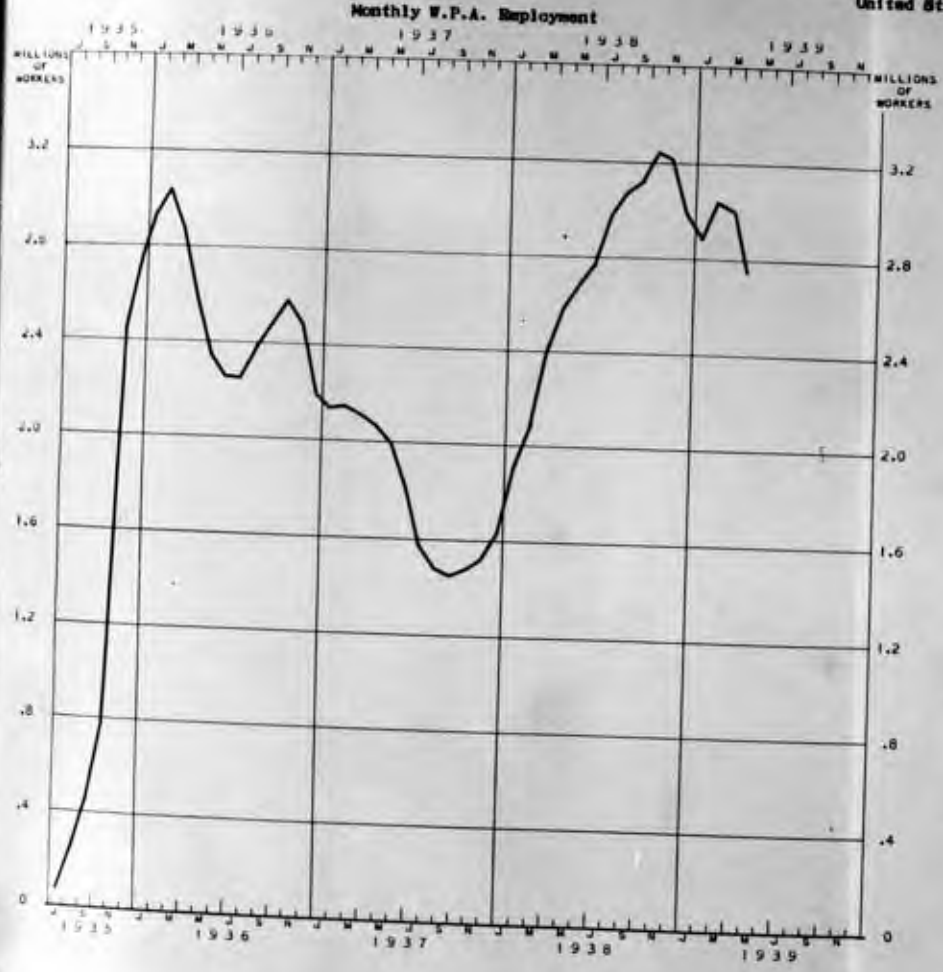
From: Miss Lonigan E.L.

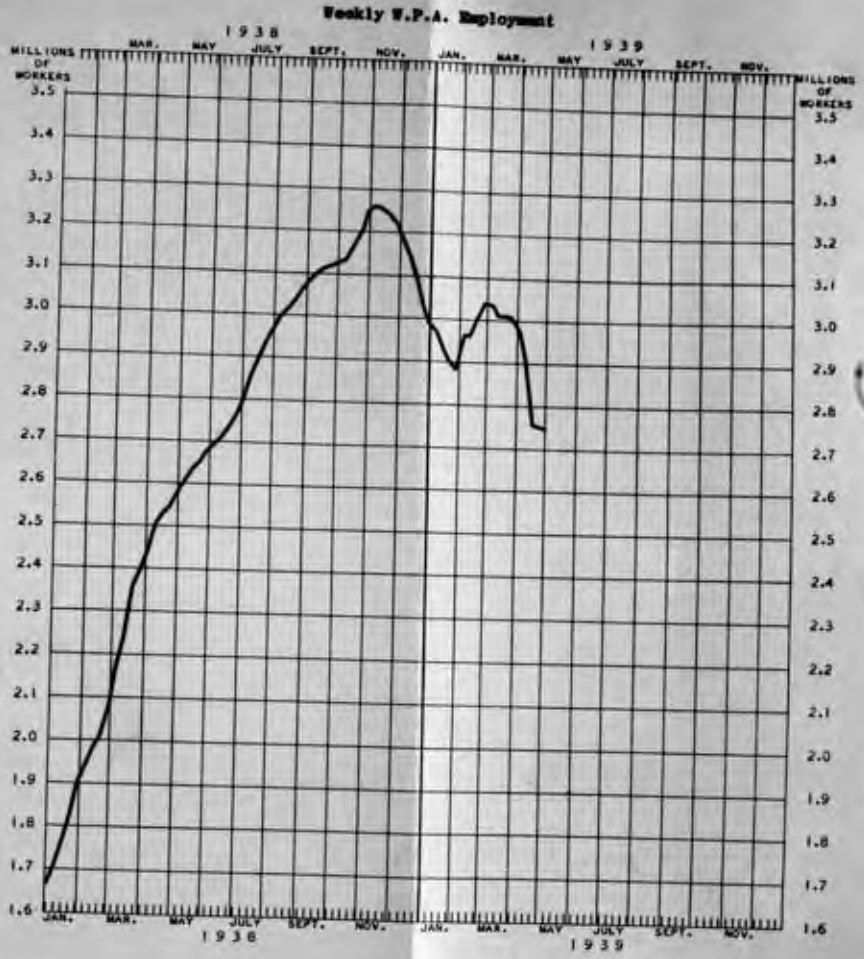
The total number of WPA workers on April 29, 1939 is 2,747,881.

The decrease from the week ending March 25 to the week ending April 29 was 259,330 workers.

WORKS PROGRESS ADMINISTRATION

Number of Workers Employed
United States





Office of the Secretary of the Treasury
Division of Research and Statistics

SOURCE: WORKS PROGRESS ADMINISTRATION

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WORKS PROGRESS ADMINISTRATION
Number of Workers Employed - Monthly
United States

	Number of Workers (In thousands)
1936	
January	2,926
February	3,036
March	2,872
April	2,570
May	2,340
June	2,256
July	2,249
August	2,377
September	2,482
October	2,581
November	2,483
December	2,192
1937	
January	2,138
February	2,146
March	2,115
April	2,070
May	1,999
June	1,821
July	1,569
August	1,480
September	1,451
October	1,476
November	1,520
December	1,629
1938	
January	1,901
February	2,075
March	2,395
April	2,582
May	2,678
June	2,767
July	2,967
August	3,067
September	3,120
October	3,245
November	3,216
December	2,986
1939	
January	2,883
February	3,043
March	3,007
April	2,748 a/

Source: Works Progress Administration.
a/ Confidential.
Monthly figures are weekly figures for the latest week of the month.
They include certified and non-certified workers.

WORKS PROGRESS ADMINISTRATION
Number of Workers Employed - Weekly
United States

Week ending	Number of Workers (In thousands)
1938	
July 2	2,807
July 9	2,853
July 16	2,899
July 23	2,938
July 30	2,967
August 6	2,993
August 13	3,017
August 20	3,039
August 27	3,067
September 3	3,086
September 10	3,102
September 17	3,114
September 24	3,120
October 1	3,129
October 8	3,137
October 15	3,167
October 22	3,201
October 29	3,245
November 5	3,263
November 12	3,258
November 19	3,244
November 26	3,216
December 3	3,185
December 10	3,139
December 17	3,083
December 24	3,021
December 31	2,986
1939	
January 7	2,967
January 14	2,927
January 21	2,898
January 28	2,883
February 4	2,966
February 11	2,964
February 18	3,010
February 25	3,043
March 4	3,034
March 11	3,009
March 18	3,012
March 25	3,007
April 1	2,976
April 8	2,901
April 15	2,757
April 22	2,750
April 29	2,748 a/

Source: Works Progress Administration.
a/ Confidential.

May 6, 1939
12:03 p.m.

HMJr: Hello.

Sumner Welles: Good morning, Henry. Are you tied up, because I don't want to trouble you if you are.

HMJr: Pardon?

W: Are you tied up with somebody?

HMJr: Well, but they're my -- they're Treasury people.

W: Oh, all right. I simply wanted to tell you these two things. In compliance with your request to be advised when the Italians are called in, the Secretary has seen the Italian Ambassador this morning at eleven o'clock.

HMJr: Yes.

W: And gave him the information and told him that there would be a forty-five day period in which to discuss this, if they so desired, than to take immediate action.

HMJr: Right!

W: Now, second, you told me the day before yesterday that that Tannenberg memorandum, you know.....

HMJr: Yes.

W: .....had been sent to Feis two days before.

HMJr: Yes.

W: Feis received the original letter this morning and the envelope was marked -- postmarked yesterday.

HMJr: Well, I'll be darned!

W: And so I simply want to tell you that.

HMJr: Well I'm -- well, then I.....

W: He had a copy sent to him the day before but the original was only received this morning and postmarked yesterday.

HMJr: I'll be darned! Archie Lochhead -- I asked him to check up -- I'm delighted to know that because there's something wrong in our mail route.

W: Well, I just wanted to let you know that at this time.

HMJr: Was the thing only mailed yesterday?

W: The envelope is postmarked yesterday.

HMJr: Well, I'll be darned.

W: He has the -- the envelope.

HMJr: Well, if he wouldn't mind sending me the envelope back, I'd like to take a look at it.

W: Be glad to -- I'll ask him to do so.

HMJr: Yeah, I'd like to take a look at it.

W: And I'd like to send you in reply to your request as to what my own point of view in that regard was. I'll send you a letter on Monday giving you my point of view.

HMJr: Right. Now, what else?

W: That's all.

HMJr: And -- we've still got our first line trenches out here.

W: Well, I prefer to see roses in them rather than you taking refuge.

HMJr: Righto!

W: All right, Henry.

HMJr: You'll have him send that over -- I want to trace that down.

W: All right, I'll do that. Good bye.

Pros & Cons

237

"PROS AND CONS" dated 5/8/39

--this draft taken to the President 5/8
at 1:30 P.M. by the Secretary.

CGH

Pros and Cons
5/8/39

238

I am here this morning in response to Chairman Doughton's letter inviting me to present information relating to certain tax proposals and other pertinent matters.

Tax proposals cannot be discussed comprehensively except in relationship to our broad national and fiscal position. We are now in the midst of a world situation which imposes on this Government a special responsibility. We must demonstrate that a democratic government has the power and the flexibility to survive a prolonged crisis and chaotic world conditions and yet emerge with the strength of its free institutions unimpaired. Preservation of our democratic form of government over a long period of years requires, in my opinion, a fiscal program which has a fourfold objective: (1) promotion of free enterprise and private investment; (2) attainment of full business recovery; (3) maintenance of our public finances in a sound and unassailable position, and (4) a just distribution of tax burdens and a more equitable distribution of national income.

Successful operation of democracy demands that all four objectives be solidly linked together.

When we consider any specific change in our fiscal program we must satisfy ourselves that the change makes for a better and not a worse distribution of tax burdens and of national income, that the change promotes and does not retard business recovery, and that the change makes easier and not more difficult establishment of a balanced relationship between revenues and expenditures.

Full attainment of these objectives is difficult at best. It is made more difficult by a new and ominous development in world affairs -- the armament race now gripping the important nations of the world. Great Britain in the present fiscal year is spending $3 billion on armaments, or almost 50 percent of its national budget; France is devoting over 40 percent of its national governmental expenditures to the same purpose; Italy, 50 percent; Germany, probably 60 percent; Japan over 70 percent. These huge expenditures are being financed largely by borrowing. The race is becoming more intense and there is no end in sight.

For us the danger is that these developments may mean a necessarily increased cost for national defense here, together with monetary instability abroad,

disruption of our foreign commerce, and perhaps other unsettlements, the consequences of which we cannot fully predict. In this connection, it is interesting to note that in our budget for this fiscal year expenditures for past wars and national defense are almost one-fourth of total expenditures.

No major problem facing this government today can be solved properly without full consideration of the position of this country in relation to the present international crisis. The unmistakable implication of the international situation is that we should look ahead to our future fiscal position and redouble our efforts to attain full recovery. High national income and a sound fiscal position are essential to adequate national defense. It is against this background that we reexamine our fiscal program.

A fundamental objective of sound finance clearly is a balanced budget. There is, of course, no good reason why taxes must exactly balance expenditures each year any more than each month, each week or each day. There are periods during which sound fiscal policy calls for an excess of outgo over income, and others when it calls for an excess of income over outgo.

In a depression it is inevitable that there will be deficits. Revenues decline at the same time that the Federal Government is called upon to undertake inescapable social and economic burdens. If, however, deficits are too long continued, the depressive effects of uncertainty tend to make recovery more difficult. The sequel to deficits in emergencies should be surpluses during years of prosperity. That was and is one of the broad purposes of seeking to raise the national income to a high level, thus assuring revenue great enough not only to end the deficits which began in 1931, but also to reduce the public debt.

In carrying out our fiscal policy it would be helpful to have machinery which would more fully coordinate our efforts. It is not the prerogative of any administrative Department to make suggestions to the legislative branch of the Government for the conduct of its work, but I am sure that you would wish me to be frank in suggesting ways of surmounting difficulties which I believe now attend the joint efforts of the Ways and Means and Finance Committees and the Treasury Department.

If, for instance, the Ways and Means and Appropriations Committees of this House and the Finance

and Appropriations Committees of the Senate could meet each session as one Joint Committee on Fiscal Policy, to consider the over-all aspects of the expenditure and revenue programs, simplification and greater effectiveness would result. The Budget Act of 1921 set up a procedure for the orderly formulation by the Executive of fiscal proposals and for their submission to the Congress as a unified budget. No comparable procedure has been set up in Congress for considering revenues and expenditures together as two inter-related aspects of a single problem. I hope this Committee will agree with me that some such innovation would improve the efficiency of the Government. By providing for a preliminary legislative consideration of the over-all picture of appropriation and revenue measures it would give Congress a broad perspective of the management of the Government's finances and permit a better ordered coordination between the executive and the legislative branches in this field.

This joint committee would in effect be a lens through which all appropriation and revenue measures could be viewed in relationship to both what the nation needs and what the nation can afford. This committee could have continuous life for the purpose of actively

studying fiscal problems between as well as during sessions of Congress. The Treasury Department would, of course, cooperate fully in this work to the extent that the committee desired.

Thus far I have dealt with the financial problems of the Federal Government alone. We must remember, however, that even if we had in operation the best conceivable Federal fiscal plan, we still would have touched less than half of the tax problem which confronts the nation. Almost 60 percent of the total tax revenues of the country are collected by state and local governments.

We have talked about removing injurious Federal-State tax conflicts for the past five years. Our predecessors talked about the same problem. I recommend that Congress create a small temporary national commission to report to Congress as soon as feasible on the various aspects of most desirable intergovernmental fiscal policy. Such a commission should be made up of men of ability who enjoy the highest possible public confidence, who are familiar with the fiscal problems of Federal, state and local governments, but who will represent the public at large rather than particular governmental units.

Overlapping taxes have grown in number and size as both Federal and state governments have sought new revenue. Grants-in-aid are being demanded of the Federal Government in increasing amounts. The results of our fiscal situation are increasingly unsatisfactory to both the state governments and the Federal Government, and more and more burdensome to many taxpayers. The findings of such a commission should assist us in achieving a more orderly relationship between the Federal, state and local fiscal systems.

Thus far I have talked about two broad fiscal matters of great importance to the Treasury. Let me turn now to questions of taxation.

I desire first to reiterate a number of recommendations for tax changes which have previously been presented to you.

1. In his Budget Message of January 3, 1939, the President recommended that Congress extend the miscellaneous internal revenue taxes which under existing law will expire next June and July, and to maintain the current rates of those taxes which otherwise would be reduced in June.

2. In his message of January 19, 1939, the President recommended legislation making all government

salaries hereafter earned and all interest on government securities hereafter issued subject to Federal and state income tax laws. That part of this recommendation dealing with government salaries, I am pleased to note, has already been incorporated into law.

3. In my statement of March 24, 1939, I presented for your consideration four alternative rate plans for old-age insurance contributions during the next three years.

4. The Treasury Department has pointed out from time to time that the present law allows excessive deductions for depletion of oil and gas wells and certain mines. Removing this inequitable special privilege would produce a substantial amount of revenue.

It seems physically impossible at this session of Congress to rewrite the tax laws before the special study committee has conferred with states and municipalities and brings in a report.

With regard, however, to the specific items mentioned in Chairman Doughton's letter, I am glad to present for your consideration a summary of the findings of the Treasury staff. Before commenting on them,

I wish to emphasize the importance of the statement in the Chairman's letter that "a fundamental prerequisite of any tax revision at this time is maintenance of the present revenue." We must not forget that one of the important objectives of our fiscal program is to approach a balance between revenues and expenditures. For this reason any tax reductions must of necessity be offset by tax increases elsewhere. I wish to emphasize that in my opinion we should under no circumstances weaken the revenue-producing capacity of our tax structure. I regard this as the keystone of any program of tax revision that may be undertaken at this session. If tax revision were confined to tax reductions, the resulting uncertainty over our fiscal policy would injure and not help business. We must take no step which the public may interpret as moving away from the objective of a balanced budget.

I turn now to a brief summary of the arguments for and against the specific tax suggestions which Chairman Doughton asked me to discuss with you:

1. The first item on Chairman Doughton's list is the suggestion that the capital stock and excess profits taxes be repealed. Under the present law

the capital stock tax is based upon a declared capital stock value which the taxpayer may revise every three years. The declared value may be any figure that the taxpayer desires to submit, regardless of the actual value of the stock. The excess profits tax applies to profits in excess of 10 percent of such a declared value. The taxes are thus not really taxes on the value of capital stock or on excessive profits. The reason for the present form of the taxes is the difficulty of administering true capital stock and excess profits taxes.

(a) The major defect of these two taxes is that they operate very erratically. The tax liability they impose depends on the taxpayer's ability to forecast profits for the next three years, as well as upon the amount of profits actually realized during each of the three years. The closer declared value turned out to be ten times average earnings, the lower are the combined capital stock and excess profits taxes. Departures from such a declared value result in higher taxes.

(b) The uncertainty of the capital stock and excess profits taxes is irritating and may thus be a business deterrent. Forecasts of earnings are particularly difficult to make in the case of new businesses and those with unstable incomes, such as the capital goods industries, with the result that taxes imposed on such businesses are at times inordinately high.

Against the proposal are the following considerations:

(a) Repeal of the taxes would result in a substantial loss of revenue. For a year with business conditions similar to 1939 it is estimated that the loss would be $125,000,000.

(b) If the taxes were repealed, corporations without profits would be altogether free from taxes applicable only to corporations. At present deficit corporations declare a capital stock value, and are thus required to pay some tax.

2. The second item on which Chairman Doughton asked me to comment is the suggestion that net losses of business, both individual and corporate, incurred in one year be offset against the income of subsequent years. At present, individuals and corporations are taxed on their annual incomes without reduction for losses incurred in prior years.

In favor of the proposal are the following considerations:

(a) Allowing the carry-forward of business losses would make taxable income

coincide more nearly with actual income over a period of several years. Businesses with alternating income and loss now pay higher taxes over a period of several years than do those with stable incomes. Many pay income taxes in single years of net income even though over a period of years they have had no net income or have suffered a net loss.

(b) Allowing the carry-forward of business losses would somewhat increase the incentive to new enterprises and to the expansion of the capital goods industries, which are subject to wide fluctuations in earnings.

(c) Allowing a loss carry-forward would reduce the administrative difficulties caused by the taxpayers' effort to shift items of income into loss years.

The disadvantages that would need to be considered in connection with the proposed carry-over are these:

(a) Assuming that the carry-forward provision was not made retroactive and that the law applied first to 1940, there would be no revenue loss until the fiscal year 1942, after which the loss would increase over the number of years required to reach full application. For example, in a year of full application it is estimated that the revenue loss from a three-year carry-forward provision would vary between $25,000,000 and $200,000,000, depending on the business conditions of the year and the three preceding years.

3. The third item on your Chairman's list is the suggestion that corporations be allowed to deduct their net capital losses in full from their ordinary incomes. Under the present law an excess of corporate

capital losses over capital gains can be deducted from ordinary income only to the extent of $2,000.

In favor of this proposal, the following considerations may be advanced:

(a) Allowing corporate net capital losses to be deducted in full from ordinary income would make taxable income coincide more nearly with the income from the total operations of the corporation. At present net capital gains are always taken into account in tax computations while net capital losses in excess of $2,000 cannot be recognized. As a result a corporation may be obliged to pay an income tax in a year when its income from other sources was wiped out by capital losses.

(b) Allowing the deduction of corporate net capital losses from other income might add to investment since corporations would have greater incentive to invest in the securities of other corporations or to launch new ventures of their own.

Against the proposal are the following considerations:

(a) The allowance of the full deduction of corporate net capital losses from other income would result in a serious revenue shrinkage in years of declining prices for securities and other property. Normally, these are the years when the need for revenue is most acute. It is estimated that on the basis of calendar year 1939 levels of business the revenue loss might be approximately $70,000,000.

(b) Corporations that hold securities could reduce their taxable income and thus minimize their tax liability by selling those securities which had declined in value.

4. The fourth item on the Chairman's list on which I have been asked to give the pros and cons is the suggestion that the deductions for capital losses of individuals be liberalized.

In favor of such a change the following considerations are pertinent:

(a) It would put the income tax more nearly on the basis of actual income over a period of years.

(b) It would tend to stimulate the assumption of financial and business risks.

The proposed more liberal treatment of capital losses would, on the other hand, have some undesirable aspects:

(a) The revenue would be reduced. For a year with business conditions similar to those anticipated for 1939 it is estimated that the loss in revenue would amount to approximately $40,000,000.

(b) The liberalization would result in some evasion of tax through deliberate manipulation of sales of assets on which losses had accrued.

5. The final item on the Chairman's list is the suggestion that the upper surtax rates be reduced. At present the normal tax is 4 percent and the maximum surtax rate, applicable to the amount of surtax net incomes in excess of $5,000,000, is 75 percent.

In favor of the proposal are the following considerations:

(a) The present top surtax rates may deter persons with very large incomes from investment in private enterprise. Under the present law the taxpayer with $500,000 surtaxable net income could retain from an additional dollar of income only 26 cents, 74 cents being taken in Federal income taxes. His share may be further reduced by state taxes. If his income were still higher he would bear even higher rates.

(b) The rate may be so high as to have passed the point of maximum revenue return by encouraging the shifting of funds from taxable investments to tax-exempt securities.

Against reducing these top surtax rates are the following considerations:

(a) When the aggregate tax burden is great persons with especially large incomes can rightfully be expected to make extraordinary sacrifices. A more equitable distribution of income may also be promoted.

(b) The existence of a large volume of tax-exempt securities now provides individuals in the higher income groups with a tax-free haven to which they can resort if they choose, so that the tax on income from all sources is much lower than the surtax rates would indicate. To meet this objection it has been suggested by some, notably Senator Glass, that tax-exempt income be included at the bottom of the rate brackets instead of at the top, as is now the case, thus increasing the rates applicable to other income.

(c) The immediate effect of lowering the top surtax rates would be a loss in revenue. For a year like 1939 it is estimated that the loss from reducing the top surtax rate to 60 percent would be a little more than $10,000,000.

(d) The efficacy of reducing high surtax rates for the purpose of stimulating investment is substantially weakened by the fact that to a

person in the surtax brackets of 60 percent, for instance, an investment would have to provide a yield of at least 8 percent with no risk in order to be more attractive than the alternative he has of investing in state bonds of prime quality. Of course, with present rates persons in the highest bracket must obtain taxable yields of at least 14 percent with no risk to retain as much profit as can be obtained from a 2½ percent non-taxable income. It is to be doubted whether there are many such investment opportunities not already seized by corporations or by persons in the $50,000 to $150,000 bracket. This fact demonstrates that a reduction in high surtax rates without at the same time reducing sharply curtailing tax-exemption privileges constitutes a very dubious device for stimulating investment.

I have already emphasized that in my opinion tax revision at this time must not be permitted to reduce the revenue-producing capacity of the tax system. That means that the adoption of any of the above

suggestions involving loss of revenue must be coupled with revenue-producing revisions elsewhere. This is a very difficult problem for Congress to face. The taxes resorted to for replacing any lost revenue should have the least harmful effects on business and should contribute to greater equity. I suggest the following three possibilities:

1. The corporation income tax rate could be increased. The corporation income tax in any event will have to be acted on at this session since it expires at the end of 1939. In renewing the tax it is important that steps be taken to reduce the possibility of closely-held corporations piling up profits and not paying them out in taxable dividends to stockholders.

2. Individual income taxes could be increased. There is merit to the suggestion that the rates on income brackets between $15,000 and $250,000 are relatively low compared with incomes of less than $15,000 and more than $250,000, and could be increased. Furthermore, to promote good citizenship, it is felt that every individual and family with income of more than $800 could pay and would be willing to pay a small tax.

3. Estate and gift taxes could be increased.

In conclusion, let me say that if you are interested in further information, my staff and I are prepared to furnish it and will be happy to work with you to the extent that you may desire.

Treasury experts
without pros & cons

5/8/39

Treasury Experts"

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It seems physically impossible at this session of Congress to rewrite the tax laws before the special study committee has conferred with states and municipalities and brings in a report.

With regard, however, to the specific items mentioned in Chairman Doughton's letter, I shall be glad to have members of the Treasury staff present their ~~findings~~ for your consideration. They are prepared to discuss with you the following:

Repeal the capital stock and excess profits taxes.

Allow business net losses in one year to be carried forward and offset against income in subsequent years.

Permit corporations to deduct net capital losses from ordinary taxable income.

Liberalize the deductions allowed for net capital losses sustained by individuals.

Reduce the individual surtax rates in the upper brackets.

I wish at this point to emphasize the importance of the statement in the Chairman's letter that "a fundamental prerequisite of any tax revision at this time is maintenance of the present revenue." We must not forget that one of the important objectives of our fiscal program is to approach a balance between revenues and expenditures. For this reason any tax reductions must of necessity be offset by tax increases elsewhere. In my opinion we should under no circumstances weaken the revenue-producing capacity of our tax structure. I regard this as the keystone of any program of tax revision that may be undertaken at this session. If tax revision were confined to tax reductions, the resulting uncertainty over our fiscal policy would injure and not help business. We must take no step which the public may interpret as moving away from the objective of a balanced budget.

The adoption of any of the above suggestions involving loss of revenue must be coupled with revenue-producing revisions elsewhere. This is a very difficult problem for Congress to face. The taxes resorted to for replacing any lost revenue should have the least harmful effects on business and should contribute to greater equity. I suggest the following three possibilities:

1. The corporation income tax rate could be increased. The corporation income tax in any event will have to be acted on at this session since it expires at the end of 1939. In renewing the tax it is important that steps be taken to reduce the possibility of closely-held corporations piling up profits and not paying them out in taxable dividends to stockholders.

2. Individual income taxes could be increased. There is merit to the suggestion that the rates on income brackets between $15,000 and $250,000 are relatively low compared with incomes of less than $15,000 and more than $250,000, and could be increased. Furthermore, to promote good citizenship, it is felt that every individual and family with income of more than $800 could pay and would be willing to pay a small tax.

3. Estate and gift taxes could be increased.

In conclusion, permit me to say that the most important task we have before us is to do everything we can to promote lasting business recovery. Our consideration of tax changes must have that necessity in mind as well as revenue needs. I sincerely hope that Congress will study the specific proposals that Chairman Doughton has mentioned as well as any others that may be made from that standpoint.

Members of the Treasury staff will be available to furnish any assistance that they can.

May 8, 1939

MEMORANDUM FOR THE SECRETARY:

Proposals for increasing revenue are described on pages 9 to 22 inclusive of the Magill-Shoup book. There are two general programs presented, one to increase Federal tax revenues by nearly $1000 million, the other to increase them by nearly $2000 million, on the basis of 1936 business conditions.

The increases in revenue in both programs would come from:

(1) Increases in individual income tax rates and decreases in personal exemptions, and

(2) Increases in the rates of the estate and gift taxes, decreases in exemptions, and coordination of the two taxes.

Changes which would reduce revenues are:

(1) The more liberal treatment of business net losses and capital net losses. (Discussed at the bottom of page 15 and on page 17.)

(2) Repeal of the capital stock and excess profits taxes (page 17), and

(3) Repeal of some of the excise taxes. (page 17)

The two programs differ only in the rates of the individual income tax.

A table showing yields of the proposed system to increase revenues by nearly $1000 million is shown on page 18. The proposed rate schedules are shown on pages 14 and 19. The income tax rate schedule for the program to raise nearly $2000 million more revenue is shown on page 22.

The Magill-Shoup programs differ from the program summarized in Schedule J of the memorandum of October 24, 1938 primarily in that the latter called for smaller increases in income and estate and gift taxes, and imposed a number of other types of taxes.

Roy Blough

May 8, 1939

These are Mr. Blough's suggestion, to go in after the third paragraph of page 8 to take tne place of all the pros and cons following after page 9.

However, action is necessary on at least one matter not included in the earlier recommendations. The corporation income tax structure expires at the end of 1939. In ~~renewing~~ reviewing the tax it is important that ~~deterrents~~ provisions be included ~~against~~ to prevent the possibility of closely-held corporations piling up profits and not paying them out in taxable dividends to stockholders. A number of other suggestions have been received by the Treasury from time to time for revising the corporation tax structure as well as other suggestions for tax revision. If you are interested in having the pros and cons of these proposals discussed and information submitted concerning their effects, we shall, of course, be glad to submit the desired information.

It would like to emphasize that any tax changes adopted should not reduce the total revenues. Whatever revisions may be made in the tax system it will have to bring in as

much revenue as the present system. This is a very difficult problem for Congress to face. We must not forget that one of the important objectives of our fiscal program is to approach a balance between revenues and expenditures. For this reason it is necessary to offset any tax reductions with tax increases elsewhere. I wish to emphasize that it is my opinion that under no circumstances should we weaken the revenue-producing capacity of our tax structure. I regard this as the keystone of any program of tax revision that may be undertaken at this session. If tax revision were to take the form only of tax reductions, the resulting uncertainty over our fiscal policy would injure and not help business. We must take no step which the public may interpret as moving away from the objective of a balanced budget.

Taxes resorted to for replacing any loss in revenue should have the least harmful effects on business and should contribute

to greater equity. I suggest the following three possibilities:

1. The corporation income tax rate could be increased.

2. Individual income taxes could be increased. There is merit to the suggestion that the rates on income brackets between $15,000 and $250,000 are relatively low compared with incomes of less than $15,000 and more than $250,000, and could be increased. Furthermore, to promote good citizenship, it is felt that every individual and family with income of more than $800 could pay and would be willing to pay a small tax.

3. Estate and gift taxes could be increased.

I shall not discuss in detail any tax measures, but my staff and I are prepared to furnish further information and will be happy to work with you to the extent that you may desire.

May 8, 1939

4:30 pm

Present:

Mr. Hanes
Mr. Gaston
Dr. White
Mr. Duffield
Mr. Blough

HM,Jr: It is very difficult for me to tell you this thing, because I don't know how to put it, but there may be a happy ending.

Well, here's the point. I showed the President what I call the report without the pros and cons. Well, he wouldn't even let me get it to him. He said that he met with the "big four" this morning and they are opposed to any tax bill; that they can't have a tax bill, and he said, "I can't go and say to Mr. Garner and the rest of them 'did you or didn't you say this'. And when I let him finally get around to Doughton's letter, he said it was terrible and I did not understand and so forth and so on.

"Thursday" -- or whenever I was over there, I said, "everything in here you o. k'd." "Well," he said, "that was before I saw the leaders."

So I said, "Mr. President, why don't you save yourself all the trouble and tell me you don't want a tax bill. It will make it so much easier." So he said, "Well, they like your idea of the Committee and all that stuff."

So I said, "Well, I am not going up on the Hill, Mr. President. Mr. Doughton has just announced that it's Administration policy that there isn't going to be any tax bill. I would not go up there."

There is no use going through all the arguments. He gave me this argument and that argument, and so on.

So I said what was I going to tell Doughton, and he called Doughton and is having him come tomorrow morning at 9 o'clock. I am to be there.

So he went all through this -- I can't repeat; not that I don't want to; I can't remember it. It's nothing new. It's just one thing after another until I was shoved completely off. I said, "You have got me down, Mr. President, but I am not going up on the Hill. If this is political, and Administration, let the Administration announce it."

"Well," he said, "maybe there is a place in between." And then he sent for a stenographer and dictated a letter that he said Doughton should write to me.

Then he said that he likes this idea of a committee and he said if the Committee would recommend reduce surtaxes, etc., do that effective the first of January, he would go along with that. The Fiscal Committee.

So he kept saying what I thought about it. I said,"I can't answer, Mr. President. After all, you have reversed yourself. You are giving this to me new. What do you expect me to say?" So he said, Well, say something. I said, "No. I am not going to say anything other than that I am not going to go up on the Hill."

Well, then, he said, "Have you ever thought that maybe this country is a $60,000,000,000 to $70,000,000,000 country. Maybe that's what it is going to be. Maybe what we are doing now;may be the basis we are on now, maybe that's what we are going to be." Andhe said, "Well, what would you do if this is a $60,000,000,000 to $70,000,000,000 country? What would you do?" I said, "I have not been thinking about that. I have been thinking of $80,000,000,000."

"Well, what would you do?"

"Mr. President, I can't answer. I have not been thinking about it.

"Well, what would you do?"

He said, "Barring armaments, which we hope are not

going to be permanent, that brings us down to $2,000,000,000. Supposing we raise $2,000,000,000 new taxes. We balance the budget." I said, "Sure. Why not?" So I said, "If you want that program, Magill and Shoup left that here last fall." So he said, "Well, bring it along tomorrow morning. We will show it to Bob Doughton." I said, "It's all written. I have locked it in the safe. I was afraid to show it to anybody." So he said bring it around tomorrow morning.

So I said, "Well, as far as I am concerned, I could go up cheerfully and talk about balancing the budget on that basis. I could do that cheerfully, but" I said, "I just never thought of it." "Well,"he said, "bring it up tomorrow morning."

Don't ask me what it means or anything else. I had about two hours. I was dragged through the knot-hole ten times. All I can say is I am alive. There is no use getting excited, and instead of threatening -- and I mean he did all of that and did all of the sneering -- I just kept as quiet as I am now. All I could think to say was under the circumstances that I won't go up on the Hill. All Mr. Doughton has to do is say well, we will simply renew the taxes. There is nothing for me to go up and explain. He didn't like that.

All I can ask you gentlemen, on your word of honor, is not to talk about it. By ten o'clock tomorrow morning it may be entirely different.

Oh, yes! He asked Jere Cooper to come along. And certainly Doughton on Saturday and Doughton today was all for this. You didn't have to urge him to write anything.

I said, "If I go up on the Hill, I can't go up because Mr. MacCormack is going to say to me what do you think of this tax and what do you think of that. "Do you want me to say the President of the United States won't let me answer? If you want me to say the President of the United States won't let me answer -- but don't you think for one minute that they are not going to bring it up."

He came back the second time and said, "Didn't we talk about having a tax on rearmament?" I said,"Sure!" As a matter of fact, Johnny, that's where you started.

I said to the President, "Here's an increase of $372,000,000. (See ticker attached.) I would like to

say at the press conference "Where is it coming from?" and so forth and so on and "how are we going to get it?"

"Simply say that you don't know anything about policy, but you are worried about where you are going to get the money."

Why not? The humor I am in if they once get me telling the truth, at least it will be good for my soul.

I tried two or three times to go. I said, "Mr. President, you have me absolutely down. I might just as well go."

"No. Sit around and talk a while." He kept saying, "What would you do?"

Well, I have a long time and this is the way I feel. It's just a question of raising another $2,000,000,000. He said, "Can you do it?" I said, "Sure we can do it. We have it all."

I told Miss Le Hand, "You know, the President put the roller over me. And then he saw a little bit of Morgenthau sticking out, so he ran the roller over me again. When he had me flat, he took out a hypodermic of $2,000,000,000 new taxes and jammed a little life into me.

Well, what's happened, they have pushed me so far they will find the real Morgenthau. See? I am sick and tired of straddling.

oOo-oOo

Press Conf

SECRETARY MORGENTHAU SAID TODAY HE WAS GREATLY DISTURBED BY THE RECORD - BREAKING $1,216,528,572 AGRICULTURE DEPARTMENT APPROPRIATION BILL AND DECLARED THAT THE TIME HAS ARRIVED TO START REDUCING DEFICITS.

5/8--R430P

ADD MORGENTHAU

THE SENATE AGRICULTURE COMMITTEE, LARGELY BY ADDING PROVISIONS FOR "PARITY PAYMENTS" TO FARMERS, RAISED THE AGRICULTURE BILL $372,000,000 OVER BUDGET ESTIMATES. THE SENATE BEGAN DEBATE ON THE MEASURE TODAY. H MORGENTHAU SAID AT A PRESS CONFERENCE THAT THE FARM BILL WOULD INCREASE THE $3,300,000,000 DEFICIT CONTEMPLATED FOR THE NEXT FISCAL YEAR.

"AND A $3,300,000,000 DEFICIT IS PLENTY," HE SAID.

HE SAID HE DID NOT CARE TO DISCUSS THE MERITS OF THE BILL BUT "I DO WANT TO SAY THAT THE INCREASE, ADDED TO OUR NEXT YEAR'S DEFICIT, DISTURBS ME GREATLY."

MORGENTHAU SAID THAT IF CONGRESS APPROVES THE BILL, IT WILL BE UP TO CONGRESS TO PROVIDE THE REVENUE.

5/8--R433P

ADD MORGENTHAU

HE WAS ASKED IF HIS STATEMENT INDICATED HE FELT IT WAS TIME TO START CUTTING DOWN DEFICITS. HE ANSWERED UNHESITATINGLY "YES."

HE DECLINED TO SAY HOW CONGRESS MIGHT RAISE THE REVENUE TO MEET THE AGRICULTURAL BILL INCREASE BUT HE SAID ITS PASSAGE WOULD MAKE THE TAX PROGRAM "MORE DIFFICULT THAN BEFORE."

HE SAID HOWEVER, IT WAS TOO EARLY TO TELL WHETHER IT WOULD BE NECESSARY TO REVISE THE TAX PROGRAM.

HE CALLED ATTENTION TO THE FACT THAT THE 75TH CONGRESS APPROPRIATED $212,000,000 FOR FARM PARITY PAYMENTS BUT FAILED TO PROVIDE REVENUE.

"I WAS UNDER THE IMPRESSION THAT TAXES WOULD BE PROVIDED FOR THEM, BUT I'VE GIVEN UP HOPE ON THAT. I AM TAKING A REALISTIC ATTITUDE," HE SAID.

(FIRST LINE ABOVE X X INDICATED HE FELT IT ETC)

S/E ONA3EP

THE SENATE APPROVED A $225,000,000 ITEM IN THE AGRICULTURE APPROPRIATION BILL FOR PRICE ADJUSTMENT PAYMENTS TO FARMERS. THE ITEM WAS APPROVED BY A VOICE VOTE.

5/8--R435P
SENATOR SCOTT W. LUCAS TOLD THE SENATE TODAY "EMERGENCY FARM LEGISLATION WILL BE NECESSARY FOR SOME YEARS TO COME."

HE ASSERTED DURING DEBATE ON THE $1,216,528,572 AGRICULTURE APPROPRIATION BILL THAT "THE WELFARE OF OUR ENTIRE NATION RESTS UPON THE WELFARE OF AGRICULTURE."

THE SENATOR SAID THAT "ONE PHASE OF OUR ECONOMIC LIFE CANNOT BE DISREGARDED" IF THE ENTIRE ECONOMIC SYSTEM IS TO PROSPER.

LUCAS TRACED EFFORTS OF A GROUP HEADED BY HIM TO DEVELOP A BROAD-SCALE FARM PROGRAM TO AID FARMERS.

DUE TO PRESIDENTIAL VETOES AND UNFAVORABLE SUPREME COURT OPINIONS, LUCAS SAID, FARM LEGISLATION HAS BEEN DRAFTED UNDER JEOPARDY DURING THE LAST 20 YEARS.

THE SENATOR FELT, HOWEVER, THAT RECENT SUPREME COURT DECISIONS INDICATED THAT "WE ARE NOW ON FIRMER GROUND" TO LEGISLATE FOR SOLUTION OF THE FARM PROBLEM.

5/8--R356P

ADD AGRICULTURE BILL, SENATE

LUCAS DEFENDED THE AGRICULTURAL ADJUSTMENT ACT AND CONTENDED THAT ITS CRITICS MUST OFFER A CONSTRUCTIVE SUBSTITUTE. HE SAID HE HAD NOT BEEN CONVINCED THAT SUBSTITUTES OFFERED TO DATE WERE SUBSTANTIAL ENOUGH TO SUCCEED.

HE SAID THAT THE AAA WAS BECOMING MORE POPULAR WITH ILLINOIS FARMERS, CITING INCREASED PARTICIPATION IN THE NEW DEAL CROP CONTROL PROGRAMS.

THE SENATOR THEN SAID THAT IF THE APPROPRIATIONS WERE VOTED HE FELT THAT SOME EFFORT SHOULD BE MADE TO OBTAIN ADDITIONAL REVENUES NEEDED.

"THE AMERICAN FARMER DOES NOT WANT AND DOES NOT SEEK A HANDOUT," LUCAS SAID.

5/8 ON442P

RE TAX STATEMENT

May 8, 1939.
11:00 A. M.

Present: Mr. Hanes
Mr. Gaston
Mrs. Klotz
Mr. White
Mr. Blough
Mr. Duffield

H.M.Jr: How is Papa Doughton?

Blough: Very cooperative, and he is willing to change this any way you want.

H.M.Jr: Now, what are the changes he made?

Blough: Now, just a second, I'll give them to you.

H.M.Jr: What changes has he made? Suppose you read it out loud the way you brought it down.

Blough: I'll read it out loud the way I took it down to him, and each of you have a copy of the way it came back.

H.M.Jr: No, read it the way you brought it back.

Blough: "My dear Mr. Secretary:

"The Committee on Ways and Means of the House of Representatives invites you to appear before the Committee on May...." - blank - don't know the date yet - "....at which time the Committee will be pleased to have an expression of your views as to any changes in our internal revenue tax laws that you consider might be helpful to business as well as equitable to taxpayers. Also, the Committee would be pleased to have you give it the benefit of any information you have as to the desirability of various tax changes which have been suggested recently by business organizations and private individuals. Among the suggestions which have been most frequently made and which I, myself, have thought might be worthy of consideration are the following:

"Repeal the capital stock and excess-profits taxes.

"Allow business net losses in one year to be carried forward and offset against income in subsequent years.

"Permit corporations to deduct net capital losses from ordinary taxable income.

"Liberalize the deductions allowed for net capital losses sustained by individuals.

"Reduce the individual surtax rates in the upper brackets.

"It would be helpful to the Committee if you would...."

H.M.Jr: What has he done? He's just changed the order?

Blough: That's the same order that the letter went down to him in, and the only difference has been that the repeal of the capital stock and excess-profits taxes was put up first, because it seemed like more of a major change.

H.M.Jr: Righto.

Blough: "It would be helpful to the Committee if you would present the arguments for and against as many of these suggestions as the Treasury has studied.

"Obviously most of these changes, if adopted, would result in a decrease in revenues. Inasmuch as a fundamental prerequisite of any tax revision at this time is maintenance of the present revenue, the Committee would appreciate it if you would also discuss possible ways of offsetting any revenue losses which might occur in any changes made. The Committee would, of course, be glad to hear your views on any other pertinent matters which you may wish to discuss."

H.M.Jr: Well, what's he changed?

Blough: Now, the only changes of any significance are these. In the first sentence "will be pleased to have an expression of your views as to any changes in our internal revenue tax laws that you consider might be helpful to business as well as equitable to taxpayers" - that wasn't in the old draft; and I have a copy of the old draft here if you would like to see it.

H.M.Jr: "....that might be helpful to business...." - that's new.

Blough: That's new.

H.M.Jr: That's all right. I think that's good, don't you?

Gaston: That makes the record check all the way through.

H.M.Jr: It's all right.

Blough: And aside from that, the fact that he in the last sentence in the first paragraph thought it might be well to indicate that he wasn't depending only on business and private individuals, so that he says - it's the first paragraph, last sentence - "Among the suggestions which have been most frequently made and which I, myself, have thought might be worthy of consideration are the following:" That's new.

H.M.Jr: Where does he say that?

Blough: Last sentence of the first paragraph.

Gaston: "....and which I, myself, have thought might be worthy of consideration...."

H.M.Jr: That's all right.

Blough: And the only other change was the next to the last sentence of the letter, top line on page 2, where he added "which might occur in any changes made," which is a purely textual change and has nothing to do with the sense.

H.M.Jr: The only part I don't like is this "It would be helpful to the Committee if you would present the arguments for and against as many of these suggestions as the Treasury has studied." Haven't we studied all of them? It's sort of....

Duffield: Well, that was in our draft because we didn't want to give - didn't want to assume that he knew what the Treasury had studied in advance. If we have studied all of them, well, that's fine.

Hanes: I'd like to put a period behind "suggested" up in the second sentence from the last in the first paragraph.

Blough: "....which have been suggested" - period?

Hanes: Yes.

Blough: He said he was quite willing to have that done. We specifically talked about that and he debated whether he thought it ought to be done and he said he was quite willing to do that.

H.M.Jr: (On phone, to Mrs. Klotz) You owe me those two tax books. - O. K.

What's that that Johnny Hanes wants?

Hanes: "Also, the Committee would be pleased...." - next to last sentence, first paragraph - "Also, the Committee would be pleased to have you give it the benefit of any information you have as to the desirability of various tax changes which have been suggested." Period. Then leave out....

H.M.Jr: What?

Hanes: ...."recently by business organizations and private individuals."

H.M.Jr: You think that might rub the President the wrong way?

Hanes: Yes, I do. Don't you? I mean I don't see any reason to rub it in.

(Mrs. Klotz comes in)

H.M.Jr: Well, the reason that....

Klotz: I'm sorry, I completely forgot about it.

Gaston: I like Mr. Hanes's suggestion.

H.M.Jr: I do too.

Blough: And may I say that Mr. Doughton discussed specifically

that passage and said he was quite willing to have that cut out.

H.M.Jr: How should it be? "Also, the Committee would be pleased to have you give it the benefit of any information you have as to the desirability of various tax changes which have been suggested."

Gaston: Period.

H.M.Jr: Suggested by whom?

Gaston: Anybody.

H.M.Jr: I see.

Gaston: Cut out that line, that next line.

H.M.Jr: All right, I think that's an improvement.

What else, Johnny?

Hanes: I don't see anything else wrong with it, Mr. Secretary. I think it's good.

White: One slight change which I take it you get the significance of.

H.M.Jr: What's that?

White: "....will be pleased to have an expression of your views...." Whether you would regard the discussion here as an expression of your views is a - you don't - you studiously avoid giving your opinion. Now, whether "views" is the same as opinion....

H.M.Jr: Well, I saw that and I'm going to leave it in and let the President strike it out.

Blough: Because, after all, the views do not tie up with these four or five specific items.

H.M.Jr: What do you mean?

Blough: I mean the sentence in which your views are asked does not relate specifically to the four or five items. You are asked - you are given general carte blanche to express your views and then he asks you

specifically for arguments for and against. So I think you're in the clear in any event.

H.M.Jr: Well, the way I feel is, I hope the President leaves it in. Isn't that what you meant? You're looking at it from the President's....

White: I'm looking at it from the point of view that he asked you - I thought you acquiesced in the fact that you weren't going to give your opinion as to the desirability or undesirability.

H.M.Jr: I also agreed I wasn't going to go up on the Hill and make a jackass out of myself.

White: Just calling attention to that.

H.M.Jr: I mean, after all, I am the Secretary of the Treasury and I'm not going to go up there and act like a - what do they call these things where you pull the strings?

White: Charlie McCarthy?

H.M.Jr: No, no.

Duffield: Marionettes.

H.M.Jr: Marionettes. Now, if the President wants to strike it out, all right. That stuck me in the eye, too.

White: Yes.

H.M.Jr: But you fellows put that in yourselves.

Blough: No, Mr. Doughton put that in. He sat down and wrote on it.

Gaston: When you discuss any proposition pro and con, you are of necessity giving your views as to that from both of those standpoints; those would be considerations you have to take in mind.

H.M.Jr: He used the word "views." The President may not like it, but you will agree it gives me much broader....

Blough: This is what you ought to be asked to do, may I say.

Gaston: A view is not a recommendation.

White: We understand the difference, Herbert. I mean it's there, it catches all our eyes.

H.M.Jr: Well, I hope we leave it in.

White: I mean he could justly say that "I'm giving my views here and not giving my opinion." You could legalistically take that position. It wouldn't change the position. I take it it doesn't change the content of this, because in this statement as it stands alone you do not give your opinion but you may be said to be giving some of your views.

Gaston: I don't recall that the discussion was about not giving his opinion. The discussion was about not making any tax recommendations to the Committee.

H.M.Jr: Well, I get Harry's point. I'm glad he brought it up. I hope that the President won't.

Now, you wouldn't say that among the specific suggestions - make it "Among the specific suggestions which have been frequently made...."

Blough: I think that would be an improvement.

H.M.Jr: I mean would that tie in? Is that necessary? See, he's asking....

White: I don't think so.

Gaston: I don't think it adds.

Hanes: I doubt it. I think I'd leave it.

H.M.Jr: Now, he finishes, again: "The Committee would, of course, be glad to hear your views on any other pertinent matters which you may wish to discuss." I don't see anything wrong with it. He doesn't say "recommendations," he says "views."

Let me put it this way. Supposing the President leaves it in. Would you be unhappy about it?

White: No, no, not at all.

H.M.Jr: Well, are we ready to call up Doughton? He asked me to call him back and tell him how I liked it, and I'll tell him we're just leaving out that one sentence. O. K.?

Hanes: Yes.

H.M.Jr: Everybody all right?

Gaston: Yes.

H.M.Jr: (On phone) Congressman Doughton, please.

Blough: He also said that he'd be glad to hear from you as soon as you have talked to the President about it.

White: Of course, even if the President should object, that paragraph which follows those specific taxes takes care of it. It says "It would be helpful if you would present the arguments for and against...." So really...

H.M.Jr: He's going to see me right after lunch on this. I asked for a 3:00 o'clock appointment. He said no, I was to continue right along through at 2:00.

(On phone) Hello. - Thank you. - Thank you. -

Can't find him.

Well now, let's just leave that. We all - everybody is happy on that? Johnny?

Hanes: Yes, sir.

H.M.Jr: Now I'm going to start reading and I'll read a paragraph and then we can - after I've read a paragraph we can go over it again, huh? Shall we go ahead?

"I am here this morning in response to Chairman Doughton's letter inviting me to present information relating to certain tax proposals and other pertinent matters.

"Tax proposals...." - Now, I'm not going to - for instance, I might like to say, on changes, "I am delighted to be here...." I'm not going to put that in now. In other words, the time is so short....

"Tax proposals cannot be discussed comprehensibly except in relationship to our broad national and fiscal position. We are now in the midst of a world situation which imposes on this Government a special responsibility. We must demonstrate that a democratic government has the power and the flexibility to survive a prolonged crisis and chaotic world conditions and yet emerge with the strength of its free institutions unimpaired."

Isn't this the same - isn't this all - but you haven't seen this, Johnny. Then I'll read it for your sake.

"Preservation of our democratic form of government over a long period of years requires, in my opinion, a fiscal program which has a fourfold objective: (1) Promotion of free enterprise and private investment; (2) Attainment of full business recovery; (3) Maintenance of our public finances in a sound and unassailable position, and (4) A just distribution of tax burdens and a more equitable distribution of national income." You'll have to....

Hanes: I've seen that paragraph there. I'd go back again to the same suggestion I made before; that is, for number 4: "A just distribution of tax burdens and national income."

H.M.Jr: Yes, but the President wrote this in. This is what he likes. I mean the way I feel, Johnny, is that some of these things....

Hanes: Well, don't stop too long on it. It isn't important.

H.M.Jr: All right. Well, this part here - the suggestions he made - some of them I thought were excellent, on others I'm willing to concur because - well, I just didn't think it was worth fighting about.

Hanes: It isn't important.

H.M.Jr: "Successful operation of democracy demands that all four objectives be solidly linked together. When we consider any specific change in our fiscal program we must satisfy ourselves that the change makes for a better and not a worse distribution of tax burdens and of national income, that the change promotes and does not retard business recovery, and that the change makes easier and not more difficult establishment of a balanced relationship between revenues and expenditures."

(On phone) Hello. (Conversation with Congressman Doughton follows:)

May 8, 1939
11:15 a.m.

HMJr: Hello.

Operator: She's going to locate Congressman Doughton and have him call you.

HMJr: Thank you.

O: You're welcome.

HMJr: Thank you.

11:18 a.m.

Operator: Go ahead.

HMJr: Hello.

Robert Doughton: Hello, Mr. Secretary.

HMJr: I think that your changes are all to the good.

D: Well, I appreciate that.

HMJr: Now, we've got just one little thing.

D: Well.....

HMJr: Have you got it before you -- the letter?

D: Yes, I'll have it here in a second.

HMJr: Well now, in the first paragraph..... Hello?

D: Yeah, I get you.

HMJr: Line -- let me see, one, two, three.....

D: How's that?

HMJr: The ninth line, beginning "Recently by business organization....." -- the ninth line.

D: Let's see, what line is that in?

HMJr: In the first paragraph.....

D: Yes.

HMJr: .....it starts, "Recently by business organizations and private individuals."

D: Yeah.

HMJr: Do you see that line?

D: Yeah.

HMJr: Well, we thought we'd strike that out if it had -- with your approval.

D: That will be perfectly all right.

HMJr: So that the previous sentence would read like this: "Also, the Committee would be pleased to have you give it the benefit of any information you have as to the desirability of various tax changes which have been suggested." See?

D: I see -- I get that.

HMJr: And then leaving out the next sentence -- those next words, "Recently by business organizations and private individuals." Just strike that out.

D: Yes.

HMJr: See?

D: That will be -- I think that's all right.
and myself discussed that and I told him I'd leave that entirely to you.

HMJr: Well.....

D: That was -- that was in your first draft, you know.

HMJr: I know it was.

D: Yes.

HMJr: And.....

D: I think that might -- I think

HMJr: That's right. Why -- why name them.

D: Well, all right. I'm glad you approve what little minor suggestions I made.

HMJr: Yes, we think they're all helpful.

D: Well, all right. Has Hanes gotten back?

HMJr: Yes, he sitting right next to me.

D: Uh-huh. Well, that's fine.

HMJr: And he thinks it's -- it's swell that you want....

D: How's that?

HMJr: He's delighted that -- this idea of your writing this letter.

D: Well, all right. I think -- I think it's a good start.

HMJr: No, he's delighted. He thinks that that's -- that's the way to do it.

D: Well, I'll see --

HMJr: Well, and when I come back from the White House, which will be oh.....

D: Yeah.

HMJr: .....three or four o'clock, I'll call you.

D: You give me a call then.

HMJr: I certainly will.

D: Thank you very much.

HMJr: Thank you.

D: Good bye.

H.M.Jr: I didn't overstate it, did I?

Hanes: (Nods no).

H.M.Jr: He wanted to know whether you were back.

(On phone) Tell Mrs. Klotz to send in somebody to type a letter for me.

I'll have it retyped.

I want to get this. Am I at "Full attainment"?

Hanes: "When we consider...."

H.M.Jr: "When we consider any specific change in our fiscal program we must satisfy ourselves that the change makes for a better and not a worse distribution of tax burdens and of national income, that the change promotes and does not retard business recovery, and that the change makes easier and not more difficult establishment of a balanced relationship between revenues and expenditures."

Bob (McHugh), write this over. Don't pay any attention to this. The only change is that you leave out this, put a period there. And I want this all on one page. Make three copies.

"Full attainment of these objectives is difficult at best. It is made more difficult by a new and ominous development in world affairs - the armament race now gripping the important nations of the world." And I know all that.

"For us the danger is that these developments may mean a necessarily increased cost for national defense here, together with monetary instability abroad, disruption of our foreign commerce, and perhaps other unsettlements, the consequences of which we cannot fully predict. In this connection, it is interesting to note that in our budget for this fiscal year expenditures for past wars and national defense are almost one-fourth of total expenditures."

The President made that change. I think it's better.

Hanes: That's a good change.

Duffield: The percentage is incorrect, though.

Blough: It's between 20 percent and 25.

H.M.Jr: Well, he says "almost one-fourth." Again, unless it's....

Hanes: You can say "a little over one-fifth."

Duffield: I mean that's a technicality. It's approximately correct.

Hanes: Close enough.

H.M.Jr: "No major problem facing this government today can be solved properly without full consideration of the position of this country in relation to the present international crisis. The unmistakable implication of the international situation is that we should look ahead to our future fiscal position and redouble our efforts to attain full recovery. High national income and a sound fiscal position are essential to adequate national defense. It is against this background that we reexamine our fiscal program."

Now, he reread this stuff, and I know the President has okayed this. I think it's swell, don't you?

Hanes: I do.

H.M.Jr: "A fundamental objective of sound finance clearly is a balanced budget. There is, of course, no good reason why taxes must exactly balance expenditures each year any more than each month, each week or each day. There are periods during which sound fiscal policy calls for an excess of outgo over income, and others when it calls for an excess of income over outgo. In a depression it is inevitable that there will be deficits. Revenues decline at the same time that the Federal Government is called upon to undertake inescapable social and economic burdens. If, however, deficits are too long continued, the depressive effects of uncertainty tend to make recovery more difficult. The sequel to

deficits in emergencies should be surpluses during years of prosperity. That was and is one of the broad purposes of seeking to raise the national income to a high level, thus assuring revenue great enough not only to end the deficits which began in 1931, but also to reduce the public debt."

I think that's all swell.

"In carrying out our fiscal policy it would be helpful to have machinery which would more fully coordinate our efforts. It is not the prerogative of any administrative department to make suggestions to the legislative branch of the government for the conduct of its work, but I am sure that you would wish me to be frank in suggesting ways of surmounting difficulties which I believe now attend the joint efforts of the Ways and Means and Finance Committees and the Treasury Department."

Blough: You may wish to compare that with the President's paragraph. It isn't quite the same but it has many of the same words in it.

H.M.Jr: Well....

Duffield: We tried to make it as nearly as we could....

H.M.Jr: It's close enough to suit me. I mean I'm trying to get down to the tax thing. And also, as I say, if it's close enough, he isn't going to - it's the thought that's there.

"If, for instance, the Ways and Means and Appropriations Committees of this House and the Finance and Appropriations Committees of the Senate...."

By the way, did you give this to Mr. Doughton?

Blough: I gave him a copy and he had gotten down to page 3 or 4 before I left.

H.M.Jr: You gave him this?

Blough: Not this. We didn't have this at that time. He has the one of last Saturday.

H.M.Jr: I hope you put a halo around it and told him.....

Blough: No, I didn't. I just made him feel as you did last night - last week. I expressed it very clearly to him.

H.M.Jr: No, no.

Blough: Oh, you mean about its being confidential.

H.M.Jr: Yes.

Blough: Yes, indeed. He emphasized it; he called in his two secretaries and said, "Not a word of this to anybody."

H.M.Jr: "The Budget Act of 1921 set up a procedure for the orderly formulation by the Executive of fiscal proposals and for their submission to the Congress as a unified budget. No comparable procedure has been set up in Congress for considering revenues and expenditures together as two interrelated aspects of a single problem. I hope this Committee will agree with me that some such innovation would improve the efficiency of the Government. By providing for a preliminary legislative consideration of the over-all picture of appropriation and revenue measures it would give Congress a broad perspective of the management of the Government's finances and permit a better ordered coordination between the executive and the legislative branches in this field."

Where did I say about - that this money that we spent was helpful, and I put in the word "maybe" it was helpful? Now, do I say that later?

Gaston: No, not unless....

H.M.Jr: Where do I say that? And the President said, "Why be so wishy-washy?"

Gaston: That was above here.

Blough: About the top of page 4.

H.M.Jr: Four.

White: You say "are" instead of "may be".

H.M.Jr: Where do I say it?

Duffield: It's at the bottom of page 3, the sentence which now reads "There are periods during which sound fiscal policy calls for an excess of outgo over income...." That sentence went over to the White House reading "There may be periods...."

H.M.Jr: Johnny, the bottom of page 3 - "There are periods during which sould fiscal policy calls for an excess of outgo over income...." Does that shock you?

Hanes: No, it's obvious. It's all right.

H.M.Jr: You say it's obvious. I said there that "there may be...." and the President said, "Why be so wishy-washy about it?"

Hanes: That's all right.

H.M.Jr: This next thing we had on page 5 - we said something about this being the funnel. The President gets in the word "lens."

"This Joint Committee would in effect be a lens through which all appropriation and revenue measures could be viewed in relationship to both what the nation needs and what the nation can afford."

I think that's swell, don't you?

Hanes: Yes.

H.M.Jr: "This Committee could have continuous life for the purpose of actively studying fiscal problems between as well as during sessions of Congress. The Treasury Department would, of course, cooperate fully in this work to the extent that the Committee desired.

"Thus far I have dealt with the financial problems of the Federal Government alone. We must remember, however, that even if we had in operation the best conceivable Federal fiscal plan, we still would have touched less than half of the tax problem which

confronts the nation. Almost sixty percent of the total tax revenues of the country are collected by State and local governments."

Haven't you upped me on that?

Blough: Ten percent.

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

Blough: The facts are correct, however, as stated here.

H.M.Jr: Better give it quickly, otherwise it will be up another ten percent.

"We have talked about removing injurious Federal-State tax conflicts for the past five years. Our predecessors talked about the same problem. I recommend that Congress create a small temporary national commission to report to Congress as soon as feasible on the various aspects of most desirable intergovernmental fiscal policy." Well, that's all about the same.

"Overlapping taxes have grown in number and size as both Federal and State governments have sought new revenue. Grants-in-aid are being demanded of the Federal Government in increasing amounts. The results of our fiscal situation are increasingly unsatisfactory to both the State Government and the Federal Government, and more and more burdensome to many taxpayers."

Blough: This is the same.

H.M.Jr: This is where I want to get down....

"The findings of such a commission should assist us in achieving a more orderly relationship between the Federal, State and local fiscal systems."

Now - "Thus far I have talked about two broad fiscal matters of great importance to the Treasury. Let me turn now to questions of taxation.

"I desire first to reiterate a number of recommendations for tax changes which have previously been presented to you."

This is the President's from here - this is the way he wanted me to do it, you see.

"In his budget message of January 3, 1939, the President recommended that Congress extend the miscellaneous internal revenue taxes which under existing law will expire next June and July, and to maintain the current rates of those taxes which otherwise would be reduced in June.

"2. In his message of January 19, 1939, the President recommended legislation making all government salaries hereafter earned and all interest on government securities hereafter issued subject to Federal and State income tax laws. That part of this recommendation dealing with government salaries, I am pleased to note, has already been incorporated into law.

"3. In my statement of March 24, 1939, I presented for your consideration four alternative rate plans for old-age insurance contributions during the next three years.

"4. The Treasury Department has pointed out from time to time that the present law allows excessive deductions for depletion of oil and gas wells and certain mines. Removing this inequitable special privilege would produce a substantial amount of revenue."

Want to say anything at this point?

Hanes: No.

H.M.Jr: "It seems impractical at this late date for Congress at this session to undertake any comprehensive reexamination of the tax laws. Moreover, before undertaking any broad revision it would be desirable to have the report of the proposed special committee on the fiscal relations of the Federal and State governments."

Now, you get the significance of this, Johnny. What?

Hanes: Did he put that paragraph in?

H.M.Jr: Yes.

"With regard, however, to the specific items mentioned in Chairman Doughton's letter, I am glad to present for your consideration a summary of the findings of the Treasury staff. Before commenting on them, I wish to emphasize the importance of the statement in the Chairman's letter - 'A fundamental prerequisite of any tax revision at this time is maintenance of the present revenue.'"

Just a second. Why did somebody give me these? Oh, that's a different - I see. Just a second. Let me just see what he did say.

Blough: He hasn't said it yet. He was going to. Here's another copy. You're looking for what Doughton said?

H.M.Jr: No, I'm looking for what the President said.

Blough: Oh, I'm sorry.

H.M.Jr: He said "It seems physically impossible at this session of Congress to rewrite the tax laws before the special study committee has conferred with States and municipalities and brings in a report."

Hanes: I like that better than I do this.

H.M.Jr: Well, these boys didn't put in what I told them.

Duffield: Remember, we discussed that in here on Saturday. We discussed that whole sentence, and this is the way it came out.

H.M.Jr: I see.

Hanes: I think this would be a deterrent right here.

H.M.Jr: Yes.

Hanes: The way it's written.

H.M.Jr: It says here "It seems physically impossible at this session of Congress to rewrite the tax laws before the special study committee has conferred with States and municipalities and brings in a report."

Blough: What does that mean? We couldn't figure out what he meant; at least, I couldn't.

Hanes: It seems clear to me.

Gaston: I think the way we've got it here is a much better expression of the thought.

Hanes: That would be - careful reading of this paragraph certainly leaves a definite impression on my mind that you're asking them not to undertake any re-examination of the tax laws, and that's just what we are asking them to do.

Gaston: Well, I think it is rather stronger the way the President's draft read.

Hanes: I don't believe it is, Herbert.

Gaston: It says "....physically impossible...."

H.M.Jr: "....at this session of Congress to rewrite the tax laws before the special study committee has conferred with States and municipalities and brings in a report."

That refers, then, just to the overlapping taxes, the way he's got it. The way you've got it, it applies to the whole business.

Duffield: May I make a suggestion for a change? It would read: "It seems impractical for Congress to undertake any comprehensive revision of the tax laws before receiving the report of the proposed...."

H.M.Jr: I'd do it just the way he has it.

Duffield: That, I think, would do it.

H.M.Jr: Who's doing this stuff? The time is so short, and if you do it the way the President did it - who can do this page and have it back to me?

Blough: I'll have my girl....

H.M.Jr: Who do you want, Blough, to come?

Blough: Get Miss Humphries in here, then.

H.M.Jr: (On phone) Tell Miss Humphries to come in here, please.

Can't you do it just the way I took it down in the President's own language? The way I get it, I take it what he's saying is "It seems physically impossible at this session of Congress to rewrite the tax laws before the special study committee has conferred with States and municipalities and brings in a report" - that that's just as to the overlapping taxes, and doesn't mean we can't go ahead with the other.

Hanes: That's the way I get it.

H.M.Jr: That's the way I get it too. I just would change that.

And you can only do it - then "With regard, however, to the specific items mentioned in Chairman Doughton's letter, I am glad to present for your consideration a summary of the findings of the Treasury staff."

Duffield: Would this make it....

H.M.Jr: No, I'd do it - please, Gene.

Duffield: But "physically impossible," Mr. Secretary - it just doesn't make sense. We've got to get another synonym for that phrase.

Gaston: If you're referring only to an agreement with the States, of course, it is physically impossible.

H.M.Jr: Well, that's the way....

Hanes: That's what it is. That's why I like it. It refers to those overlapping taxes.

H.M.Jr: It is physically impossible to do it until these fellows bring it in, and he didn't say anything else; and what is physically impossible is only to do it - only as applies to the overlapping taxes. Now, he didn't include the other thing. And the way it's written here is - what you're saying is that you can't have a tax bill. I think it's terrifically important.

Blough: Well, I hope that's the way he meant it, but in view of the fact he put the recommendations in

first and then this....

H.M.Jr: Well, I'm going to take it that way. I mean I wrote down word for word what he said. Now, if I use word for word what he said, he certainly can't complain.

Blough: We have a sheet to be rewritten.

(Miss Humphries comes in)

H.M.Jr: Miss Humphries, take page 8, will you please? Sit down, Miss Humphries. Page 8. Now, in the middle of the page, that paragraph which said "It seems impractical at this late date...."

Humphries: Yes, sir.

H.M.Jr: I want that paragraph changed, you see, and I want it just the way the President said it. And please keep this thing now on page 8 - I mean I haven't got time - I mean what you come back with will have to be page 8; if it's a short page, all right. But I want it the way he wrote it. In place of that paragraph "It seems impractical...." I want to say "It seems physically impossible at this session of Congress to rewrite the tax laws before the special study committee has conferred with the States and municipalities...." - would you say "before the"?

Duffield: "....and brought in a report."

H.M.Jr: Would you say "the proposed"?

Hanes: "....on the fiscal relations of the Federal and State governments"?

H.M.Jr: Would you say "brings in a report"? And "....special study committee...." - would you say "proposed special study committee"?

Gaston: "....special study committee which I am suggesting...."

H.M.Jr: What?

Gaston: "....special study committee which I am suggesting...."

H.M.Jr: I think I'd just take it the way he's got it, then we can do it.... Miss Humphries, let me just give it to you exactly the way he has it, and if there's one word or so afterwards....

"It seems physically impossible at this session of Congress to rewrite the tax laws before the special study committee has conferred with the States and municipalities and brings in a report."

Now, that takes the place of that.

Humphries: All right, sir.

H.M.Jr: And would you go out - and then I'll get a new page 8, you see, and if you could start somebody on it and be ready - have you got enough help back there?

Humphries: Yes.

H.M.Jr: Got enough help?

Blough: We'll get it.

Gaston: This is a matter of tense; it should be "has conferred and brought in a report."

H.M.Jr: Herbert, this is terrifically important. Johnny is right. The way it is there would completely shut it off. The way the President says it, that at this late date in this session we can't take up the report of this committee, the committee has only to do with the States and municipalities. Now, having said that, we say: "With regard, however, to the specific items mentioned in Chairman Doughton's letter, I am glad to present for your consideration a summary of the findings of the Treasury staff."

You people evidently don't think it makes sense.

Duffield: You don't want to hear our argument, do you?

H.M.Jr: No.

Gaston: I think they broadened out the statement to what they thought the President intended, but it is possible

to interpret the President's statement in the way you do, which is fine.

Blough: I certainly hope the President wanted you to say just what you said.

H.M.Jr: As I say, nine times out of ten, I do want to hear; this is the tenth time, and I don't. It makes life easier, I think, for both you and me.

Now, where was I?

Hanes: "With regard...."

Blough: "With regard, however,...."

H.M.Jr: "With regard, however, to the specific items mentioned in Chairman Doughton's letter, I am glad to present for your consideration a summary of the findings of the Treasury staff. Before commenting on them, I wish to emphasize the importance of the statement in the Chairman's letter that 'a fundamental prerequisite of any tax revision at this time is maintenance of the present revenue.'"

(Mrs. Klotz comes in after having been out for a few minutes)

Hello.

Klotz: Hello.

H.M.Jr: Going to join us?

Klotz: Yes.

H.M.Jr: "We must not forget that one of the important objectives of our fiscal program is to approach a balance between revenues and expenditures."

Hanes: Where is that?

Gaston: On 9.

Hanes: Yes.

Gaston: Second sentence.

H.M.Jr: (Reads silently for brief period).

Put in here - I won't put it in today, I haven't got time - right there an insert, you see, of what I have written. You can type this out for the men, and this is the place where it would go. "Every item of expenditure should be carefully scrutinized and as our outlay for rearmament increases and puts additional men to work we could well afford to curtail other forms of public works."

What do you people think of that? Do you think it's dangerous, tying it up?

Hanes: Afraid they might tie up the armament program with the pump-priming one, which would be bad.

H.M.Jr: Well, I've got this as a result of reading Keynes's most recent statement that everybody is so excited about.

What do you think, Harry?

White: I like the idea. Probably might rephrase it a little bit differently to avoid....

H.M.Jr: Well, anyway....

White: I like the first part of it.

Hanes: You're going to put that in instead?

H.M.Jr: No, in addition, to supplement it. But that's where it would go.

Hanes: I have some general suggestions on that page. I don't know if you want them now. We can correct it later. But I want to take out these - "We must do this" and say "I hope we will...."

H.M.Jr: That's all right, but what I want you to do on this thing - I want everybody - if there is some big glaring policy thing like this other thing you caught, see? On the question of emphasis of words or kind of words we still have another chance.

Hanes: We can always change that later.

H.M.Jr: Have you got that new page 8?

Blough: It's not back yet.

Humphries: It's coming.

H.M.Jr: "We must not forget that one of the important objectives of our fiscal program is to approach a balance between revenues and expenditures. For this reason any tax reductions must of necessity be offset by tax increases elsewhere. I wish to emphasize that in my opinion we should under no circumstances weaken the revenue-producing capacity of our tax structure. I regard this as the keystone of any program of tax revision that may be undertaken at this session. If tax revision were confined to tax reduction, the resulting uncertainty over our fiscal policy would injure and not help business. We must take no step which the public may interpret as moving away from the objective of a balanced budget."

This is all new, isn't it?

Duffield: No.

Blough: There may be a slight expansion there because the President had asked for a whole page on it; but this was all in.

Duffield: The language was some place in the statement.

H.M.Jr: Well, I agree with Hanes that it's too emphatic, but I'm not going to take the time now.

"I turn now to a brief summary of the arguments for and against the specific tax suggestions which Chairman Doughton asked me to discuss with you:

"1. The first item on Chairman Doughton's list is the suggestion that the capital stock and excess-profits taxes be repealed."

I think the President is going to like this approach.

"The first item on Chairman Doughton's list...." - this is so much better. The way we had it before, I was sick - the way we had it before. Doesn't everybody like this?

Duffield: Yes.

H.M.Jr: Anbody? Harry?

White: Much better.

H.M.Jr: "Under the present law the capital stock tax is based upon a declared capital stock value which the taxpayer may revise every three years."

Is that the way it is now?

Blough: That's correct.

H.M.Jr: What?

Blough: That's right.

H.M.Jr: "The declared value may be any figure that the taxpayer desires to submit, regardless of the actual value of the stock. The excess-profits tax applies to profits in excess of ten percent of such a declared value. The taxes are thus not really taxes on the value of capital stock or on excessive profits. The reason for the present form of the taxes is the difficulty of administering true capital stock and excess-profits taxes."

Does anybody want to say anything on that?

"(a) The major defect of these two taxes is that they operate very erratically. The tax liability they impose depends on the taxpayer's ability to forecast profits for the next three years, as well as upon the amount of profits actually realized during each of the three years. The closer declared value turned out to be ten times average earnings...." and so forth and so on. Well, that's all right as far as I'm concerned. All right? Anybody?

Hanes: Yes.

H.M.Jr: "(b) The uncertainty of the capital stock and excess-profits taxes is irritating and may thus be a business deterrent."

"....and may thus be a business deterrent"? Well, all right.

"Forecasts of earnings are particularly difficult to make in the case of new businesses and those with unstable incomes, such as the capital goods industries, with the result that taxes imposed on such businesses are at times inordinately high.

"Against the proposal are the following considerations:

"(a) Repeal of the taxes would result in a substantial loss of revenue. For a year with business conditions similar to 1939 it is estimated that the loss would be $125,000,000.

"(b) If the taxes were repealed, corporations without profits would be altogether free from taxes applicable only to corporations. At present deficit corporations declare a capital stock value, and are thus required to pay some tax, although in many cases the tax is of insignificant size. There is much to be said for the position that all corporations should contribute to meet the cost of government whether or not they make profits.

"(c) Rather than repeal these taxes they could be revised and made to apply to actual capital value and excessive profits. Such taxes, if successfully developed, could serve as the basis for special profits taxes necessitated by war."

Duffield: That paragraph is new.

Blough: Yes, it's new.

White: We were very dubious about the second sentence in that.

Blough: Yes.

White: Might scare them.

H.M.Jr: I hate to talk about taxes "necessitated by war."

Duffield: We had a good many....

Hanes: I'd leave that paragraph out.

White: It could easily come out.

Blough: Take the whole paragraph out, for that matter.

White: No, take the second part out.

Hanes: Take the whole paragraph out. I don't think it adds anything.

H.M.Jr: I don't like it.

White: What part's coming out?

H.M.Jr: The whole of it. I want to be perfectly frank with you gentlemen, the way I try always to be. I want to leave the impression with my hearers that I am for the changing of these five taxes.

Blough: Well, that was something that we didn't really - we weren't really sure of. We debated that among ourselves.

Duffield: I got worried yesterday for fear we were doing too much of that, not knowing what we were supposed to do.

H.M.Jr: I want to be an advocate....

Blough: Then we ought to redo these.

Gaston: In that light, I'd limit these to (a) and (b) and I'd cut (b) at the end of the first sentence - "If the taxes were repealed, corporations without profits would be altogether free from taxes applicable only to corporations."

White: We fought over many of these words. My position is this: These taxes - these tax changes have

merits, they can stand on their own feet on their merits. It is not necessary to ignore just arguments on both sides or to attempt by your phraseology to bias your position; that if these taxes are as undesirable as people hold them to be, then these proposals ought to be able to stand on their own feet. I don't think in these pros and cons there ought to creep in any too obvious bias.

H.M.Jr: That's perfectly true, but on the other hand when I get through I want the people to say, "Well, where does Morgenthau stand on this thing?" And I want to leave the impression in their minds that I want these changes.

Gaston: In reading this over hastily I got the impression that you were setting these things all up and then knocking them all down.

White: You mean that the arguments, whether or not sound - you ought to eliminate them?

Gaston: No, I don't mean that at all, but I mean that the argument is too strong on the negative here and it gives the net effect of knocking down the suggestions. And I think in this one here I would just say (a) and (b) and (b) down to the word "corporations."

H.M.Jr: Now, what page are you on?

Gaston: Page 11, at the bottom of the page. Argument (a) is that we lose revenue. Argument (b) is that it would leave non-profit corporations free of taxes. That's all there is to it.

Duffield: You see, Mr. Gaston, what you're doing there - you're giving some little argument in support of both of your points pro and no arguments in support of both of your points con.

White: You're being dishonest.

Duffield: You are, I am afraid, a little bit too obviously loading the dice, so obviously that we might get in trouble.

H.M.Jr: You fellows worked on this yesterday?

White: Oh yes - everyone we fought over.

H.M.Jr: When did you work on this yesterday?

Blough: I worked all day, and they worked about three hours.

White: I think this (c) could come out without exposing yourself to that claim. I don't think that applies to the second - not to the second paragraph, second sentence.

Duffield: I agree to take out (c).

Blough: May I say this, that the previous draft under (b) would have left out the last sentence, but not the next to the last sentence.

H.M.Jr: I think "If the taxes were repealed, corporations without profits would be altogether free from taxes applicable only to corporations" - what? Stop there, Johnny?

Hanes: Down at the bottom of the page - "At present deficit corporations declare a capital stock value, and are thus required to pay some tax." Period. That's where I would stop.

H.M.Jr: Herbert?

Gaston: Yes.

H.M.Jr: You wanted - you were going to stop before that.

Gaston: Well, that's all right. It's no different where Johnny stops. I would certainly cut out (c).

Hanes: You're stating the fact that the deficit corporations do have to pay a tax.

Blough: Although a very little one in many cases.

White: Don't want to mention that.

Hanes: Some of them - it's damned significant to some of them.

H.M.Jr: Well, within this room only, I'm going to get away with just as much murder on this as I can; I don't care who knows it.

White: I'll fight on every point I think is important. You can overrule me.

H.M.Jr: I want you to. Definitely. I mean not fight....

White: I mean I'll....

H.M.Jr: Present your views.

White: I'll present my position.

H.M.Jr: Well now, Harry, do you think the beginning of page 12 should be on there?

White: Well, I think it's desirable to stop at "corporations" rather than at "pay some tax," because as it is now that last sentence there would hardly belong in the cons, but in the pros.

H.M.Jr: Where would you start?

White: My first preference would be "of insignificant size." But my second preference is in line with what you want to do. I think I'd stop at where Herbert suggested, at the end of "corporations."

H.M.Jr: Have it "altogether free from taxes applicable to corporations." Stop there?

White: That would be my preference, but I don't feel strongly.

H.M.Jr: Well, I don't care. Which way do you want it, Johnny?

Hanes: I don't really care. I think it just states the fact if we continue down to the bottom of the page. It makes a little longer reading. I don't think it makes an awful lot of difference.

H.M.Jr: Herbert Gaston?

Gaston: Well, I think it's all right to stop at the bottom of the page.

H.M.Jr: Blough?

Blough: I'm willing to stop at "pay some tax," although I think your pro case is stronger if you indicate the tax is of insignificant size. But either way is all right.

H.M.Jr: Gene?

Duffield: Bottom of the page is all right with me.

H.M.Jr: I'm for the bottom of the page. It will mean you don't have to rewrite one page.

Blough: Would you like to have page 12 rewritten now?

Duffield: Wait, there may be some more on it.

H.M.Jr: Wait a minute, Miss Humphries. She's doing fine. She isn't nervous yet. Are you?

Humphries: I'm all right.

H.M.Jr: Now we're going to take off the top of page 12.

Now we're coming to "2. The second item on which Chairman Doughton asked me to comment is the suggestion that net losses of business, both individual and corporate...." - I like that so much better than before, with the pros and cons. This is swell. Who had this idea of Doughton's writing a letter?

Duffield: You did.

H.M.Jr: All right.

Blough: You did; it was your idea.

H.M.Jr: I didn't know whether by today Harry thought it was his idea.

White: I need about a week for that.

H.M.Jr: The great thing is, though, to get the President to think it's his idea.

Hanes: That's the real trick.

H.M.Jr: "The second item on which Chairman Doughton asked me to comment is the suggestion that net losses of business, both individual and corporate, incurred in one year be offset against the income of subsequent years. At present, individuals and corporations are taxed on their annual income without deduction for losses incurred in prior years.

"In favor of the proposal are the following considerations:

"(a) Allowing the carry-forward of business losses would make taxable income coincide more nearly with actual income over a period of seven years."

Well now, that's all right. I think you can do over 12. All right, Johnny?

Hanes: Yes, sir.

H.M.Jr: Anything on 12?

Humphries: Leave out the first paragraph and leave out (c).

H.M.Jr: Is that somebody else's?

Humphries: I can give this to them.

H.M.Jr: "Businesses with alternating income and loss now pay higher taxes over a period of several years than do those with stable income. Many pay income taxes in single years of net income even though over a period of years they have had no net income or have suffered a net loss."

Blough: Now, we had an illustration in there which we cut out along the lines of not overemphasizing the pros, but which we could put back in again.

H.M.Jr: Let's have it.

Duffield: Then do you want to put any illustrations under the cons, because there are illustrations for the cons?

Hanes: No.

H.M.Jr: What? Leave it alone.

Hanes: Leave it alone.

H.M.Jr: What did you say?

Hanes: I'd leave it alone.

White: Yet, I feel that if you men feel there is such a strong case for this you can be very unbiased in the presentation.

Blough: There is this to be said. A good debater can make a bad case look good.

H.M.Jr: I don't want to be unbiased either. I've got a formula which is laid down and I want to live just within the formula.

Blough: We can do a better job than this with that in mind. We were trying to make it pretty well....

H.M.Jr: Well, all right. I've been honest enough.

Duffield: Are we to put the example in?

Blough: No.

H.M.Jr: "Businesses with alternating income...." - where were we, at (c)?

Blough: Yes.

H.M.Jr: "Allowing the carry-forward of business losses would somewhat increase the incentive to new enterprises and to the expansion of the capital goods industries, which are subject to wide fluctuations in earnings.

"(c) Allowing a loss carry-forward would reduce the administrative difficulties caused by the taxpayers' efforts to shift items of income into loss years.

"However, the proposed carry-over of business losses would also have disadvantages:

"(a) In the first place, it would result in a substantial loss in revenue."

Now, before we get off 13, anything?

Gaston: Well, I would change that introduction to the disadvantages somewhat so as to make it less emphatic.

Hanes: I would too.

Gaston: I'd say "The disadvantages that would have to be considered in connection with the proposed carry-over are these:"

H.M.Jr: Write it on a piece of paper, Herbert. Here, write it out, please.

What are we waiting for?

Gaston: There you are.

H.M.Jr: "The disadvantages that would need to be considered in connection with the proposed carry-over of business losses are these:" Is that right? That would be in place of....

Gaston: "However, the proposed carry-over of business losses would also have disadvantages:"

White: That's all right.

Gaston: The point is that you're just considering advantages and disadvantages. Here you're saying "However, there are disadvantages," seeming to argue against it.

White: We tried to vary the language slightly, but that's all right.

H.M.Jr: "In the first place, it would result in a substantial loss of revenue."

Hanes: Leave out "substantial"?

White: Did you notice the figure?

H.M.Jr: How big is the figure?

Hanes: I don't know how big those figures are.

Gaston: Twenty-five million to two hundred million, depending on the characteristics of the business year, they have here.

White: We can leave it out.

Hanes: Isn't it time to build a case on the fact that these deterrents - their elimination is going to increase the flow of business enterprise; if it does do it, there will be no decrease in revenue, and if it doesn't do it it doesn't make any difference.

Blough: "....result in a loss in revenue."

H.M.Jr: "....result in a loss of revenue."

I am now on top of page 14.

Gaston: I don't know that, in line with Johnny's suggestion - I don't know that we ought to make a flat statement that it will result in a loss of revenue. "(a) Unless this change should result in a substantial increase in business, there would be a loss in revenue."

H.M.Jr: Wait a minute.

Blough: Wait, Miss Humphries.

H.M.Jr: What would you say? I haven't got it. Let me see page 13.

Gaston: I'd say "(a) Unless the change should result in a substantial increase in business activity, there would be loss of revenue."

H.M.Jr: Well now, are we going to introduce that all the way through? Are you going to say that....

White: Have to use that on every single one of them.

H.M.Jr: I mean that's the philosophy....

Gaston: Well, that's true.

H.M.Jr: Are you going to say that in every case?

Gaston: But here we're making a flat statement that it would result in a loss of revenue.

H.M.Jr: Well, wouldn't it?

Gaston: Other conditions remaining the same.

H.M.Jr: Isn't this whole thing presented on the basis of the business of '38 or '37 or '36?

Gaston: Then if that's true, I think somewhere you should introduce into the statement about these things that if the changes should result in a great increase in business, these revenue losses might be offset.

H.M.Jr: Now, Herbert, we haven't said that anywhere. If you want to say that that's got to go in the thing, it's got to go in the beginning. That's the difference between Mr. Hanes and myself on this thing.

Gaston: It doesn't seem to me that we can discuss all these proposed changes without taking into consideration the reason for advocating the changes. And what is that reason? That an apparent - an initial loss in revenue may result in a stimulus to business.

H.M.Jr: An initial loss? But, Herbert, you come out here flat-footed - I mean I'm amazed at your bringing it up at the eleventh hour; we've been over this thing five times. I mean you're going to change the whole philosophy of this thing.

Gaston: No, no.

H.M.Jr: It changes the whole thing. He's told me to start and finish with the statement that we mustn't lose any revenue. Now, are you going to bring in this business that if you cut the thing - you're going to cut it and then gamble on making it back? That's what Hanes said. I mean I don't want to argue now about whether he is right or wrong, but that's what Hanes said and I said I didn't want to take that position. We've been perfectly fair. I mean his philosophy - I don't like to interpret it for him - is to cut the thing and gamble on recovery, don't ask for any increased revenue. Now, the President, the Speaker and Doughton have all said they want

dollar for dollar. These other people have talked to me and said that as Secretary of the Treasury I must take that position. I mean we've been over this thing I don't know how many times. Am I - please.....

Blough: You're absolutely right in your statement. It's completely consistent with your previous position right down the line.

H.M.Jr: Don't "yes" me.

Blough: I wouldn't do that, Mr. Secretary.

H.M.Jr: Of course, Gaston hasn't been in on all these discussions, so maybe he hasn't heard me.

Hanes: Neither have I. I've heard very little of it.

H.M.Jr: What?

Hanes: I say I haven't been in on many of them, haven't heard much about it. But that appeals to me. You know my position on that.

H.M.Jr: And you know mine, and I don't feel, right or wrong - I mean that I want to go over there now and - because then I might as well take the whole thing and throw it out, because I can't get away with that. I mean here's the President, the Speaker and Doughton, entirely each one on their own, saying, "dollar for dollar." That's the basis for the whole thing.

Gaston: I think that's right. I would agree to that.

H.M.Jr: Well, how do the two things gee?

Gaston: But still I think that there ought to be some recognition in here of the possibility that some of these changes will result in a stimulus to business which in itself may bring more revenue.

Blough: I think that's quite correct, that we have not put in a clause or phrase which could have been put in each of these revenue figures, saying, as we have in certain cases, "At certain levels of business this would be the case." Now on this particular one we didn't use a particular level of business but a

range of loss depending on a variety of business levels.

Gaston: I think that would solve the thing, just to say "At any given level of business this would result in a loss of revenue."

H.M.Jr: You say it: "$25,000,000 to $200,000,000 depending upon the business conditions of the year and the three preceding years."

Gaston: Well, that's in that one sentence right there. I'd say in the first place that it will result at a given level of business in a loss of revenue.

Blough: That's on page 13.

H.M.Jr: No, on page 14.

Gaston: I'm speaking about the last paragraph on 13.

H.M.Jr: Well, leave out that sentence entirely. I'm willing to do that.

Gaston: Oh, we're citing them the main disadvantage of all of these things; they mean, on any certain level of business, a loss in revenue.

H.M.Jr: No, I'm willing to leave that sentence out entirely. Why assume that? I'm willing to say that I - I'm not going to assume - I'll meet you that much.

Gaston: That's the main argument against the carry-over, that you would lose revenue, have to have some tax ....

H.M.Jr: Suppose I read this. "Assuming that the carry-forward provision was not made retroactive and that the law applied first to 1940, there would be no revenue loss until the fiscal year 1942, after which the loss would increase over the number of years required to reach full application. For example, in a year of full application it is estimated that the revenue loss from a three-year carry-forward provision would vary between $25,000,000 and $200,000,000, depending on the business conditions of the year and the three preceding years."

Now, you wouldn't object to that change. I'd leave off the sentence "In the first place it would result...." In other words, I won't lay down a dictum.

Hanes: You're saying flat-footedly that this is going to result in a loss of revenue. I don't believe that.

H.M.Jr: I'll meet you half way by saying nothing.

Hanes: I go along with that. I want to tell the truth so long as it doesn't hurt us too much.

Gaston: This doesn't carry it. I think you've got to say that at a given level of business there will be a loss.

H.M.Jr: I'm sorry, gentlemen, I've got 45 minutes and I've got to take this thing over to the President. We're not through.

Gaston: I'd say let it stand as it is.

H.M.Jr: No, I won't, I'll leave off (a).

Gaston: The paragraph isn't complete without it.

H.M.Jr: I can't help it; it's the idea.

Hanes: We can change the wording; it isn't so very vital.

H.M.Jr: Leave it off.

Blough: What is the decision on that, please?

H.M.Jr: Leave off "In the first place, it would result in a substantial loss in revenue."

Blough: Begin on top of page 14.

H.M.Jr: Yes. Wait a minute. Blough, does that not make sense to you?

Blough: I think it would be sounder to take Mr. Gaston's view that in the first place it would result in a loss in revenue at any given level of business. That's really what we're saying. We're not saying

business will go up or business will go down, but we're saying that at a given level of business there would be a revenue loss. Now, if business goes up, why, then of course we're money ahead. We may be....

H.M.Jr: How am I going to get through this thing? I don't know whose fault it is that Gaston wasn't with you yesterday. It isn't mine. I mean to have all these arguments in front of me - it's pretty tough on me.

Blough: Yes, I'm very sorry.

Hanes: I'd leave it off for the time being. Then we can rephrase it to make a complete sentence out of it so it doesn't change the sense.

Blough: I'm entirely willing to do that. I think the thing will carry without that sentence, but it would be better to have one there.

H.M.Jr: Oh, I'm just desperate. I'm sorry. It's pretty tough to have to work like this.

White: I have one suggestion that might simplify it.

H.M.Jr: What?

White: I have a simple suggestion, that instead of leaving that out, saying "In the first place, it might result...." Use the word "might" instead of "would." It might satisfy everybody.

H.M.Jr: "....it might result...."

White: "Might" instead of "would."

H.M.Jr: "Might" instead of what?

Duffield: "....might result in a loss of revenue."

White: Since you go on to explain it.

H.M.Jr: That doesn't satisfy Hanes.

Hanes: That's all right. I don't think it's terribly important, Henry. I'd leave it off for the time

being. It doesn't change the sense. You're stating the facts in the next paragraph. It doesn't change the sense to leave it off. If it doesn't read smoothly, why, we can change it.

H.M.Jr: All right.

Now, (b) - "It would complicate the mechanics of administering the income tax."

Blough: It's not a very important one, I'm going to say.

Duffield: We just said up above that it would simplify it.

Blough: It does both. But I don't think this is important enough, in view of the fact you wanted to load it on the pro side; I'd cut (b) out.

H.M.Jr: "Allowing a loss carry-forward would benefit many businesses while relatively few might be stimulated to expand their activities as a consequence of carry-forward privilege."

Duffield: Harry will have to argue that one.

Hanes: I'd leave that out.

H.M.Jr: You'd leave what out?

Hanes: (c).

White: It's very definitely true. You can leave it out, but you're doing so.... The stimulating effect applies to a very small proportion of the total number of businesses that would benefit by it.

Hanes: We're trying to induce others to go into business. That's what we're trying to do.

White: Yes, businesses that haven't lost any money, are not likely to lose it. Most businesses wouldn't....

Hanes: The history is that they all do lose in the first five years. Those will be the ones encouraged to take a chance.

Blough: I'm with Mr. Hanes on number (c) for this reason.

H.M.Jr: All right, it's enough. Now, (c) is out, (b) is out.

"The third item on your Chairman's list is the suggestion that corporations be allowed to deduct their net capital losses in full from their ordinary incomes. Under the present law an excess of corporate capital losses over capital gains can be deducted from ordinary income only to the extent of $2,000."

Anything wrong on 14? All right.

"In favor of this proposal, the following considerations may be advanced:

"(a) Allowing corporate net capital losses to be deducted in full from ordinary income would make taxable income coincide more nearly with the income from the total operations of the corporation. At present net capital gains are always taken into account in tax computations while net capital losses in excess of $2,000 cannot be recognized. As a result a corporation may be obliged to pay an income tax in a year when its income from other sources was wiped out by capital losses."

Blough: I think we could strengthen (b).

Duffield: Let's don't at this time.

Blough: No.

Duffield: I mean we'll do it when it comes back.

Blough: Yes.

H.M.Jr: Anything on (a)?

"(b) Allowing the deduction of corporate net capital losses from other income might add to investments since corporations would have greater incentive to invest in the securities of other corporations or to launch new ventures of their own."

Blough: It's a weak statement which could be strengthened.

H.M.Jr: It's a very weak statement.

Blough: Instead of "might" we could say "would tend to add to investments" or "would operate to encourage investments" or "would encourage investments."

H.M.Jr: The President won't like that anyway. "....incentive to invest in the securities of other corporations ...." Must you say (b)? It will rub him the wrong way.

Blough: Well, that's where a good deal of the business incentive is supposed to be found.

White: That's the truth that lies in the recommendation. You see, many of these suggestions - the more closely you examine them the more tenuous becomes their connection with expansion.

H.M.Jr: All right.

"Against the proposal are the following considerations:

"(a) The allowance of the full deduction of corporate net capital losses from other income would result in a serious revenue shrinkage in years of declining prices for securities and other property. Normally, these are the years when the need for revenue is most acute. It is estimated that on the basis of calendar year 1939 levels of business the revenue loss might be approximately $70,000,000.

"(b) Corporations that hold securities could reduce their taxable income and thus minimize their tax liability by selling those securities which had declined in value."

Well, all right, before we go on....

Blough: There again the strength of that "could" could be reduced by "might," so it would read "might reduce" - if you don't like that.

Hanes: I think it's all right like it is.

H.M.Jr: "4. The fourth item on the Chairman's list on which I have been asked to give the pros and cons ...." - you use "pros and cons"?

Duffield: I insisted we get it in just once for the President.

H.M.Jr: All right.

"....is the suggestion that the deduction for capital losses of individuals be liberalized.

"In favor of such a change the following considerations are pertinent:"

Anything more on 16?

"(a) It would put the income tax more nearly on the basis of actual income over a period of years."

I'm not going to attempt to put mine together, Miss Humphries. Afterwards you'll have to get my copy. Give me one for myself, one for the President. I'm not going to stop now.

"(b) It would tend to stimulate the assumption of financial and business risks.

"The proposed more liberal treatment of capital losses would, on the other hand, have some undesirable aspects:

"(a) The revenue would be reduced. For a year with business conditions similar to those anticipated for 1939 it is estimated that the loss in revenue would amount to approximately $40,000,000.

"(b) The liberalization would result in some evasion of tax through deliberate manipulation of sales of assets on which losses had accrued.

"(c) The administration of the income tax would be further complicated."

Blough: That last isn't - that's true, but it isn't of enough importance that it needs to be given a great deal of attention.

H.M.Jr: Well, I hate to put in things that you're going to say - here you're saying before that it simplifies it. Now it's adding to it. How much will it add to the complication?

Blough: I wouldn't say it was worth mentioning.

H.M.Jr: Well then, leave (c) out.

Blough: It's a little difficult to figure carry-overs, and so on.

And in (b) - the liberalization might result in some evasion; I think it would, but....

H.M.Jr: I think I'd leave that in there.

Blough: Leave it as it stands?

H.M.Jr: Yes.

"5. The final item on the Chairman's list is the suggestion...."

Herbert, have you got anything on this?

Gaston: No, I agree with leaving out (c).

H.M.Jr: Shout, fellows - shout if there is anything you don't like.

"The final item on the Chairman's list is the suggestion that the upper surtax rates be reduced."

(H.M.Jr. continues to read silently)

I'm down to (a). Anybody want to say anything about it?

Hanes: I want to change (a) when it comes back. I don't think it's necessary to change it now.

Duffield: Which (a) is that?

Hanes: Top of page 18.

H.M.Jr: "(a) When the aggregate tax burden is great persons with especially large incomes can rightfully be

expected to make extraordinary sacrifices. A more equitable distribution of income may also be promoted."

Blough: That's a fighting paragraph, as you realize.

H.M.Jr: I don't understand that at all. I don't understand (a). "When the aggregate tax burden is great persons with especially large incomes can rightfully be expected to make extraordinary sacrifices."

Blough: In other words, it is equitable to have these high surtax brackets because with a high tax burden they can be expected to pay extraordinarily high rates; and it may increase the equity of distribution of income.

H.M.Jr: Oh.

Blough: Now, of course, I realize there is a lot - it may not be so, but it is an argument.

H.M.Jr: I see.

Now, in passing - anybody on 18, anything?

Hanes: I don't like that - (c), isn't it? No, it's (a). I don't like that paragraph the way it reads - "....make extraordinary sacrifices." I don't know why that should be so.

H.M.Jr: Of course, if that is true, if that statement is true, then there is no reason for changing it.

Gaston: I wouldn't agree to that at all. The reason for changing them is the argument that they choke business and you can't collect these very high rates, that they decrease your tax return and impede business.

White: Did you read (c)?

H.M.Jr: Shall I read (b) and (c)?

White: Might change his mind.

H.M.Jr: "(b) The existence of a large volume of tax-exempt securities now provides individuals in the higher income groups with a tax-free haven to which they can resort if they choose, so that the tax on income from all sources is much lower than the surtax rates would indicate."

Hanes: Where are you? I've lost you. Have you passed page 18?

H.M.Jr: No, we're coming back to it.

"To meet this objection it has been suggested by some, notably Senator Glass, that tax-exempt income be included at the bottom of the rate bracket instead of at the top, as is now the case, thus increasing the rates applicable to other income.

"(c) The immediate effect of lowering the top surtax rates would be a loss in revenue. For a year like 1939 it is estimated that the loss from reducing the top surtax rates to 60 percent would be a little more than $10,000,000."

Duffield: This was the point that the President raised.

H.M.Jr: That's right.

White: It's (d) that I meant was the significant one.

H.M.Jr: "(d) The efficacy of reducing high surtax rates for the purpose of stimulating investments is substantially weakened by the fact that to a person in the surtax bracket of 60 percent, for instance, an investment would have to provide a yield of at least 8 percent with no risk in order to be more attractive than the alternative he has of investing in State bonds of prime quality. Of course, with present rates persons in the highest brackets must obtain taxable yields of at least 14 percent with no risk to retain as much profit as can be obtained from a 2½ percent non-taxable income."

Well now, when you say "non-taxable income" that doesn't mean income from Federal bonds, does it?

Blough: No, income from Federal bonds is taxable in the surtax brackets now. It wouldn't be affected by this.

H.M.Jr: It would not be. What would be affected by it?

Blough: It would mean the income from State and local bonds.

Duffield: Treasury notes.

Blough: And other fully exempt securities.

H.M.Jr: But not Federal.

Duffield: Federal notes.

Blough: Not the partially exempt Federal bonds, no.

Hanes: Are you making that as a recommendation? That sounds like you're - that's injecting a brand new thought in here. Is that what you're trying to do?

Blough: It's not my thought.

H.M.Jr: It's the President's.

Gaston: What thought is that, John?

Duffield: Senator Glass's bill.

Hanes: I'd like to leave out - just stop at the first sentence.

Blough: Well, of course, I don't know anybody around the Treasury who has ever been very optimistic or happy about Senator Glass's proposal, which he made when he was Secretary of the Treasury back in 1920, and it is in here only because, as I understood it, it was specifically referred to in the President's comments.

H.M.Jr: Specifically.

Hanes: Maybe he will have forgotten it. I'll bet Senator Glass has.

H.M.Jr: That's a good line.

Gaston: He talked about changing the gold content of the dollar as being repudiation and taking other people's money. This proposition of his is to tax tax-exempt securities; that's what it is.

Hanes: Let's try to get by without that one.

H.M.Jr: I'm just thinking.

(H.M.Jr. goes out and returns in few minutes with Mrs. Klotz)

H.M.Jr: We're down to here.

You know, without getting into this thing, this raising of - I want you people to think - listen to this, Johnny, will you, for a minute. It's more important than any word, if you don't mind.

Hanes: Yes.

H.M.Jr: I've had this now for two days. This last thing he's emphasized - I wonder if I couldn't give this statement, give my front part, and simply say when we come to these recommendations that the Treasury staff will discuss the pros and cons of these suggestions given by Mr. Doughton. I never got up there - after I get through and these fellows are just sitting on the edge of their chair, they begin to ask, "Why did you say this and why did you say that?"

Now, let's just take a minute, let me just think hard for a minute. What am I trying to do? I'm trying to open the door, I've said again and again, so that these changes in the tax laws will be re-examined from the standpoint of deterrents. I go up there - get this letter listing the things, and I go up there, make my statements - "Glad to be here, glad to see Chairman Doughton has listed these five things. And the Treasury staff is here to explain the pros and cons." That's my statement. I could or could not, if I wanted to, close on

the increases. That isn't necessary. That's the kind of thing I may or may not want to do.

And then close on this statement here which I read before the radio, and just close on this note:

"I sincerely hope that Congress will take a careful look at the tax laws to see if there are any deterrents holding businessmen back from making future commitments. Businessmen ought to feel that the Administration wants them to go ahead and take a normal business risk and that we want them to make money.

"Of course we must have additional revenue, but in my opinion the way to make it is through business recovery and not through higher tax rates." I mean that would be my closing thing.

I don't know that I have ever gone up on the Hill and gotten into a pros and cons discussion.

Hanes: The idea is to take out all of your....

H.M.Jr: Not to get into it.

Hanes: ....tax statements.

H.M.Jr: I know what's going to happen. I mean by the time you give the pros and cons - let's be honest with each other - I mean some of these arguments are so darn specious that I wouldn't put my name to them. I'm not being personal now.

White: No, no, certainly not on the cons, Mr. Secretary.

Duffield: (Laughs).

White: Because every con argument had to get by Roy and he wouldn't let a specious argument in.

Blough: Well, when you said, "Well, it's an argument anyway," then I said, "All right."

H.M.Jr: Well, I mean - let's....

White: I think the conclusion you're coming to suggests this fact, from my point of view. It suggests that the more closely you examine these taxes, the more carefully you trace out their consequences, the much less certain you become that they are tax deterrents. That doesn't mean that they aren't a deterrent to some degree, but I mean the extent of the deterrent becomes much more a debatable point. And it seems to me that you accomplish your purpose, if I understand your purpose in this, starting from now - I'm not going back over the history - you accomplish your purpose if you give this to Congress; and they'll discuss all the pros and cons at very great length, and if there are merits in these taxes they'll be brought out in the discussions both in the Committee by your tax experts and others as well as on the floor of the House. So if your desire is to get this matter opened up and get action, I think you'll accomplish it, whereas I think you protect yourself by being in the position of an adviser, presenting both sides of the question without giving your view, unless you wish to give your view in response to their question.

H.M.Jr: I'm trying to see what Doughton has said to me, see how it reads. Well, it's all right the way it is.

I could still take this position. Where would it leave the suggestion for additional revenue? Would I make those?

White: That could be worked in. We could follow your thought without much trouble at all - not give any specific comments, turn it over to your staff, and still have your general discussion with respect to the necessity for maintaining the revenue-producing capacity of your tax structure. It could be done.

Blough: Did you keep the sheets I handed you on Saturday in which I proposed that you do exactly that? Those did include those tax increases at the end.

H.M.Jr: Well, I just - I don't know what you....

Klotz: I have them. It was the last few sheets.

Blough: They were triple-spaced sheets, three or four sheets.

H.M.Jr: What happened?

Blough: You thought it was too short at the time.

H.M.Jr: You've got it here, haven't you? You've got it on 21.

Blough: Oh, all of that is in. I mean this proposal to leave out all those pros and cons was written up on Saturday.

Klotz: Do you want it? I have it.

H.M.Jr: Please.

Duffield: May I ask, would you then leave in renewals of recommendations previously made?

H.M.Jr: Oh yes. But I mean the way I feel now - and it isn't just because I am under such great pressure - I just can't do this stuff, that's all. I can't do it. I mean I can't get myself to give these pros and cons.

White: It can be done as you - you can avoid it without much trouble. You could write in page 9 just an additional paragraph where you begin with "I turn now to a brief summary, with the arguments for and against...." - you could substitute a brief paragraph or two, leaving everything out and weaving in the suggestion that if it results in a reduction of revenue "Let me suggest these following taxes should be considered," without giving the pros and cons. It can be done quickly.

From one point of view, the Secretary of the Treasury should never be the man who goes into details with respect to specific tax proposals. That's a technical matter. So you have that much justification.

The only other thing is that this would make an interesting statement when it's published in a press release.

H.M.Jr: Which one?

White: As is.

(Mrs. Klotz brings in the suggested version written up by Mr. Blough)

Blough: That was intended to be fitted in right after the recommendations. Remember, we had that debate on the paragraph that we didn't want any tax increase. This would fit in right at that point.

H.M.Jr: What page?

Klotz: Page 10.

Blough: No, 9. It's intended to be fitted in either right here - right here, for that matter.

H.M.Jr: Let me read what he's got here. I think this might be the answer.

Would it go in on page 8?

Blough: Yes.

H.M.Jr: Would it go on page 8?

Blough: It was planned, of course, before this letter was talked about. But it would fit in right before it says "With regard, however, to the specific item mentioned in Chairman Doughton's letter...." - on page 8.

H.M.Jr: "However, action is necessary in at least one matter not including the corporation income tax."

(Continues reading silently)

Stockholders?

Blough: That was the President's suggestion.

H.M.Jr: Oh. (Continues reading silently).

Well, I personally think this, that I would - I'd run through to page 9, and then my thought is to

say there that the Treasury staff is prepared to do these things, and then - page 21 - I suggest the three possibilities for increasing taxes. Something like that.

White: That could be very easily done.

H.M.Jr: What?

White: That could be very easily done. You have your tax experts here to comment on any of the specific proposals. Then bring out the point that, however, if any of the suggestions are to result in a reduction in revenue, in light of what you said previously, they have to seek other ways of replacing it. Then I would suggest you then begin on page 21, so you practically cut out everything between the bottom of page 9 and the top of page 21, and substitute one paragraph.

H.M.Jr: What I would say is that in response to Congressman Doughton's letter the Treasury experts are willing to give the arguments for and against his suggestions; and then list them, you see. List his suggestions.

And then say, "Now, inasmuch as these suggestions will undoubtedly have the net effect of causing a loss of revenue, I want to take this opportunity to bring to your attention the least...." - I don't want to use "disagreeable" - or something like that - "....the least irksome method of making up this revenue." And then list those things.

Blough: I like that better than the one I suggested.

Duffield: I think that's better. I think it would be unfortunate if you didn't mention the things which he has....

H.M.Jr: Oh, definitely. Now, don't get me wrong. I want to be for them, but I don't want to give the pros and cons.

Duffield: That's fine.

H.M.Jr: Do you suppose you could give me two kinds of copies and still get it over there by 1:30? I should think so.

Blough: Yes, sir.

H.M.Jr: Give me a complete copy with the thing the way it is here, with the pros and cons; and then give me another one about the way I've said it, you see?

Blough: We can't give you a complete one, but we can give you the tail end to fit in.

H.M.Jr: She can give me the others. You've got 45 minutes. Well, don't lose any time.

But you get it. I want to put myself on record for these five things and then say, "Now, the Treasury staff is here to give you the pros and cons."

White: You say you want to put yourself on record as favoring....

H.M.Jr: I want to acknowledge receipt of Mr. Doughton's letter. "Now, these five various taxes that Mr. Doughton has brought up - the Treasury staff is here in compliance with your request to give the arguments for and against." But I want to bring in the five. Then "Inasmuch as these undoubtedly will cause loss of revenue, I want to take this opportunity to suggest other taxes to make up the difference."

Blough: Do you want to say, "I am for the five"?

H.M.Jr: No, just the way I said. But bring in the five and then bring in the total.

Now, Miss Humphries, who's - I'll leave word - what office is this that's going to do it?

Humphries: Room 207.

H.M.Jr: Don't you want to go with them, Herbert? I wish you would.

Blough: Certainly do.

H.M.Jr: Please.

A - May 6
(Approved by H.M.Jr.
May 6)

My dear Mr. Secretary:

The Ways and Means Committee of the House of Representatives invites you to appear before the Committee on May _____. At that time the Committee will be pleased to receive any information you have on various tax changes which have been suggested recently by business organizations and private individuals. Among the suggestions which have been most frequently made are the following:

Repeal the capital stock and excess profits taxes.

Allow business net losses in one year to be carried forward and offset against income in subsequent years.

Permit corporations to deduct net capital losses from ordinary taxable income.

Liberalize the deductions allowed for net capital losses sustained by individuals.

Reduce the individual surtax rates in the upper brackets.

It would be helpful to the Committee if you would present the arguments for and against as many of these suggestions as the Treasury has studied.

Obviously most of these changes, if adopted, would result in a decrease in revenues. Inasmuch as a fundamental prerequisite of any tax revision at this time is maintenance of the present revenue, the Committee would appreciate it if you would also discuss possible ways of offsetting any revenue losses. The Committee would, of course, be glad to hear your views on any other pertinent matters which you may wish to discuss.

The Honorable Henry Morgenthau, Jr.,

The Secretary of the Treasury.

B - May 8th
(Typed up to include suggestions of Congressman Doughton)

My dear Mr. Secretary:

The Committee on Ways and Means of the House of Representatives invites you to appear before the Committee on May , at which time the Committee will be pleased to have an expression of your views as to any changes in our Internal Revenue Tax Laws that you consider might be helpful to business as well as equitable to taxpayers. Also, the Committee would be pleased to have you give it the benefit of any information you have as to the desirability of various tax changes which have been suggested, ~~recently by business organizations and private individuals~~. Among the suggestions which have been most frequently made and which I, myself, have thought might be worthy of consideration are the following:

Repeal the capital stock and excess profits taxes.

Allow business net losses in one year to be carried forward and offset against income in subsequent years.

Permit corporations to deduct net capital losses from ordinary taxable income.

Liberalize the deductions allowed for net capital losses sustained by individuals.

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#2

discuss possible ways of offsetting any revenue losses which might occur in any changes made. The Committee would, of course, be glad to hear your views on any other pertinent matters which you may wish to discuss.

Sincerely yours,

The Honorable Henry Morgenthau, Jr.
The Secretary of the Treasury
Washington, D. C.

C - May 8
(Submitted to President May 8)

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It would be helpful to the Committee if you would present the arguments for and against as many of these suggestions as the Treasury has studied.

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Sincerely yours,

The Honorable Henry Morgenthau, Jr.
The Secretary of the Treasury
Washington, D. C.

May 7, 1939

348

2211 THIRTIETH STREET
WASHINGTON, D. C.

Every item of expenditure
should be carefully scrutinized
and as our outlay for
armament increased and
ts additional men to work
could well afford to
tail other forms of public
ks.

Finish with what I said
for Movies —

salaries hereafter earned and all interest on government securities hereafter issued subject to Federal and state income tax laws. That part of this recommendation dealing with government salaries, I am pleased to note, has already been incorporated into law.

3. In my statement of March 24, 1939, I presented for your consideration four alternative rate plans for old-age insurance contributions during the next three years.

4. The Treasury Department has pointed out from time to time that the present law allows excessive deductions for depletion of oil and gas wells and certain mines. Removing this inequitable special privilege would produce a substantial amount of revenue.

It seems impractical at this late date for Congress at this session to undertake any comprehensive reexamination of the tax laws. Moreover, before undertaking any broad revision it would be desirable to have the report of the proposed special committee on the fiscal relations of the Federal and state governments.

With regard, however, to the specific items mentioned in Chairman Doughton's letter, I am glad to present for your consideration a summary of the findings of the Treasury staff. Before commenting on them,

although in many cases the tax is of insignificant size. There is much to be said for the position that all corporations should contribute to meet the cost of government whether or not they make profits.

(c) Rather than repeal these taxes they could be revised and made to apply to actual capital value and excessive profits. Such taxes, if successfully developed, could serve as the basis for special profits taxes necessitated by war.

2. The second item on which Chairman Doughton asked me to comment is the suggestion that net losses of business, both individual and corporate, incurred in one year be offset against the income of subsequent years. At present, individuals and corporations are taxed on their annual incomes without reduction for losses incurred in prior years.

In favor of the proposal are the following considerations:

(a) Allowing the carry-forward of business losses would make taxable income

The disadvantages that would need be considered in connection with the proposed arrangement of business losses are these:-

coincide more nearly with actual income over a period of several years. Businesses with alternating income and loss now pay higher taxes over a period of several years than do those with stable incomes. Many pay income taxes in single years of net income even though over a period of years they have had no net income or have suffered a net loss.

(b) Allowing the carry-forward of business losses would somewhat increase the incentive to new enterprises and to the expansion of the capital goods industries, which are subject to wide fluctuations in earnings.

(c) Allowing a loss carry-forward would reduce the administrative difficulties caused by the taxpayers' effort to shift items of income into loss years.

However, the proposed carry-over of business losses would also have disadvantages:

~~(a) In the first place, it would result in a substantial loss in revenue.~~

Assuming that the carry-forward provision was not made retroactive and that the law applied first to 1940, there would be no revenue loss until the fiscal year 1942, after which the loss would increase over the number of years required to reach full application. For example, in a year of full application it is estimated that the revenue loss from a three-year carry-forward provision would vary between $25,000,000 and $200,000,000, depending on the business conditions of the year and the three preceding years.

~~(b) It would complicate the mechanics of administering the income tax.~~

(c) Allowing a loss carry-forward would benefit many businesses while relatively few might be stimulated to expand their activities as a consequence of carry-forward privilege.

3. The third item on your Chairman's list is the suggestion that corporations be allowed to deduct their net capital losses in full from their ordinary incomes. Under the present law an excess of corporate

May 8, 1939
9:16 a.m.

HMJr: Hello.

Operator: Blough hasn't come in yet. I have Congressman Doughton.

HMJr: All right.

O: Go ahead.

HMJr: Hello.

Robert Doughton: All right, Mr. Secretary.

HMJr: How are you?

D: All right. How are you?

HMJr: I'm fine.

D: That's good.

HMJr: And how are you coming along on that letter?

D: All right, we're working on it now. I've made a few suggestions -- changes.....

HMJr: Good!

D: .....and if they don't appeal to you, why -- the way you have it, it will be all right with me. I made one or two suggested changes and we're having two or three copies made of it, and he'll take it down and you can handle it as you please. If you want to take it up with the Chief again.....

HMJr: Well, now if you want to -- I mean, if you can -- sign it and then if it isn't all right I can send it back.

D: Yeah -- well no, we can -- if it's not all right, you call me on the phone and we'll agree on any modification.

HMJr: Yeah, but you want.....

D: Without -- without -- you sending it back.

HMJr: But I mean, in order to save time, do you want to sign it?

D: How's that?

HMJr: Do you want to sign it?

D: Well, I want to sign it before I send it to you, but there's no use in me doing that until I -- you see, I'll just make a new copy and send to you when I get ready to fix the date.

HMJr: I see.

D: And then we'd agree on the form, you know.

HMJr: I see.

D: And then you can just -- I'll keep my copy here and then you can just phone back any suggested changes or you can make a new copy, if you want, and send it back.

HMJr: Fine!

D: And I'll just hold it in abeyance here until I get ready to fix the date.

HMJr: All right. And in case -- what date would you have in mind? Do you think you could reach me maybe the end of this week?

D: Well, I can tell better in a day or two. I'll just see what we can do in the House. If we can get up -- we are going to get our bill back from the drafting service Wednesday morning.

HMJr: Yeah.

D: We'll be a day or two on that -- going over it again. Well then, if the House should not-be occupied with something else and we couldn't take it right up, why I could probably get you the latter part of this week.

HMJr: Yeah, that would help a lot.

D: Yeah. Well, I'll do my best on that then. I'll see if I can't work that out of the organization.

HMJr: Well, after you've had a day or so to think this over, how do you like this approach?

D: I like it fine.

HMJr: So do I.

D: I like it fine. I think it's excellent.

HMJr: I think it's the way to do it.

D: Yeah, I think it's -- I think it's fine, and I think it's very considerate of you, and I think -- it may be worked out practically.

HMJr: Well, you're -- after all, you're Chairman and with that magnificent record up there why, you're the fellow that ought to do it.

D: Well, after you read this amended copy that -- that they've taken down, you call me back and tell me what you think of it.

HMJr: I'll do that.

D: Thank you very much.

HMJr: Good bye.

D: Good bye.

May 8, 1939
9:19 a.m.

HMJr: Dan.....

Dan Bell: Yes.

HMJr: I don't know whether you'll have it ready -- time in ten minutes, but what I want you to do sometime this morning -- I'd like to know on the appropriation bills which have passed to date whether we are over or under the budget figures -- that's number one.

B: Yeah.

HMJr: And number two, what does this new bill -- agricultural bill mean -- how much is it over, and what does it do, you see?

B: Yeah.

HMJr: And also number three, did they ever give us any revenue for the last bill. What are they.....

B: Parity -- parity payment?

HMJr: Yeah.

B: No.

HMJr: Well, if you could give me one, two, three and then be thinking over whether -- I might want to say something to the President about it at one o'clock. And the other thing, I'm thinking about is saying something about it in my press conference.

B: Yeah.

HMJr: So be thinking about it, will you?

B: Yeah. The first, on the appropriation bills, they're not bad up to the time the Senate packed on this three seventy-five -- this three hundred and seventy-five million for parity payments certainly goes over it.

HMJr: Well.....

B: But I'll get you one, two, three.

HMJr: You get the idea.

B: Yeah.

HMJr: And be thinking over whether you think I ought to, at my press conference, jump in and say that -- well, that it -- it just isn't in the wood, or something like that.

B: Yeah. Or say that you assume that they'll carry out the President's suggestion in his two budget messages that -- to get taxes for the last one before they start out on another one.

HMJr: Something like that that I can take up with him.

B: Yeah.

HMJr: You see?

B: Yeah. Is there a nine-thirty meeting?

HMJr: There is.

B: All right. I doubt if I can get it by then, but I can get some figures on it this morning.

HMJr: No, I know you can't, but I wanted to put the idea.....

B: Thanks a lot.

HMJr: Good bye.

GROUP MEETING

May 8, 1939.
9:30 A. M.

Present: Mr. Hanes
Mr. Gaston
Mr. White
Mr. Haas
Mr. Foley
Mr. Duffield
Mr. McReynolds
Mrs. Klotz
Mr. Gibbons
Mr. Lochhead
Mr. Graves

H.M.Jr.: You didn't take it, Herbert?

Gaston: What?

H.M.Jr.: The Father Coughlin magazine.

Gaston: Yes. You handed it to me. I have it on my desk.

H.M.Jr.: Would you get it, please?

Gaston: Yes.

H.M.Jr.: I thought you saw it.

McReynolds: I saw some printed matter there. I knew there was a Congressional Record attached to it.

H.M.Jr.: Where is Bell? What have you got, Mac?

McReynolds: Nothing here that needs to be talked about. This came in--a bill on "Buy American" stuff. Harry Collins called me about it on Saturday. They are proposing some new legislation on it. But it hasn't got to the point where it needs any consideration--the legislation--but it will come up regularly, of course.

H.M.Jr.: How was the golf?

McReynolds: Well, two lovely golf days. Couldn't have been any better. I haven't any boasting to do about the golf, but I had a grand time. I played both Saturday and yesterday.

H.M.Jr.: Good.

(Bell comes in.)

Dan?

Bell: The free silver is again piling up in the Treasury to about 70 million. About the only way we can get it out is to increase the volume of tens. The present limit on it is 250 million dollars. Do you want to increase it another 50?

H.M.Jr.: Yes.

Bell: All right.

The only other thing I have is, I have an invitation to go to Harvard on the 16th for this Littauer group. I'm trying to find a good excuse to get out of it.

H.M.Jr.: Don't look at me.

Bell: Think I ought to go?

H.M.Jr.: I think they are doing good work up there, yes.

Bell: It's on the investment budget.

H.M.Jr.: I think it's good work. You look so healthy these days.

Bell: Feel pretty good. Don't have to walk down the corridors so many times.

H.M.Jr.: I didn't know that it was that you objected to.

Bell: Gee, that's one thing--ten times a day.

H.M.Jr.: Will you have a memorandum for me on that thing? I've asked Bell to give me a memorandum on just what this increase in agricultural appropriations means and where we stand in relation to the budget. It's the last thing in the whole business, and I'm thinking about the possibility of saying something publicly, drawing the country's attention to the fact that this is 375 . . . .

Bell: 375 million.

H.M.Jr.: . . . . over any budget estimate. How can we run the country's finances when with just a snap of the fingers they shoot it up 375 million? I mean there isn't much use trying to do anything like tax proposals.

Gaston: Why not introduce this into this other talk, in connection with your talk about fiscal planning, joint meetings of the Committees? You might use that as an illustration.

H.M.Jr.: That might be a good one. Has it passed the Senate?

Bell: No, it's reported out of the Committee. Don't think it passed the Senate.

McReynolds: They predict it will pass with about 15 minutes' discussion.

Gibbons: Gardiner Jackson brought in a group of C.I.O. Maritime fellows from the West Coast on Friday. You might have seen in the paper that the C.I.O. and A.F. of L. are together on stopping the Maritime Commission from operating Maritime boats between Seattle and New York. They wanted somebody to bring it to the attention of the President. They are going to call a strike. I told them the thing to do was for Gardiner Jackson to get hold of either Mr. Farley or their national committeeman. Gardiner suggested I do that, so I am going to talk to talk to Farley about it, if it's all right with you.

H.M.Jr.: (Nods yes)

Gibbons: They think that the Coast Guard had done such a swell job, that they came to us as a last resort. The Maritime Commission is apparently not going along with them. I'm in sympathy with them personally, but I don't think we should stick our neck out. It's Jim's function, don't you know, to get the political organization together. O. K.?

H.M.Jr.: Well, I just don't want to--I mean without knowing anything about it, I don't like to--personally, I don't like to mix politics into those kinds of things anyway. So all I'd say is that the

decision to keep out of it is good and if Farley wants to get in on it, that's his business. But I hate to use a political organization for that purpose.

Gibbons: It's a question of policy of the Administration and--I mean he represents the Administration; you represent the Treasury.

H.M.Jr.: But this is something different. But as I say, your decision to keep out of it is all right. If they want to get the political organization in it, that's their business.

Gibbons: That's their affair. I don't think the Treasury wants to . . . .

H.M.Jr.: I mean I personally don't think . . . .

Gibbons: We are indirectly connected because the Coast Guard is training . . . .

H.M.Jr.: I don't think it's a political matter, but that's for Jim to decide. O. K.?

Gibbons: Well, it isn't a financial or Treasury matter.

H.M.Jr.: Definitely not.

Gibbons: Matter of policy of the President, broader than just one Department.

H.M.Jr.: Dan, read Pearson and Allen today, what they say about reorganization. Some people can talk to them all they want. And then remember my little memo that I got. You know the conversation that took place about my memo.

Bell: O. K.

H.M.Jr.: I mean somebody else can talk to Pearson and Allen, tell them how they feel about the transfer of Bureaus, but I mustn't. It's very interesting.

Bell: All right.

Lochhead: The week-end news has had no effect on the exchanges. They are all very quiet. Nothing at all to report on those.

I think you noticed the column in the Post this morning on loans to South America.

H.M.Jr.: Yes.

Lochhead: Trial balloon of some kind?

H.M.Jr.: Well, Mr. Lochhead--incidentally, you already were famous, but your story made you infamous. Now it's all over Washington.

Lochhead: Got them very interested.

H.M.Jr.: Haven't you heard the story? It's the best story of the week. Mr. Lochhead walked in here the other morning--you haven't heard this, have you, Harry?-- . . . .

White: I don't think so.

H.M.Jr.: . . . . looked outside my window at the 3-foot trench and the parade going by and said, "You know what the men on the street are saying about the trenches out there? That they are the Treasury's first line of defense against Nicaragua." Very funny. We were all lined up to receive the Nicaraguans and I said something about it--I don't know who would be standing next to me--I guess it was Woodring--and he whispered it to the next fellow and you could just hear it go down the whole line of twenty people--"You know about Nicaragua . . ." They gave you full credit for your story. So if you see it in Harlan Miller's column you'll know Woodring gave it to him.

White: That's why they put that layer of horse manure on it.

H.M.Jr.: That's why they put the three inches of scrap rock.

Lochhead: In connection with South America I wanted to bring up again that Admiral Waesche asked me to ascertain how you felt about their cruise this summer being down the West Coast. They went down the East Coast last time. I did speak to Duggun officially over there. Of course, he is very enthusiastic. But I didn't want it to go any further until I found out from you how you felt about it.

H.M.Jr.: It's all right.

Lochhead: Is it all right to tell them?

H.M.Jr.: Well, you fellows fix it up. I think it's fine.

Gibbons: They were going to the Mediterranean. The State Department stopped that.

Lochhead: Question now of whether they go north of Europe. They went to South America last year.

H.M.Jr.: But the northern part of the east coast of South America would be O. K. East Coast, isn't it?

Lochhead: West Coast. They went to the East Coast last year. West Coast--Columbia, Ecuador, and all that.

H.M.Jr.: All right.

Harold?

Graves: Nothing.

H.M.Jr.: I think it would be nice, Harold, if Mr. Hanes and myself, now that you've got the 32 branch offices opened--you could give us a report, and then maybe if we like it Mr. Gaston might give it out.

Graves: We promised . . . .

Hanes: There's a release ready. Whether that's gone out . . . .

Graves: That release is gone.

Gaston: That release was on the opening of the last of the offices.

Graves: But I had promised already to Mr. Gaston a statement in about two weeks that would give the results of the operations in those divisions that have been operating longest.

Gaston: Yes.

H.M.Jr.: All right.

This is an amusing story. We had an invitation for two nights this week from Mrs. Mabel Willebrandt to have dinner with her and

Mr. Mayer from Metro-Goldwyn-Mayer. So Mrs. Klotz was asked to call them up and tell them we were very sorry, Mrs. Morgenthau and I were engaged. So what did she say--couldn't we come for lunch?

Klotz: Uh-huh.

H.M.Jr.: I said, "No." Finally . . . .

Klotz: They said, "Do you know who Louis Mayer is? He's the Mr. Mayer."

H.M.Jr.: They weren't satisfied, so Mrs. Willebrandt calls up Mrs. Morgenthau Saturday evening and says, "I just want to know whether you don't want to accept my hospitality." Mrs. Morgenthau said, "I'd love to accept your hospitality. We had a big discussion about it. But we are so busy. And if Mr. Mayer wants to see my husband on business, he would be very glad to see him at his office."

"Oh, no, it isn't business, it's just social. Just thought that he'd like to meet him."

So Mrs. Morgenthau says, "If he wants to get him any time at the Treasury, Mr. Morgenthau will be glad to see him."

"Oh, nothing to do with taxes."

So I'm missing a good dinner, also a headache.

McReynolds: Well, Mabel is a right interesting person.

H.M.Jr.: Mabel is all right--ever since we sold her a million gallons of prune juice in Farm Credit.

Gaston: Grape concentrate, wasn't it?

H.M.Jr.: Grape concentrate. The movie colony bought a million dollars worth of grape brandy as a hedge against inflation. I think it subsequently turned sour.

Klotz: Oh, that's terrible.

Bell: There was a surplus on the market. Farm Credit got it back.

H.M.Jr.: That's all you've got?

Graves: Yes, sir.

H.M.Jr.: Harry?

White: That statement, revised statement, is all ready now.

H.M.Jr.: Well, eleven o'clock.

White: And the capital is continuing to flow in in very large amounts. We have a . . . . . .

H.M.Jr.: Johnny, eleven o'clock.

White: . . . . complete survey and analysis.

McReynolds: You've got a date.

H.M.Jr.: Who with?

McReynolds: Gray and Willard.

Klotz: I changed it.

H.M.Jr.: I suggest you talk with your secretary. She might bring you up to date.

McReynolds: I was here at nine o'clock this morning--five minutes of nine.

Klotz: She wasn't, though.

(Hearty laughter)

H.M.Jr.: I haven't teased you, Mr. Justice, in a long time. Eleven o'clock tomorrow.

McReynolds: O. K.

H.M.Jr.: Can you still take it?

McReynolds: Still take it.

H.M.Jr.: Anything else, Harry?

White: We're having a survey and analysis of the whole gold and capital situation done. It will be ready as soon as you--be ready tomorrow to take up as soon as you want to. And of the

trade situation, too.

H.M.Jr.: I didn't get very much out of your memorandum on Paraguay and Nicaragua.

White: Oh, it was very brief. We don't know anything about it. Nothing very complete is available to us.

H.M.Jr.: I agree with you.

White: No statistics. We get nothing from the State Department. There was more in it, in self defense--there was much more in it than there was in the State Department memorandum.

H.M.Jr.: Now, to come back, I thought that over the week-end you were to do business with the Nicaraguans. What happened?

Lochhead: I understand that you appointed Mr. Jones as your proxy.

H.M.Jr.: And Mr. Jones went down to Kentucky. Nothing happened?

Lochhead: As far as I know, haven't heard a word.

H.M.Jr.: If you stay behind a minute, I'll tell you what I said to Mr. Sumner Welles about that. I got it all off my chest.

White: Another thing. We were supposed to send a man down to Paraguay two months ago. The State Department changed their mind. Had we sent somebody down there we'd have known something in time for this negotiation.

H.M.Jr.: Paraguay?

White: Paraguay, yes. But they publish very little statistics and there is nothing that comes up here.

H.M.Jr.: George? I see the automobile business is "poof."

Haas: The production dropped more sharply than sales.

You wanted those figures there. You want that every day?

H.M.Jr.: No, I think twice a week.

Haas: Here's the price situation.

H.M.Jr.: Right.

(On phone). General Craig, please.

Haas: And this employment business, when you have a free moment.

H.M.Jr.: Yes. (To Mrs. Klotz) I want to see Haas sometime.

In confidence I think you'll all be very pleased to know that I believe today Mr. Foley's name is going up as General Counsel, and he's getting it because he earned it. I'm very pleased to recommend it.

Foley: Thank you, sir.

H.M.Jr.: From now on it's "Mr. General Counsel."

White: I'll make mine scotch.

H.M.Jr.: I'll make mine scotch. The drinks are on Ed.

Foley: We have another letter from Congressman Thomas in regard to the Sokol case. Harold Graves and Steve Gibbons and Mac and I talked it over on Saturday and we thought that we'd write another letter saying that we would not produce the Canadian . . . .

H.M.Jr.: (On phone) Hello. (Conversation with Major Lee, of General Craig's office, follows:)

May 8, 1939
9:50 a.m.

HMJr: Hello.

Operator: General Craig is not in his office. They expect him shortly. Major Leahy is there.

HMJr: Well, I'll talk to Major Leahy.

O: All right. Go ahead.

HMJr: Hello.

Leahy: Good morning, Mr. Secretary.

HMJr: Good morning. Will you tell the General for me that I want to thank him very much for having sent over those memorandums?

L: Yes, sir.

HMJr: And that until -- for the time being I think I can get along without them.

L: Yes, sir.

HMJr: And that if I wanted them again I am going to call on him.

L: Fine, Mr. Secretary.

HMJr: But I didn't want to write a formal letter because I didn't think he'd want it on the records.

L: Yes. Well, when we can be of assistance you just let us know.

HMJr: Thank you very much.

L: Good bye, Mr. Secretary.

HMJr: Good bye.

Foley: He is also asking for Harold's appearance tomorrow morning. I think it would be a good idea for Harold to go down with Sam Klaus, Sam having worked on it and knowing more about it than anyone else in the Legal Division. And Sam and Harold have been working with the files and know about what to say and what not to say. And I think that that's the best way to proceed, if it's all right with you.

H.M.Jr.: Now, is this on the Canadian liquor or is this on this informer's fee?

Foley: It starts with the informer's claim, and Thomas from our file has gotten certain information as to the settlement insofar as the Canadian distilleries are concerned, and now he wants to go into that file; and it is that that we are resisting on the grounds that the file contains confidential communications between our Government and the Canadian Government and it isn't related to the matter that he has before him as a subcommittee to determine his so-called claim.

H.M.Jr.: Of course, I think it is most unfortunate--it's water over the dam, but--that those files were ever permitted to go up in the shape they did. Everything should have been gone over letter by letter, and I think it was most unfortunate that they were permitted to go up there with all that stuff in there. And I think that if we had taken the attitude right from the beginning that this fellow Sokol when he got--what was it, a hundred thousand dollars?

Foley: More than that.

Gaston: A hundred and three thousand.

H.M.Jr.: That he got all he was entitled to. And we should have just aired the whole thing. Now it kind of puts us on the defensive. I think it's most unfortunate.

Let me ask you this, to clear up my memory. In the final settlement of those Canadian liquor cases, did we ever get a written recommendation, a written request from the

State Department asking us to settle for three million dollars?

Graves: Yes. The offer was transmitted, Mr. Morgenthau, through the Canadian Legation to the State Department.

Foley: Phillips wrote you a letter--Phillips as Acting Secretary.

Graves: Then it came to us.

H.M.Jr.: Then they asked us.

Graves: I wouldn't want to say that they made in their transmittal any recommendation that we accept it.

H.M.Jr.: Now, when I was away, Mr. Taylor conducted those negotiations, huh?

Graves: I don't remember that.

H.M.Jr.: Yes, I think so. See if he didn't recommend--I mean who--I mean I want to know who finally put it through, just so we know whether we want to ask Mr. Taylor to come down and to help out. It was done in his room.

Foley: It was approved by the State Department--by the Department of Justice before it was accepted.

Graves: Oh, it was approved by the Attorney General. No question of that.

Foley: And the Department of State, because that same letter that went . . . .

H.M.Jr.: I think you'll find--because I was away--I think you'll find that Mr. Taylor must have recommended it, and we . . . .

Graves: I don't think so. I think that Mr. Taylor was practically out of the picture at the time, Mr. Secretary. My present recollection is that you sent for me yourself and you told me that that settlement had been agreed upon: three million dollars. Now, where you had that suggestion I don't now remember.

H.M.Jr.: Well, I'm not ....

Klotz: I'd think we'd have the record in the files--the record in the diary.

H.M.Jr.: Would you check it?

Klotz: He started it.

H.M.Jr.: Put somebody on it, anyway. Well, you'd better--do you (Graves) need stuff to go up--do you want any of my stuff?

Graves: I might examine what you may have. I think I was planning--if you wanted me to go there at all, I was planning to keep that all out of it.

H.M.Jr.: And just keep on the Sokol thing.

Graves: Keep it on the Sokol. If it comes to the Canadian distillery matter, I was going to say that the Treasury Department had a conferee, which is a fact, in the settlement of those cases and the Department of Justice had conferees, and we made a settlement, recommending it to our superiors. It was approved. It didn't happen exactly that way, but I think that's the way the record looks.

H.M.Jr.: How did it happen?

Graves: As I say, the way it happened--after we had been negotiating for a month down there, we had this offer transmitted from the Canadian Legation to the State Department to us, offering three million in the aggregate--spelling it out, so much to one company, so much to another, etc. And you called me in and told me that that was the settlement.

H.M.Jr.: Well now . . .

Graves: And I think maybe you had had some information from Mr. Phillips . . . .

H.M.Jr.: Well, look it up, will you, please. Let's just get the thing. Could you keep it on this basis when you go up tomorrow. Be prepared to talk about Sokol, and say that if they want to go into the Canadian liquor thing, you'd

have to get instructions from me, or that there are other departments concerned, see? Let's keep it that way, see?

If you (Hanes) want to know about it, get Harold to explain it to you. It's a long, complicated story. The gist of it is that this fellow Sokol is trying to get a bill through to get another 50 thousand dollars out of us. We don't think he's entitled to it. Loring Black is his attorney. He's got some other fellows up there interested, trying to put it through.

Now, the whole file has got in the hands of this fellow Thomas from New Jersey. He's the fellow that made it so unpleasant for Miss Perkins. I don't mind, our record is all right, but I'm afraid that we are bringing in the State Department. Was that the time that their Trade Treaty was pending?

Graves: That's right.

H.M.Jr.: And didn't they say that the Trade Treaty--this was part of the thing that they wanted us to do?

Graves: That's right.

H.M.Jr.: I thought so. You look it up.

Klotz: That's right. I remember.

H.M.Jr.: I'm not afraid of my own record, but as I remember there was considerable pressure on us.

Graves: That's right.

H.M.Jr.: What?

McReynolds: From the very beginning there was a build-up there.

H.M.Jr.: Well, I think it's perfectly proper for you to go up and talk about Sokol to the limit, but when it comes to talking about the settlement of the Canadian cases, in which the State Department is all mixed up, we'd better--before you do that, we'd have to talk to the State Department and Justice.

Graves: But if you will . . . .

H.M.Jr.: But in the meantime you look up . . . .

Graves: I have this suggestion I'd like to make about that. I think this man Thomas--is that his name?-- . . . .

Foley: J. Parnell Thomas.

Graves: . . . . is quite unfriendly and hostile about this thing, and I believe the more mystery we make about it the worse off we're going to be. I have the idea that if we could tell this man Thomas actually what happened about that settlement, keeping out the State Department, it might put an end to it. I think that if we undertake to withhold information, even with that qualification, that it may arouse his curiosity further.

H.M.Jr.: Well, Mrs. Klotz, get my diary, see why I said yes, and what happened, you see? And then I can see you again this afternoon.

Foley: We have a memorandum as to why you said yes. The four reasons were . . . .

Graves: Of course, those, Ed, were after the settlement was all consummated. That was in a letter we were sending to Senator Bailey months after the settlement had been agreed to.

Foley: I thought those were the reasons, though, that brought about the settlement.

Graves: That's right, they were.

H.M.Jr.: Did I write to Bailey about it?

Graves: Yes, afterwards you gave him a memorandum.

H.M.Jr.: Well, why isn't that memorandum still good?

Graves: It's still good, but it brings in information we would not want to give this man now about the State Department.

H.M.Jr.: Well, Harold, I am more than willing to let you handle it in your own way. Take a look at what I've got, see? I give you carte blanche to handle it in your own way.

Graves: Well, if I may say this further, we have already talked to Sam Whittaker. You remember Sam Whittaker was the Special Assistant to the Attorney General who worked on these cases, who is now Assistant Attorney General.

H.M.Jr.: I see.

Graves: Whittaker and McMahon were the Justice Department conferees, in that case, and they are perfectly willing to go down with us now.

H.M.Jr.: Whittaker is a good man.

McReynolds: Excellent.

H.M.Jr.: Why not take him up with you?

Gaston: He was the prosecutor out in Seattle, wasn't he?

Graves: No, he was the Special Assistant that went out to Seattle.

McReynolds: They put him in at our request.

Graves: I thought we could put it up to this man as an ordinary routine settlement effected by the Treasury and Justice Departments.

Foley: I think it would be a good idea, Mr. Secretary, to talk to Whittaker and tell him what we are doing. I see no reason to take him up, since his presence hasn't been requested.

H.M.Jr.: I'll say this. I'm willing to leave this in Graves' hands and Foley's hands. If you've got any doubt, come in and see me before you go up. Are you willing to take that responsibility?

Graves: Fine.

H.M.Jr.: And then look at what's in my record. I know the pressure on it was terrific from the State Department, to do it.

Graves: I know it.

H.M.Jr.: What?

Graves: Yes. But I think we ought to keep that all out of this testimony before this Committee.

Klotz: I think Hornbeck was the man from State Department.

H.M.Jr.: No, the fellow in charge--assistant fellow in charge that looks after Canada. What's his name?

Graves: Hickerson. But Bill Phillips was really the important figure in the State Department in connection with that.

McReynolds: Hickerson was our man in that. He was on our side right from the very beginning.

H.M.Jr.: Well, it's a long time ago.

Graves: Phillips and Moore took the lead in the State Department.

H.M.Jr.: Well, if you want to see me this afternoon after you have seen my stuff, let me know.

Graves: Yes, sir.

H.M.Jr.: Where was I?

Foley: Right here.

I have a memorandum here for you on that request of Morris Ernst. I thought you might want to have it when he comes in.

Klotz: He is going to call for an appointment.

H.M.Jr.: All right.

Foley: And you asked about Monseigneur Ryan. He is about to leave Catholic University--seventy years old, retiring this year. This is a memorial dinner. I think all the Cabinet has been asked, so the names might be used on the Committee.

H.M.Jr.: You think I ought to go?

Foley: I think you ought to, because he's been a very

good friend of the Administration.

H.M.Jr.: All right.

Now, isn't J. Will Taylor Chairman of the Appropriations Committee?

McReynolds: Yes.

H.M.Jr.: Well, who knows him well?

McReynolds: I don't think anybody.

Bell: You mean in the House? I know him very well.

H.M.Jr.: Do you?

Bell: Yes.

H.M.Jr.: Well, take a look at this, and I wonder if--it says "Representative from Tennessee." He's not from Tennessee.

Foley: No, he comes from Colorado.

McReynolds: Wait a minute, there is a Taylor from Tennessee.

Gaston: This isn't the Chairman of the Committee.

McReynolds: He's a Republican representative from the mountains of Tennessee, some place--been there for many years.

Bell: Never heard of him.

McReynolds: He's been there for many years. McKellar charges me with knowing him, but I never saw him.

Foley: Reece is from Tennessee, a Republican member from Tennessee, and is on the National Economic Committee. Now, O'Connell, who is our representative, knows Reece very well. Maybe we could do it that way.

Hanes: I know Reece very well.

H.M.Jr.: Well, this is the thing, you see, that Taylor said--he said my father is a member of the firm of Kuhn, Loeb, and Company.

Gaston: Said he's a majority partner.

H.M.Jr.: Then Father Coughlin picked it up, makes a whole story about it. I want Congressman Taylor to retract it.

Gaston: Looks like one of those things that Father Coughlin planted with this man to say.

H.M.Jr.: Now, who could talk to Taylor? Who knows how to reach him?

Hanes: I can get it done all right. I can get Lindsay. Lindsay will handle it for me.

H.M.Jr.: He will?

Hanes: Sure he will.

H.M.Jr.: Fine. Here is the thing. Here is the whole business. Then after we get it printed--then I think maybe we might consider writing Father Coughlin a little letter, you see?

Foley: All right.

Lochhead: Why shouldn't Kuhn, Loeb, and Company deny it? They have their stock records. That's official. The firm itself can give an official denial.

H.M.Jr.: Here is the suggested letter. But I think we'd better have--well, no, the thing is devoted to me and my father and I'd like to take care of it myself.

Gibbons: In Social Justice Magazine?

Gaston: Yes, yes.

Foley: I had this legislation to authorize wire-tapping under certain conditions. I wanted to know whether you wanted to recommend it.

H.M.Jr.: Oh, get me--I want to sit down and talk. I can't--I want to go into the whole philosophy, and I'd like to talk to . . . . Supposing you see if you can talk to fellows like Frankfurter and Bill Douglas and ask them how do they feel about a thing like this. Do you know Justice Stone?

Foley: No, I don't know him.

H.M.Jr.: Well, I do. I'd like to get their reaction on a thing like this. But you talk to those two.

Foley: I'll talk to Felix and Bill.

H.M.Jr.: Yes.

Foley: All right.

Duffield: Nothing.

Gaston: The boys are anxious to go to Daylight Savings schedule on the Monday afternoon conferences as we did last year. Three o'clock instead of four.

H.M.Jr.: Let me find out--I asked for an appointment.

(On phone) Have we heard from the White House about my--if I have any appointment today? Ask Kannee.

McReynolds: No flag on the White House a while ago.

Gaston: Chick Schwarz was looking out my window and said he saw the President coming in from his week-end.

H.M.Jr.: John?

Hanes: Nothing.

H.M.Jr.: Well now, Hanes and Gaston and Duffield and White be here at eleven o'clock. Will you get word to Blough?

Klotz: (Nods yes).

May 8, 1939
10:22 a.m.

Operator: Go ahead.

HMJr: Hello.

Allan Sproul: Hello, Mr. Secretary.

HMJr: How's my bullish friend in New York.

S: (Laughter) I still feel the same way but the market is going all right.

HMJr: Yes. Well, we spent so many billions one way and we might give them another eight this way.

S: Well, I think you're right on that.

HMJr: But that is the way I feel.

S: Yeah.

HMJr: But I -- I can't afford to take a risk for one-eighth.

S: Well, unless it develops that they after all.

HMJr: Well, I just can't afford it.

S: Yeah.

HMJr: I'd much rather be criticized for being too generous than to have an issue go flat.

S: Well, I think you're right on that.

HMJr: On a one-eighth basis?

S: Yes.

HMJr: But it ought to go and if everything's all right, why we'll tell them tonight that we'll close.

S: Well, there's -- I don't think there's any question about that.

HMJr: Right!

S: They'll need -- the market feels it's gotten a generous offer here.

HMJr: Well, that's all right, and when this is over we'll take a look at your -- your other nine hundred million.

S: Righto!

HMJr: Thanks for the help.

S: All right.

HMJr: Good bye.

S: Good bye.

May 8, 1939
12:54 a.m.

HMJr: Hello.

Operator: Blough. Go ahead.

HMJr: Hello.

Leroy Blough: Hello.

HMJr: Blough.....

B: Yes.

HMJr: I've thought this way -- I don't want to take to the White House the 'pros' and 'cons' at all.

B: All right.

HMJr: But just send me over the one so I won't be fumbling.

B: Yes.

HMJr: And leave out the 'pros' and 'cons'.

B: O. K.

HMJr: See?

B: All right.

HMJr: See?

B: You bet.

HMJr: All right.

Decy

Mr Bell gave copy to Hanes.

TREASURY DEPARTMENT

WASHINGTON

382

CONFERENCE AT 8:30 P. M., MAY 8, 1939,

AT THE HOME OF THE SECRETARY OF THE TREASURY

Those present besides the Secretary were Under Secretary Hanes, Jean Monnet, Special Representative of French Minister Daladier, and Mr. Bell.

It appears that Mr. Monnet came to this country at the request of the French Premier with a special letter to the President of the United States to discuss the possibilities of a settlement of the indebtedness of the Government of France to the United States. At lunch today the President advised the Secretary of the Treasury of Mr. Monnet's visit and discussed in a general way with him the conference that he had had with Mr. Monnet, and asked the Secretary of the Treasury to see him in order to determine whether there is any basis for negotiating a settlement of such indebtedness at this time. The President explained to the Secretary that there had been some suggestion from the French side that it pay on account in cash 10 or 15 per cent of the gold reserve of the Bank of France, which payment would amount to between $300,000,000 and $500,000,000, and that the French turn over to the United States as an additional payment on account of its indebtedness certain islands belonging to the French Government. The President said that he had advised Mr.

Monnet, jokingly, that he did not want the islands, but that in the case of war we would just take them, and on any basis they have no value. He intimated, however, that the islands in the Pacific might be worth considering as a landing base for a Pacific airplane route.

It further seems that the President had in mind a proposition something like the following: That we divide the indebtedness into two parts, namely, pre-armistice and post-armistice. Possibly we could cancel the pre-armistice debt as our contribution to the joint expense of the war. That the post-armistice debt, including both cash advances and war stocks, would be repaid over a period of years without interest; that the French might make a substantial payment on account, but that he thought three or four hundred million dollars was entirely too much to take from France's gold reserve in view of the gravity of the situation now confronting Europe, but that they might add to a smaller cash payment certain strategic war material under the control of the French Government. The President mentioned anti-aircraft equipment but Mr. Monnet said that the output of the French nation was not even sufficient for their own requirement; therefore, this suggestion could not mean any substantial payment on account. Mr. Monnet was asked if other materials, such as tin, nickel, manganese, rubber, etc., are available to the French Government which could be turned over to the United States as payment on account of its debt. He said probably some rubber could be acquired for this purpose.

The Secretary asked just what the picture would look like if we settled the debts on the basis suggested by the President. He was told that the principal amount of the obligations held by the Treasury for account of cash advances made prior to the Armistice aggregated $1,970,000,000 and the principal amount of the obligations held for advances made after the Armistice aggregated $1,027,477,800. In addition, the Treasury acquired obligations in a principal amount of $407,341,145.01 which represented the purchase price of surplus war materials sold to the French Government on credit in 1919 and 1920. This, therefore, made a total post-armistice indebtedness of approximately $1,434,000,000. Against this post-armistice indebtedness there had been repaid on account of principal of cash advances the sum of $64,302,901.29, so that the total principal indebtedness, exclusive of accrued and unpaid interest, at the time of the debt settlement amounted to $3,340,516,043.72, of which $1,970,000,000 represented the pre-armistice debt and $1,370,516,043.72 represented post-armistice indebtedness. This whole indebtedness, together with accrued and unpaid interest up to June 15, 1925, was consolidated and refunded under the terms of the debt agreement concluded April 29, 1926 between the United States and the Government of France. Total bonds issued to the Government of the United States under that debt agreement aggregated $4,025,000,000. Under that agreement the Government of France has paid to the United States on account of principal of the indebtedness $161,350,000 and on account of interest on the

bonds given to the United States under such agreement $38,650,000. No payments have been made since 1931.

I told the Secretary that there was one distinct disadvantage in considering the settlement of the French debt on a basis of the post-armistice indebtedness and the cancellation of the pre-armistice indebtedness for the reason that the principal amount of the post-armistice indebtedness of the Government of Great Britain to the United States, after deducting repayments and before refunding, amounted to only $508,000,000, whereas the pre-armistice indebtedness amounted to $3,566,000,000. Even though the American people would accept a settlement of the post-armistice indebtedness of the Government of France in full settlement of all of its indebtedness to this country, it is doubted whether they would grant the same terms to the British Government in view of the small amount borrowed by that Government after the Armistice. It should be remembered, however, that Great Britain has paid a total of $2,025,000,000 on account of its indebtedness to the United States, whereas France has paid only $486,000,000.

Mr. Monnet explained this in a general way as his conversation with the President, which was in substantial accord with what the President had told the Secretary at lunch. In discussing the general settlement he said that he would like to ask two questions which had been worrying him since his conference with the President, after which he had had time to think about the matter. One was what

attitude would the American public place upon a suggestion of a debt settlement at this time coming from the French Government. He said that it seemed to him that they might very well state that any settlement offered at this time would be for the purpose of enabling the French to borrow more money from the American people in order to wage another war. He added that there would undoubtedly be a great deal of criticism in the Congress of the United States of any settlement proposed at this time. We all agreed that he could certainly expect that. Then he said that being true, supposing there is a settlement and the objective of this settlement is to borrow further money from this country, would the American people buy French securities. He said he was of the opinion that they would not buy them in any unlimited amount. We all agreed that that was also our view. It seemed to him then, he said, that the French, even though they could make a settlement favorable to them from a strictly monetary standpoint, they would not attain their objective to borrow further funds.

The Secretary explained to him that last year the Government of Hungary submitted what he considered a very fair offer to settle that country's indebtedness to the United States, which settlement was submitted to the Congress of the United States. He said he talked to several Senators and Congressmen with a view to getting congressional action on that subject at the last session, but was told by several of these gentlemen that there was no desire on their part to effect a

settlement of the international debts due the United States because so long as they are outstanding and unpaid the chances of the United States being drawn into another European war are remote. On the other hand, if the debts are settled and the decks are clear, we run a much greater chance of being drawn into the next war.

The Secretary explained to Mr. Monnet that he had just heard about this suggestion at lunch and he had not had an opportunity to talk to Mr. Hanes and Mr. Bell about the matter and that he had not come to any definite conclusions about it. He said that we would study the matter and that in the course of the next few days he hoped he could call Mr. Monnet at his New York address and have him come down for another discussion of the matter.

After Mr. Monnet left we discussed the matter for a few moments and while we do not believe there is any chance of any debt settlements being accepted at this time by Congress, we did conclude that we should not turn down abruptly any suggestion of taking islands as a part payment on the French war debt, because if we take them under any French settlement which might be concluded we would establish a precedent and we might be able to get some very good islands, such as Bermuda and some islands in the Pacific, under any British settlement that we might be able to negotiate.

DWB

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE May 8, 1939

TO Secretary Morgenthau

FROM W. H. Hadley

Review of the Government Market

Week ending May 6, 1939

The government security market was strong and moderately active throughout the past week. There was considerable buying and buying demand by banks in New York and outside. In contrast to other markets, the governments continued to move into new high ground, the pressure of excess funds being the principal stimulant for this movement. Treasury bonds were up 1 to 17/32nds generally with issues callable in 8 years or more up an average of 1/2 point. Treasury notes showed mixed tendencies. The shorter issues were 1 to 6/32nds down while the longer issues were unchanged to 6/32nds better. The decline in the shorter issues, especially the September "rights", was the result of switching from these issues into long term bonds. Guaranteed issues were unchanged to 10/32nds better in sympathy with the strengthening in the direct obligations.

HOLC Refunding

The offering this morning (Monday) of 1 and 2-year notes in replacement of the maturing June notes of the H. O. L. C. was well received. The "rights", which were quoted 100.8 on Saturday, closed today at 100.12. The 3/8% 1-year notes closed at 100.7, and the 5/8% 2-year notes closed at 100.16. Most of the turn-ins on this issue will come late Tuesday or Wednesday. Today the exchanges in New York totaled about $34 million.

Dealers' Portfolios

Dealers' portfolios were reduced about $10 million during the week. Principal changes were a reduction of $10 million in Treasury bond holdings and $5 million in Treasury bill holdings. This was somewhat counteracted by an increase of about $6 million in H. O. L. C. issues, probably "rights".

(in millions)

	Week ended April 29	Week ended May 6	Net Change
Treasury bonds	24.8	15.1	- 9.7
Treasury notes (1 year)	16.2	20.2	+ 4.0
Treasury notes (1-5 yrs.)	32.0	28.2	- 3.8
Treasury bills	8.0	3.2	- 4.8
H. O. L. C. bonds	23.0	29.0	+ 6.0
F. F. M. C. bonds	2.2	0.4	- 1.8
	106.2	96.1	-10.1

Excluding Treasury bill operations, dealers' volume averaged about $130 million daily, of which a little more than $100 million was in Treasury bonds.

New Security Issues

There were no large offerings this week. Issues totaled $5,300,000, of which only about $1 million was for new capital. There were, however, municipal bond awards totaling $48,800,000.

Corporate Bond Market

The corporate market was firm and fairly active. Gains were recorded in all groups of the high and medium grade corporate bonds. Demand for high grade issues was quite pronounced but there was a limited supply and prices moved up an average of about 5/8ths of a point. Medium grade bonds

advanced about 1 point. Price levels in corporate issues are still considerably below the level prior to the reactions in March and April but from 1 to 2 points on average above the April low.

Treasury Investment Accounts

There were no commitments for purchases or sales in the New York market for Treasury investment account. However, there was an investment of $6 million in special 2% notes for Postal Savings and $800,000 in special 2% notes for account of Government Life Insurance Fund. Government Life now holds $17,100,000 of these special 2's and Postal Savings holds $107 million.

Federal Reserve System Account

Transactions in the System account were limited to replacement of a $39,830,000 Treasury bill maturity with various other Treasury bills, including about $26 million of the new issue. In addition to this replacement there were shifts in other Treasury bill issues totaling $9,777,000.

GC:A:LWC

MAY 8 - 1939

MEMORANDUM FOR MR. McREYNOLDS,
ADMINISTRATIVE ASSISTANT TO THE SECRETARY:

In re: Nicholas Roerich,
Docket No. 83065.

Pursuant to your oral request a brief history of the above-entitled case follows:

The case involves deficiencies in income tax, 25% delinquency penalties and 50% fraud penalties for the years 1926, 1927 and 1934. The deficiencies in taxes and penalties asserted in the deficiency notice dated December 2, 1935 were based upon a confidential report dated October 31, 1935 by Internal Revenue Agent F. L. Tuck of the Office of the Agent in Charge of the Upper New York Division.

The petitioner, Nicholas Roerich, a citizen of Russia and a holder of a French passport, came to this country in 1920. He has described his occupation as that of artist, scientist and writer. It appears that he was also a promoter of a certain religious cult.

Sometime after his arrival in the United States he became acquainted with certain wealthy individuals who were citizens of the United States, including one Louis L. Horch, at that time a wealthy foreign exchange broker in New York, New York. Mr. Roerich interested these wealthy United States Citizens to the extent that they contributed funds in large amounts from time to time which were used by Mr. Roerich in making extensive excursions or expeditions in Europe and Asia. He traveled in Europe and Asia on such expeditions from time to time during the years 1923 to 1934 inclusive, during which time he painted pictures which were sent back to the United States where they were purchased. The largest known purchases of such paintings were made by Mr. Louis L. Horch in 1926 and 1927. Profit from said purchases constitute the bulk of the petitioner's income as disclosed by the investigation of the Revenue Agent.

Memorandum for Mr. McReynolds,
In re: Nicholas Roerich, Doc. No. 83065.

During the year 1934 Mr. Roerich was also an employee of the Agriculture Department of the United States Government in which capacity he traveled in the Orient allegedly in search of drought resisting plants. Apparently Mr. Roerich has never returned to the United States since his employment by the Government in 1934 but bought an estate for some $30,000.00 American money in India, where he has since remained. His testimony was presented in the instant case by way of deposition taken before the United States Consul in India.

Mr. Roerich did not file any income tax returns for the years 1926, 1927 and 1934 (except a tentative return for 1934). Accordingly, the delinquency and fraud penalties were asserted. Petition was filed with the Board of Tax Appeals February 28, 1936. The case was tried in New York in February, 1938. The Board's findings of fact and opinion were promulgated September 21, 1938 (38 B. T. A. ____ No. 75) pursuant to which its decision was entered November 10, 1938.

The Board's decision sustained the Commissioner's determination of deficiencies in taxes for the most part for every year involved. It sustained the Commissioner's imposition of the delinquency penalties for every year involved but sustained the fraud penalty only for the year 1934.

A petition for review of the Board's decision was filed by the petitioner on February 6, 1939. The case has been set for trial on June 6, 1939 and will be tried at that time. No offers of compromise have been submitted and if any offers are submitted or if any change occurs in this case, you will, in view of your interest in the matter, be promptly advised.

E. H. Foley Jr.
E. H. Foley, Jr.,
Acting General Counsel.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE May 8, 1939

TO Secretary Morgenthau

FROM Mr. White

Subject: Mexican Exports of Petroleum

During the last nine months of 1938, Mexico's exports of petroleum and products decreased by 67 percent from $31 million in 1937 to $10 million in 1938.

Half of Mexico's exports went to the Netherlands West Indies when the Royal Dutch Shell had a very large petroleum refining plant. After the expropriation of the foreign oil properties by Mexico in March 1938, exports to that area ceased.

Exports to the United States decreased from $6.0 million in 1937 to $1.9 million in 1938, a decline of 69 percent. Exports to Great Britain dropped 42 percent and exports to all other countries declined 73 percent.

Exports to Germany dropped least -- from $2.4 million to $1.9 million.

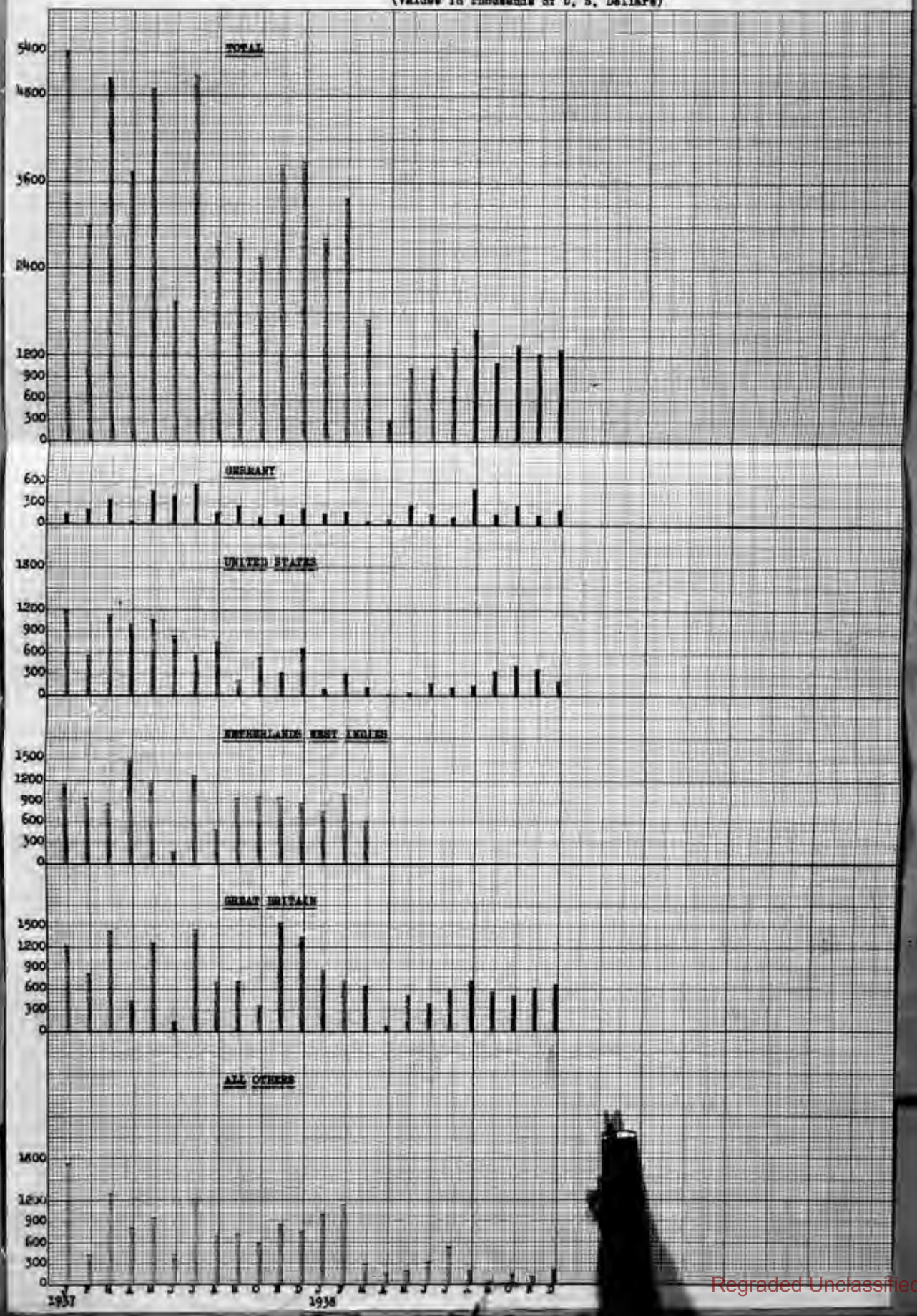
Mexico's Exports of Petroleum
(In thousands of U. S. dollars)

	From April to December (inc.) 1937	1938
Netherlands West Indies	8,325	-----
United States	5,959	1,860
Germany	2,361	1,898
Great Britain	7,939	4,607
All others	6,977	1,900
Total	31,561	10,264

(We now have detailed tables of Mexican exports of various oil products for 1937 and 1938. (1939 figures are not yet available.)

MEXICO - Exports of Petroleum and Products by Countries, Monthly from Jan. 1937

(Values in Thousands of U. S. Dollars)



Mexico - Exports of Petroleum and Products to Principal Countries, Monthly, January 1937 to Date

(Value in thousands of dollars) 1/

	Total	Germany	United States	Great Britain	Netherlands West Indies	All Other
1937						
Jan.	5,445	148	1,199	1,210	1,163	1,724
Feb.	2,982	208	564	817	957	436
Mar.	5,064	350	1,121	1,424	888	1,281
Apr.	3,736	42	991	435	1,464	805
May	4,894	471	1,051	1,262	1,171	939
June	1,960	408	837	122	161	432
July	5,078	567	569	1,457	1,273	1,211
Aug.	2,791	158	756	696	495	685
Sept.	2,821	251	228	704	940	698
Oct.	2,557	99	531	370	972	586
Nov.	3,852	141	328	1,551	970	862
Dec.	3,872	224	668	1,342	879	759
1938						
Jan.	2,835	137	75	872	768	983
Feb.	3,375	180	314	730	1,022	1,129
Mar.	1,700	23	127	648	610	291
Apr.	306	73	10	67	-	156
May	1,033	279	45	510	-	199
June	1,024	151	175	384	-	314
July	1,317	98	111	582	-	527
Aug.	1,572	501	148	728	-	195
Sept.	1,111	155	351	564	-	41
Oct.	1,368	275	431	516	-	146
Nov.	1,235	141	373	604	-	117
Dec.	1,298	225	216	652	-	205

1/ Converted from Pesos at average monthly rate of exchange.

RECONSTRUCTION FINANCE CORPORATION

WASHINGTON

JESSE H. JONES
CHAIRMAN OF THE BOARD

May 8, 1939

HENRY MORGENTHAU, JR.

Investment in one ticket on Johnstown to win	$5.00
Proceeds received from the investment	8.00
Taxable income	3.00

Cash inclosed

Jesse H. Jones
Agent

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION CONFIDENTIAL

DATE May 8, 1939

TO Secretary Morgenthau

FROM Mr. Haas

Subject: The Business Situation,
Week ending May 6, 1939.

The situation in brief

(1) Business continues to be held back by the coal strike, which is affecting activity in various lines, and by uncertainties abroad, which in some degree have been a factor retarding consumer purchases of durable goods such as houses and automobiles.

(2) Attention is being attracted to a sustained upturn in sensitive commodity prices in this country and abroad, accompanied by reports of European buying in various commodity markets. At the same time, stock prices have shown some improvement, following a period of stability on unusually low sales volume such as frequently marks the end of a prolonged decline.

(3) The price upturn seems particularly significant in occurring at a time when news from abroad continues unsettling, and when domestic business activity offers no stimulus to prices. The rise, if continued, will give a strong boost to business confidence in this country, and should bring out a considerable volume of domestic buying, since it catches industry in a light inventory position.

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Sales of durable consumer goods decline

The uncertain European situation, together with a clouded domestic business outlook and unseasonably cold weather, have caused a hesitation among consumers in buying houses and automobiles, as reflected in residential contract awards and automobile sales during April.

The F. W. Dodge residential awards for April (daily average) declined to $4,576,200, as compared with a March figure of $4,638,000. Seasonally, the April awards should have been about 23 per cent higher than in March. Some encouragement is seen, however, in an upturn at the end of the month (April 23-30), when the daily average rose to $5,915,500, though previous experience has shown this period of the month to be very erratic.

Retail automobile sales during April were lower than in March and below general expectations, whereas recent experience indicates that they should have shown a seasonal gain over March. Sales of 15 leading makes in April, according to the Wall Street Journal, totalled 286,465 units, which compare with 317,232 units sold during the previous month.

Responding to the unfavorable sales trend, and to higher than normal new-car stocks, automobile production this week was reduced sharply to 71,420 units, from 86,640 units produced last week. Ward's estimate of total automobile production for the second quarter has consequently been reduced to 850,000 units, which compares with expectations of about 1,000,000 units a month ago.

Steel activity slightly lower

The rate of steel operations this week was reduced slightly further to 47.8 per cent of capacity versus 48.6 per cent last week, continuing the sagging decline (partly seasonal) which began a month ago. As shown in Chart 1, the trend in recent months has been following approximately that of last year, but at a substantially higher level. In both years, it will be noted, no real spring upturn developed.

The week has seen some improvement in various sections of the industry. Tin plate orders are increasing, and operations of plate mills have been stepped up to 70 per cent of capacity, the highest rate of the year. The recent decline in steel activity has been halted in some districts, and a few sections report increased operations. U. S. Steel orders increased during the past week to 47 per cent of capacity, which compares with the low previous week's figure of 37 per cent.

Steel producers are economizing on coal consumption in various ways, partly by taking blast furnaces out of production. Of 22 blast furnaces taken off the active list recently, 16 have been banked, not blown out, which suggests that steel companies expect a resumption of steel buying in the near

future. The tighter steel situation in Europe is bringing increased inquiries for steel products from European and South American countries, according to reports in the trade. Important steel buying from the automobile companies for 1940 models is looked for by June 1.

Price rise continues

The recent upturn in commodity prices, which has continued without interruption through the current week, seems particularly significant as a business factor, since (1) it comes at a time when neither the European political situation nor the domestic demand situation are contributing to increased price confidence; (2) a price rise at this juncture would provide a powerful stimulus to business confidence, particularly in view of the light inventory position of industry; (3) basic conditions favor a reversal of the declining trend of business activity.

The action of stock prices recently, along with the rise in commodity prices, has tended toward increasing business confidence. During the past few weeks of war tension, coal strike, and declining business activity, stock prices in this country have held at a steady level and the volume of trading has diminished. Such a situation frequently marks the final stage of a decline. Stock prices abroad have been gradually improving, and our markets rose somewhat during the past week.

Business confidence, as measured by our confidence index derived from bond prices, has shown no further decline since mid-April (See Chart 2).

Industrial production lower in April

Preliminary data of the Federal Reserve Board indicate that in April the FRB index of industrial production declined 3 points to 95, owing principally to the sharp reduction in output of bituminous coal. The volume of manufacturing production was maintained close to the March rate, indicating that despite the war unsettlement of recent months, business in this country continues on a stable basis.

A factor contributing to business stability has been a well-maintained level of national income in recent months, and consequently a relatively high level of consumer buying.

In March, national income payments were at an annual rate of approximately $65.9 billions, as compared with $65.6 billions in February and $66.2 billions in January. Incomes of factory workers, making up a considerable portion of national income, have been aided during the first quarter of this year by a gain in factory employment in relation to industrial production. This represents a partial regaining of the lag between production and employment which became evident last fall. As shown in Chart 3, total factory employment during the first quarter of the year has been well maintained despite the substantial drop in production, while in the textile and steel industries employment has actually made sharp gains.

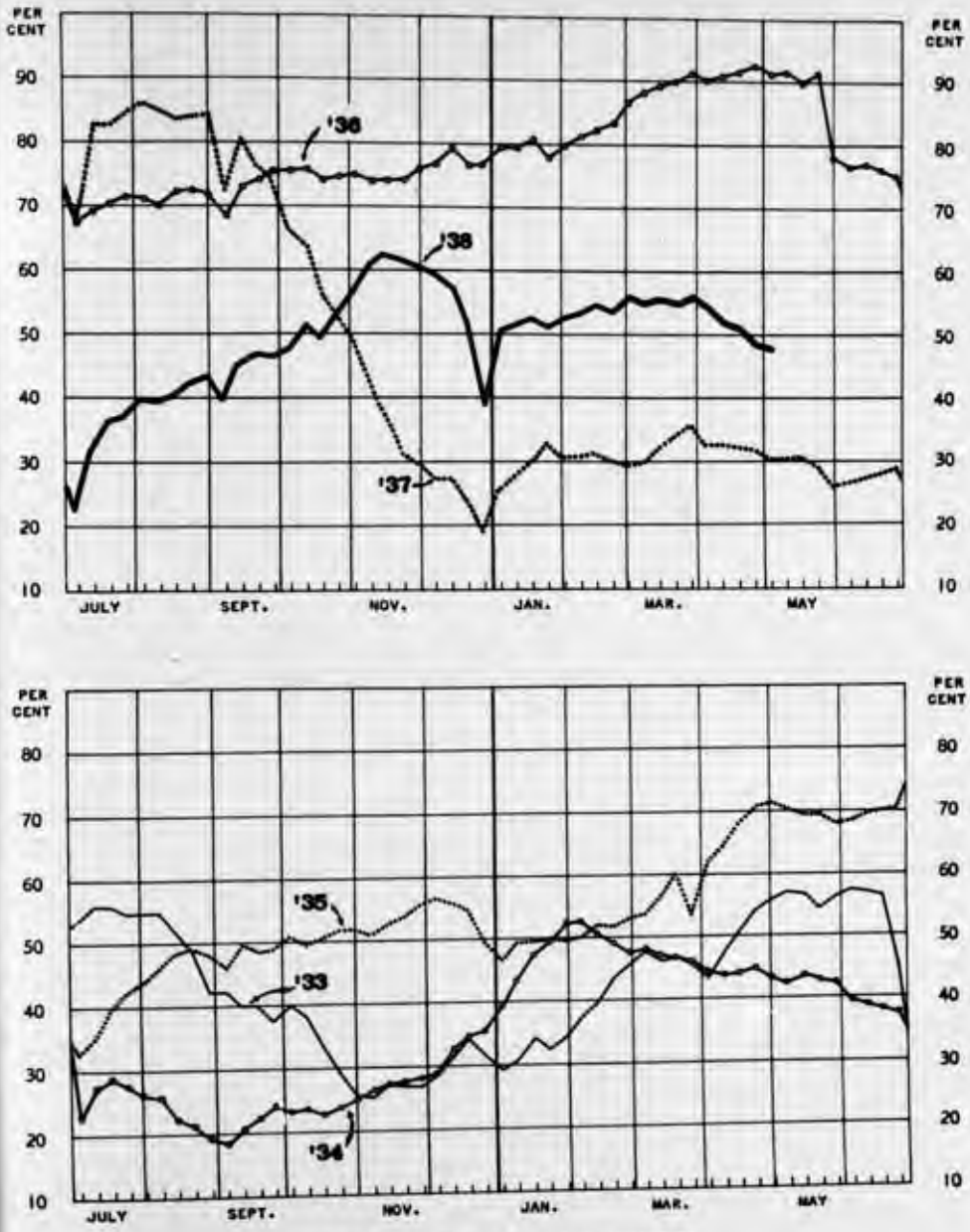
Current business news

Our new orders index for the last week of April (Shown in Chart 4) regained part of its previous week's loss with the upturn in steel orders. New orders for textiles fell off from the high figure of the previous week, but remained at a moderately favorable level, while orders for products other than steel and textiles held unchanged.

The New York Times index for the week ending May 1 held steady at 86.4, which compares with 86.2 for the previous week. A substantial upturn in the carloadings index, both for miscellaneous loadings and "all other", featured the week, offsetting moderate declines in all the other components. Preliminary data for the week ending May 6 indicate a slight decline in the adjusted index of steel production and a marked decline in the index of automobile production.

WEEKLY STEEL OPERATING RATE IN PERCENT OF CAPACITY

Comparison of Years Beginning July; 1933 to Date



SOURCE: AMERICAN IRON AND STEEL INSTITUTE

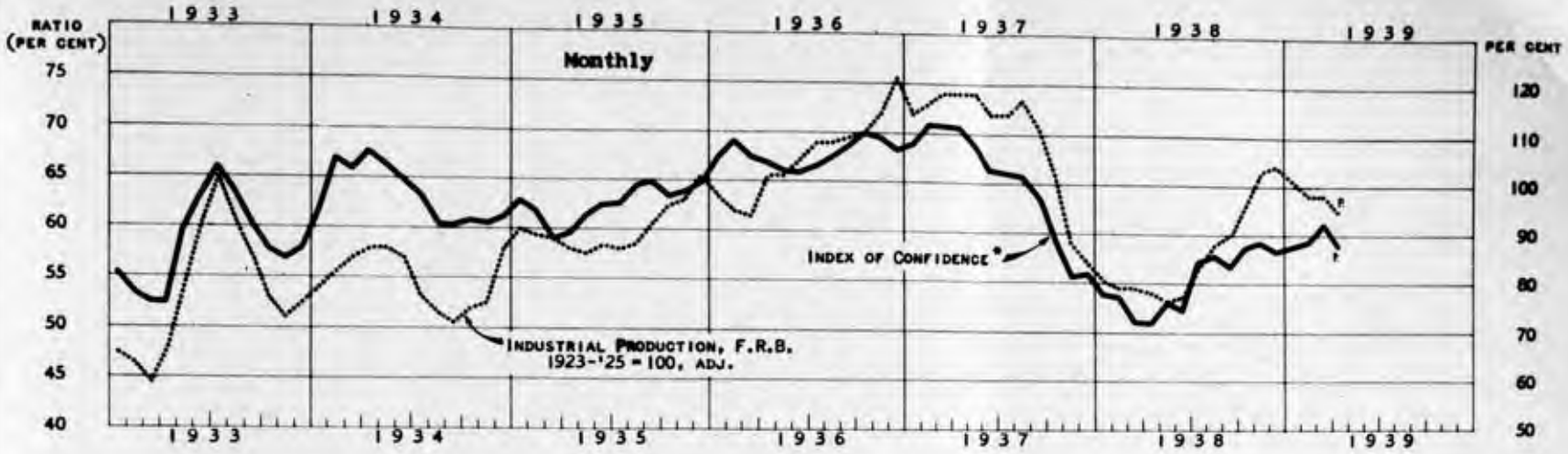
Office of the Secretary of the Treasury
Division of Research and Statistics

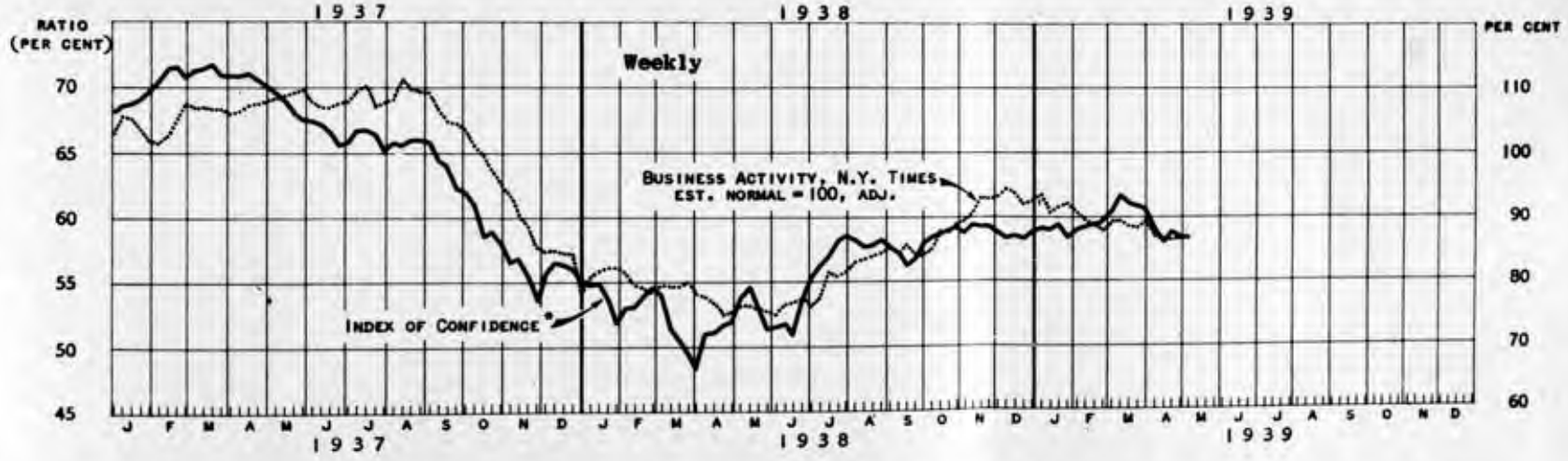
C - 246

402

Chart 2
CONFIDENTIAL

INDEX OF CONFIDENCE* AND BUSINESS ACTIVITY





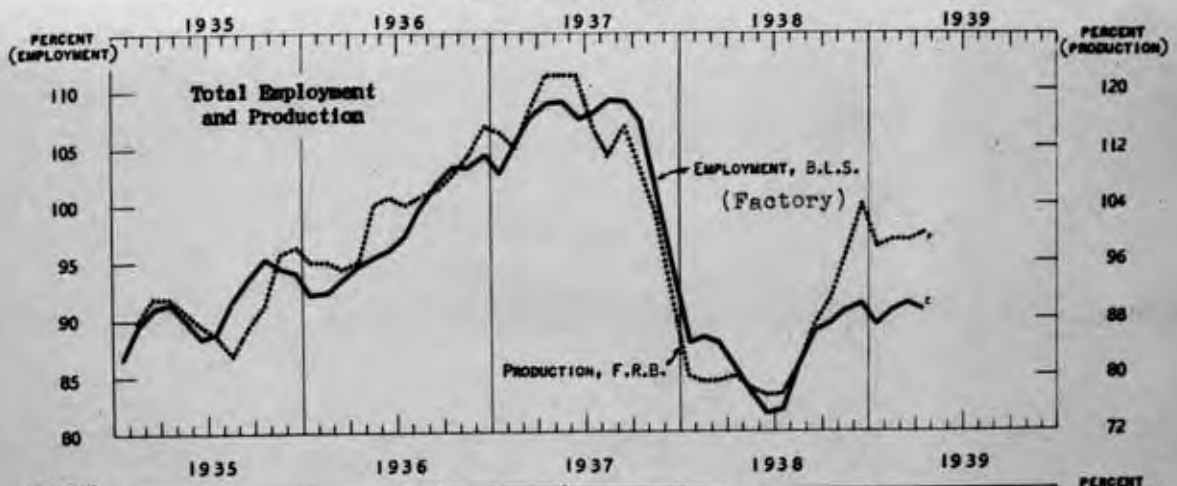
*RATIO OF YIELD ON MOODY'S AAA BONDS TO YIELD ON BAA BONDS.

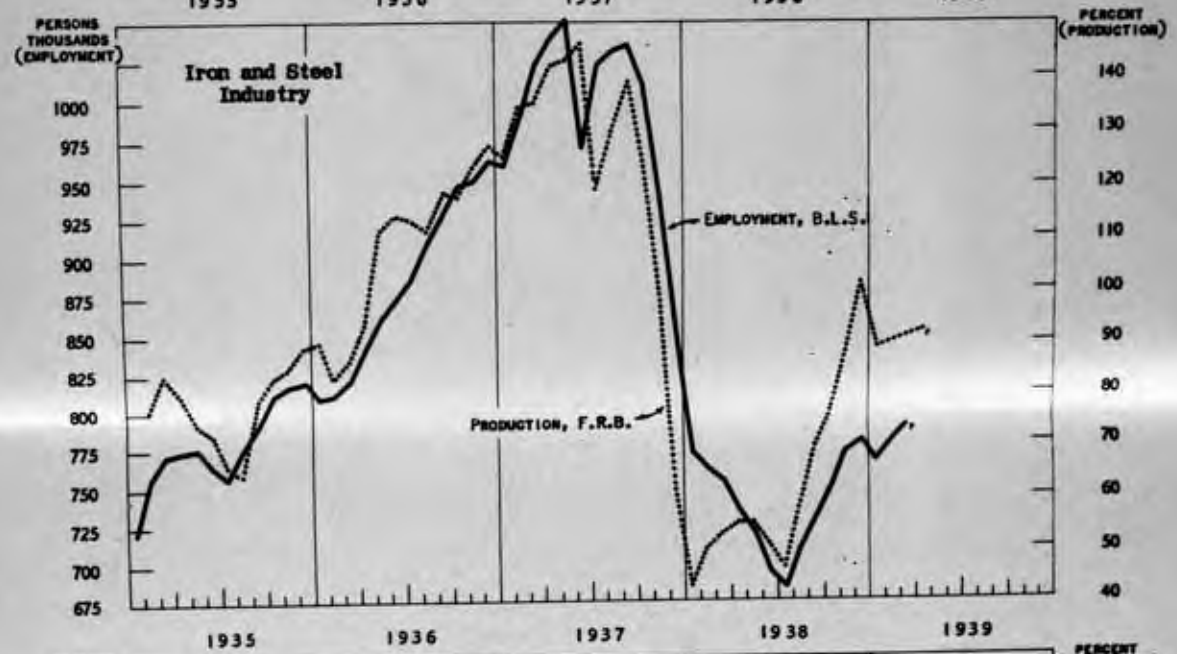
Office of the Secretary of the Treasury
Division of Research and Statistics

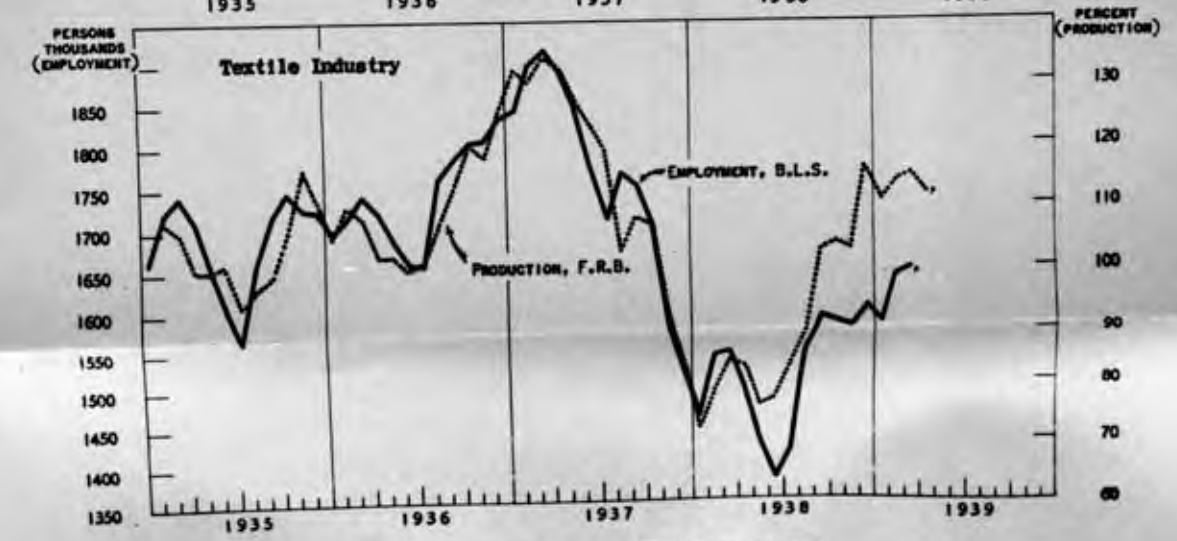
C - 264

Employment Current Month, Production Previous Month

1923 - '25 = 100, UNADJUSTED*







*IRON AND STEEL, AND TEXTILES, ACTUAL NUMBER EMPLOYED

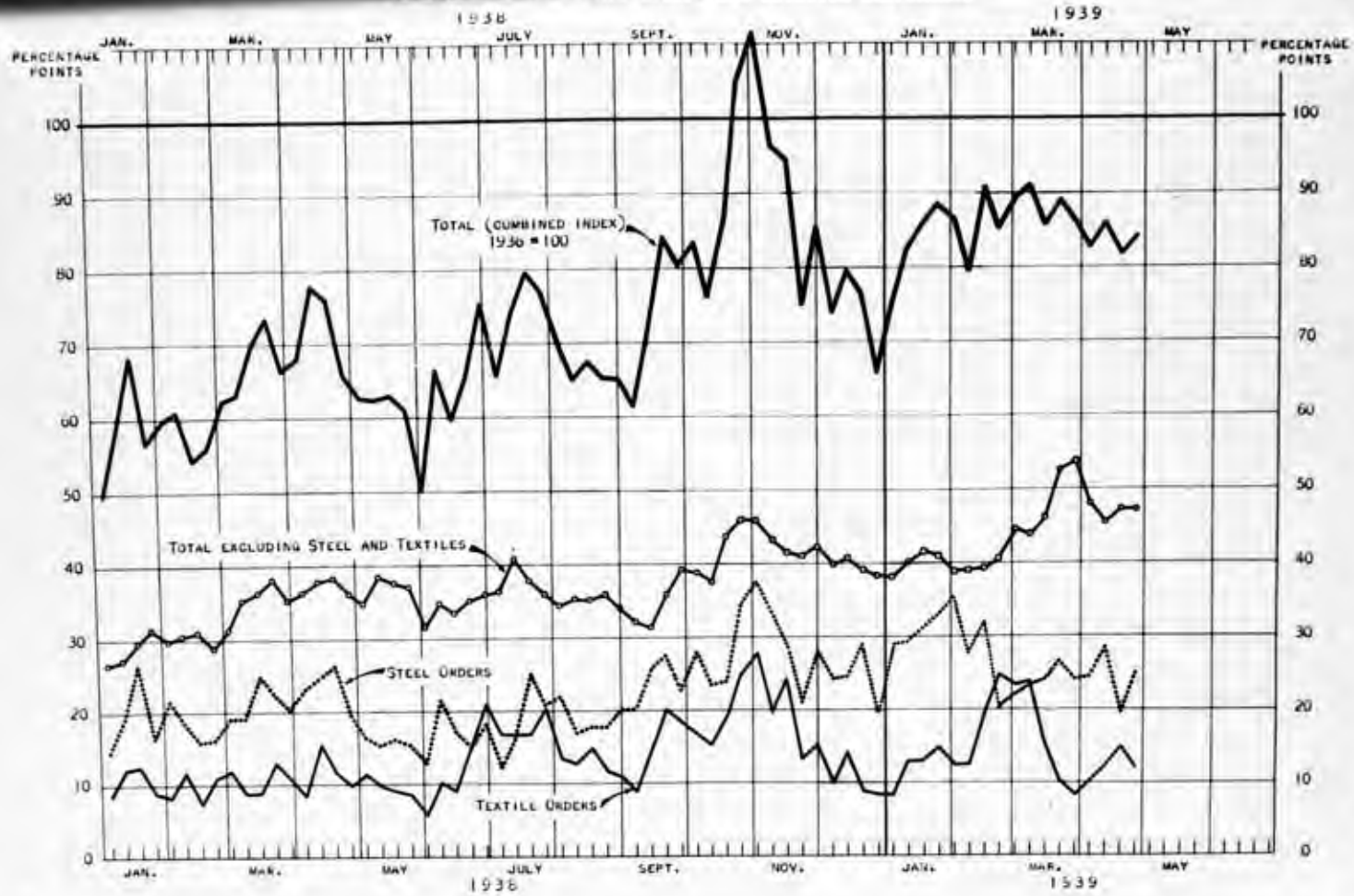
Office of the Secretary of the Treasury
Division of Research and Statistics

C - 256

Chart 3
CONFIDENTIAL

403

Combined Index of New Orders and Selected Components



Office of the Secretary of the Treasury
Division of Research and Statistics

I - BS - A

Chart 4

404

CONFIDENTIAL

May 8, 1939

Original in p.452

MEMORANDUM FOR THE SECRETARY:

Attached are two copies of the memorandum of October 24, 1938, which served as the basis of a conference which you and Mr. Hanes had with the President about that time.

The summary of the tax changes, together with the revenue increases and decreases, are shown on the folded last page, Exhibit 8.

HD/egh

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE October 24, 1938.

TO Mr. Hanes

FROM Mr. Blough RB

Subject: Methods of raising additional tax revenues.

To raise the specified sum of $2,000,000,000 additional annual revenue will probably necessitate all of the tax increases described below or their equivalents, unless business and national income increase substantially over present levels. A brief summary of the changes is shown in Exhibit A.

Whether the increased rates and new taxes described will in fact produce the required $2,000,000,000 is problematical, for three reasons: (1) The Division of Research and Statistics has found it physically impossible to prepare the estimates of yield for some of the taxes within the necessary time limit; (2) the estimates made thus far are for taxes considered each by itself without reference to the impact of one tax on the revenues from the others; and, most important, (3) the basis of the estimates has of necessity been the economy as it was situated before the imposition of the taxes, while in actual fact the shock of such a large increase in taxes in so short a time might so disrupt business and reduce the national income as to seriously affect the tax-producing capacity of the whole tax system. 1/

It is deemed impossible to increase the revenue by $2,000,000,000 in the current fiscal year 1938-39. Substantial increases in revenue might be secured for that year either by passing tax legislation at a special session of Congress before the end of the calendar year 1938, or by passing tax measures in the early months of 1939 retroactive to 1938. The disadvantages of either method are perhaps too obvious to require comment.

If the continuing tax changes described herein were passed during the regular 1939 session of Congress, substantial parts of the increases would be effective for the fiscal year 1939-40, but the program as a whole would not have its full effect on revenues until fiscal 1940-41, and in minor respects the full effect would be delayed until fiscal 1941-42 (due mainly to fiscal year income tax returns and delayed estate tax returns). To produce the desired revenue for fiscal 1939-40, special temporary legislation would accordingly be necessary. A brief summary of legislation to accomplish this result is shown in Exhibit B.

1/ Since the above was written, estimates and intelligent guesses of revenue yields indicate that the added revenue likely to be received from the described tax changes in a full year, at the probable 1939-40 level, would be short of $2 billions by about $200 millions. See Exhibit J.

In choosing among the limited number of possible tax sources an important objective has been to avoid as much as possible harmful repercussions on the economy. It is believed that this can be attained best by increasing the estate and gift taxes and the individual income tax before resorting to additional taxes on business, and by imposing additional general business taxes before resorting to sales and excise taxes. However, it has proved necessary to provide increased rates and new taxes even for the more undesirable tax types. In the following description of sources of additional revenue, the sources are listed roughly in what is believed to be their order of merit under existing conditions.

Estimates of yields of individual taxes and tax changes insofar as they are now available are shown in Exhibit J.

I. Estate Tax

1. Change the specific exemption from $40,000 to a specific exemption determined by aggregating the following exemptions allowable as a deduction from the gross estate. If the decedent is survived by:

(a)	A widow	$30,000
(b)	A widower	15,000
(c)	One orphan under 21	30,000
(d)	Each other child under 21	5,000

For administrative purposes a minimum specific exemption of $10,000 should, however, be allowed, irrespective of the number and type of beneficiaries. It is estimated that on average the effect of this proposal will be to reduce the specific exemption from $40,000 to between $20,000 and $25,000.

2. Increase the estate tax rates by adopting the rate schedule shown in Exhibit C. The combined effects of the changes in exemptions and rates are tabulated in Exhibit D and shown in graphic form in Exhibit E.

3. Eliminate the $40,000 estate tax insurance exclusion.

4. Pass a joint resolution in February 1939 eliminating the provision which allows an executor to value an estate as of the date one year after the decedent's death, and restricting the period for filing estate tax returns to twelve months instead of fifteen months after death as at present. The effect of this resolution would be to augment the revenues for the fiscal year 1939-40 to the extent that payment of estate taxes on the estates of decedents dying during the period April-June 1939 would otherwise have been deferred until after June 30, 1940. 1/

II. Gift Tax

1. Decrease the annual allowance of tax-free gifts per donee from $4,000 to $2,500.

2. Reduce the specific gift tax exemption from $40,000 to $15,000.

1/ After the estimates were prepared it would appear that the revenue increase in 1940 would not be great enough to warrant a special joint resolution.

3. Increase the gift tax rates to the same level as those proposed for the estate tax.

III. Income Tax

A. Individual income tax.

1. Reduce personal exemption to $800 for single individual and $2,000 for married person and head of family.

2. Compute both the normal tax credit of 10 percent of earned income and the lower and upper earned income limits of $3,000 and $14,000, respectively, on the amount of net income after deducting the personal exemption and credit for dependents, instead of before such deduction, as at present.

3. Increase the surtax rates by adopting the rate schedule shown in Exhibit F. The combined effects of the changes in exemptions, normal tax credit and rates are tabulated in Exhibit G-1 and G-2 and shown in graphic form in Exhibit H-1 and H-2.

4. Disallow the deduction for taxes paid other than business taxes and State personal net income taxes.

5. Restore the exemption of dividends from normal Federal income tax as under the Revenue Acts prior to 1936. This will act to reduce revenues but is deemed an important factor in tax equity in view of increases in individual and corporation rates.

6. Tax husbands and wives as units by aggregating their income, though permitting, at their option, the filing of separate returns. Under present law husbands and wives may file joint returns, or, at their option, separate returns. In the latter case the husband and the wife may each report and be taxed on such income as is viewed to be theirs under State property laws. In community property States the usual division is one-half of the community income to each spouse; the practice followed in other States is less uniform. This results in interstate variations of Federal income tax burden. In addition, the use of separate returns enables wealthy husbands and wives to avoid high surtax rates, which would otherwise be applicable. If the incomes of husbands and wives be considered as properly constituting a unit, existing practice is inequitable. To overcome such inequity the tax liability may be determined on the basis of the aggregate income of husband and wife, the liability then being prorated to each according to the amount of his income. Since many people believe equity would thus be increased and since the change would produce very substantial revenue, the proposal is included here.

7. Impose income normal tax and surtax on (a) salaries of State and local officials and employees, and (b) interest from future issues of Federal, State and local obligations.

8. Amend section 117(c), providing alternative taxes on capital gains and losses, by substituting 50 percent for 30 percent wherever it appears, so that capital gains will bear their due share in the increased individual income tax rates.

9. Change the limit on surtax on gains from sale of oil and gas properties prospected by individuals from 30 percent of sale price to 50 percent of sale price. (Section 105, Revenue Act of 1938.)

10. Change the treatment of capital losses (a) by providing a carry-forward of long-term losses (not offset against long-term gains or other income) for a period of three years, against long-term gains; and (b) by extending the short-term carry-over of losses to three years.

11. The basis for determining capital gains for property previously transmitted at death (Section 113(a)(5) shall be the basis of the property in the hands of the decedent instead of the fair market value at the time of acquisition. The basis for determining loss shall be the basis so determined or the fair market value of the property at the time of death, whichever is lower. This procedure for determining capital gains and losses is the same as that now in force for property acquired by gift. Capital gains not previously realized or subject to income tax would thus become taxable to the beneficiary if the property were sold or exchanged, eliminating in part a tax loophole for capital gains in the present income tax law.

12. Allow net business losses of individuals (to include losses from partnerships) and fiduciaries to be carried forward for a period of three or more years (from year of origin of loss) to be offset against business income but not other income. The first possible year of origin should be the taxable year beginning during 1939. This change will therefore not affect the revenues for the fiscal year 1940. The purpose of the change is to reduce the inequity in taxing fluctuating incomes now present in the law, which inequity becomes very serious with high rates of tax.

B. Corporation income tax.

1. Allow a net loss carry-over for purposes of all corporate income taxes for a period of three or more years from the year of origin. In computing the carry-over, adjust the net loss by disallowing all depletion deduction not based on cost or March 1, 1913 value and adding tax-exempt interest and the remaining 85 percent of dividends received. The first year of origin should be the taxable year beginning during 1939. This change reduces the revenue but in view of increased business taxes it is deemed desirable to reduce the inequity involved in taxing fluctuating incomes by allowing the carry-over. This change will not affect the revenues for the fiscal year 1940.

2. Increase the corporate income tax rates sufficiently to produce at least enough revenue to offset the effects of the loss carry-over (1. above), in an average year.

3. Lower the percentages for depletion deduction from 27½ percent of gross income in the case of gas and oil properties to 13-3/4 percent; from 23 percent of gross income in the case of sulphur mines or deposits to 11½ percent; from 15 percent for gross income in the case of metal mines to 7½ percent; and from 5 percent in the case of coal mines to 2½ percent.

4. Impose corporation income tax on interest from future issues of Federal, State and local obligations.

C. Temporary income tax.

The increased revenues derived from changes in income taxes will be reflected only in part in the fiscal year 1939-40. With respect to corporations the discrepancy between the full year's application of the changes and their fiscal year 1940 effects is negligible. If, however, the revenue from individual income taxes in that year is to be equal to the revenue resulting from a full year's application of the changes, an additional income tax may be imposed payable on March 15 and June 15, 1940 only, this tax to be a sufficient percentage of the income tax due for the taxable year 1939 to make up the revenue deficiency.

This tax will be necessary only if it is desired to secure full revenue increases in the fiscal year 1939-40.

IV. Other Business Taxes

A. Capital stock and excess profits taxes.

Repeal the capital stock tax, effective for the July 1940 payment, and the excess profits tax, effective for the taxable year ending after June 30,1940. The repeal of these taxes reduces the revenue, but because of the undesirable nature of the taxes, it is deemed desirable to supply the revenue from the business privilege tax discussed in C below.

B. Unincorporated business privilege tax.

Impose a 2 percent tax on "privilege net income" of unincorporated business enterprises including any trade or business which, if conducted or engaged in by a corporation, would be taxable under the income tax, but

excluding the professions and any cases in which more than 80 percent of the gross income is derived from the personal services rendered by the individual or the members of the partnership or other entity in which capital is not a material income-producing factor. "Privilege net income" is defined in all respects in the same manner as the net income of corporations is defined under the Revenue Act of 1938 except that (a) tax-exempt interest on Government obligations held in connection with carrying on trade or business shall be included in the taxable base; (b) deductions shall not be allowed for (1) rent paid on business property, (2) taxes paid on business property, (3) interest paid for capital engaged in the business, and (4) depreciation of buildings; and (c) the deduction on account of the personal service of an individual or member of a partnership shall in no case exceed $5,000 per such individual or member. A specific exemption of $5,000 is allowed for each enterprise.

C. Corporation privilege tax.

Impose a 4 percent tax on the privilege net income of corporations defined as in (1) above, except for the limitation in (c) which does not apply. A specific exemption of $5,000 is allowed.

A comparison of the base for the corporation privilege tax and the corporation income tax by major industrial groups is shown in Exhibit I.

The ~~taxes proposed in (1) and (2) above~~ shall be payable in two installments on March 15 and June 15. The purpose of these payment dates is to secure additional needed revenue in fiscal 1939-40; otherwise four installments might be allowed as in the income tax.

V. Excise Taxes

1. Increase the excise tax on beer from $5 per barrel to $7.

2. Increase the excise tax on distilled spirits, except brandy, from $2.25 per gallon to $2.50 per gallon, and levy a corresponding floor stock tax.

3. Shift the present tax on radio parts to a tax on completed radios and increase the rate to 10 percent.

4. Impose a tax on the gross receipts of radio broadcasting companies.

5. Increase by 50 percent the rates of tax on the manufacture of cigars, tobacco, and snuff. The present rates on cigars are from 75 cents per thousand to $13.50 per thousand, depending upon the weight; and on tobacco and snuff, 18 cents per pound.

6. For the period from date of enactment to June 30,1940, increase the gasoline tax from 1 cent per gallon to 2 cents per gallon, and thereafter decrease the rate from 2 cents per gallon to 1½ cents per gallon.

7. Substitute for the present taxes on the transfer of bonds and stocks, a tax based on the sale price thereof at the rate of 1/4 of 1 percent in both instances. The present rates are

Bonds - 4 cents per $100 face value;
Stocks- 4 cents per $100 par or face value or fraction, or if without par or face value, 4 cents per share. However, if selling price is $20 or over, whether with or without par or face value, the rate is 5 cents instead of 4 cents.

8. Reenact the check tax which lapsed December 31, 1934. The rate of this tax was 2 cents per check or draft.

9. Reduce the present exemption under the 10 percent admission tax from 40 cents to 20 cents.

Exhibit A

Summary Statement of Described Methods of Increasing Tax Revenues

Estate Tax

- Decreased exemptions
- Greatly increased rates, except in top brackets
- Elimination of deduction of insurance
- Other changes

Gift Tax

- Decreased exemptions
- Increased rates to equal new estate tax rates

Income Taxes

- Greatly increased personal surtax rates, except in top brackets
- Decreased personal and family exemptions
- Aggregation of family incomes for tax computation
- Imposition of Federal personal and corporation income taxes on: (1) interest from future issues of Federal, State, and local bonds; (2) exempt State and local salaries
- Increased corporation income tax rates (to be offset in future years by loss carryover)
- Other changes

New business privilege tax on corporations and unincorporated business (present capital stock and excess profits taxes to be repealed)

Excise Taxes: increased rates on

- Beer
- Distilled spirits
- Tobacco (other than cigarettes)
- Gasoline
- Transfers of stocks and bonds
- Admissions (by decreasing exemptions)
- Radios

New excise taxes on

- Checks
- Radio broadcasting companies

Exhibit B

Additional Tax Changes to Increase Revenues in Fiscal Year 1939-1940

Estate Tax

Joint resolution to be passed in February 1939 eliminating the provision which allows an executor the option of valuing an estate as of the date one year after the decedent's death, and restricting the period of filing estate tax returns to 12 months instead of 15 months after death as at present.

Income Taxes

Temporary emergency tax on individuals and corporations computed as a percentage of the income tax on 1939 incomes, payable March 15 and June 15, 1940.

Excise Taxes

Additional 1/2 cent a gallon on gasoline for the fiscal year 1939-1940 only.

Exhibit C

Proposed estate tax rate schedule

Taxable base: net estate after specific exemption 1/ (dollars in thousands)	Size of bracket (dollars in thousands)	Bracket rate	Cumulative tax
$ 0 - $ 5	$ 5	4	$ 200
5 - 10	5	8	600
10 - 20	10	12	1,800
20 - 30	10	16	3,400
30 - 40	10	20	5,400
40 - 60	20	23	10,000
60 - 80	20	26	15,200
80 - 100	20	29	21,000
100 - 150	50	32	37,000
150 - 200	50	35	54,500
200 - 250	50	38	73,500
250 - 300	50	41	94,000
300 - 400	100	44	138,000
400 - 500	100	47	185,000
500 - 600	100	50	235,000
600 - 800	200	53	341,000
800 - 1,000	200	56	453,000
1,000 - 2,000	1,000	59	1,043,000
2,000 - 5,000	3,000	62	2,903,000
5,000 - 10,000	5,000	64	6,103,000
10,000 - 15,000	5,000	66	9,403,000
15,000 - 20,000	5,000	68	12,803,000
20,000 - 30,000	10,000	70	19,803,000
30,000 - 50,000	20,000	72	34,203,000
50,000 and over		73	

Treasury Department, Division of Tax Research October 24, 1938

1/ The specific exemption is the sum of the following: For a widow, $30,000; a widower, $15,000; first orphan under 21, $30,000; and each other child under 21, $5,000.

EXHIBIT D.

Estate tax: Comparison of amounts of tax and effective rates on selected sizes of net estate (before exemption) under the present law and under the proposal

Net estate before exemption 1/ (in thousands)	Amounts of tax: Present law	Amounts of tax: Proposal	Effective rates: Present law	Effective rates: Proposal
$ 25	-	$ 200	-	.8%
30	-	600	-	2.0
40	-	1,800	-	4.5
50	$ 200	3,400	.4%	6.8
60	600	5,400	1.0	9.0
80	2,000	10,000	2.5	12.5
100	4,200	15,200	4.2	15.2
200	19,800	47,500	9.9	23.8
400	58,600	129,200	14.7	32.3
600	103,400	225,000	17.2	37.5
800	154,200	330,400	19.3	41.3
1,000	211,000	441,800	21.1	44.2
2,000	543,600	1,031,200	27.2	51.6
4,000	1,388,800	2,270,600	34.7	56.8
6,000	2,460,200	3,530,200	41.0	58.8
8,000	3,658,200	4,810,200	45.7	60.1
10,000	4,936,600	6,090,200	49.4	60.9
20,000	11,635,800	12,789,400	58.2	63.9
40,000	25,435,000	26,988,600	63.6	67.5
60,000	39,334,600	41,488,400	65.6	69.1
100,000	67,334,600	70,688,400	67.3	70.7

1/ The exemption under the proposal on the basis of 1936 data is on average $21,132. For the purpose of this computation, however, a $20,000 exemption was assumed.

Exhibit E

47
147

EFFECTIVE ESTATE TAX RATES PRESENT LAW AND PROPOSAL

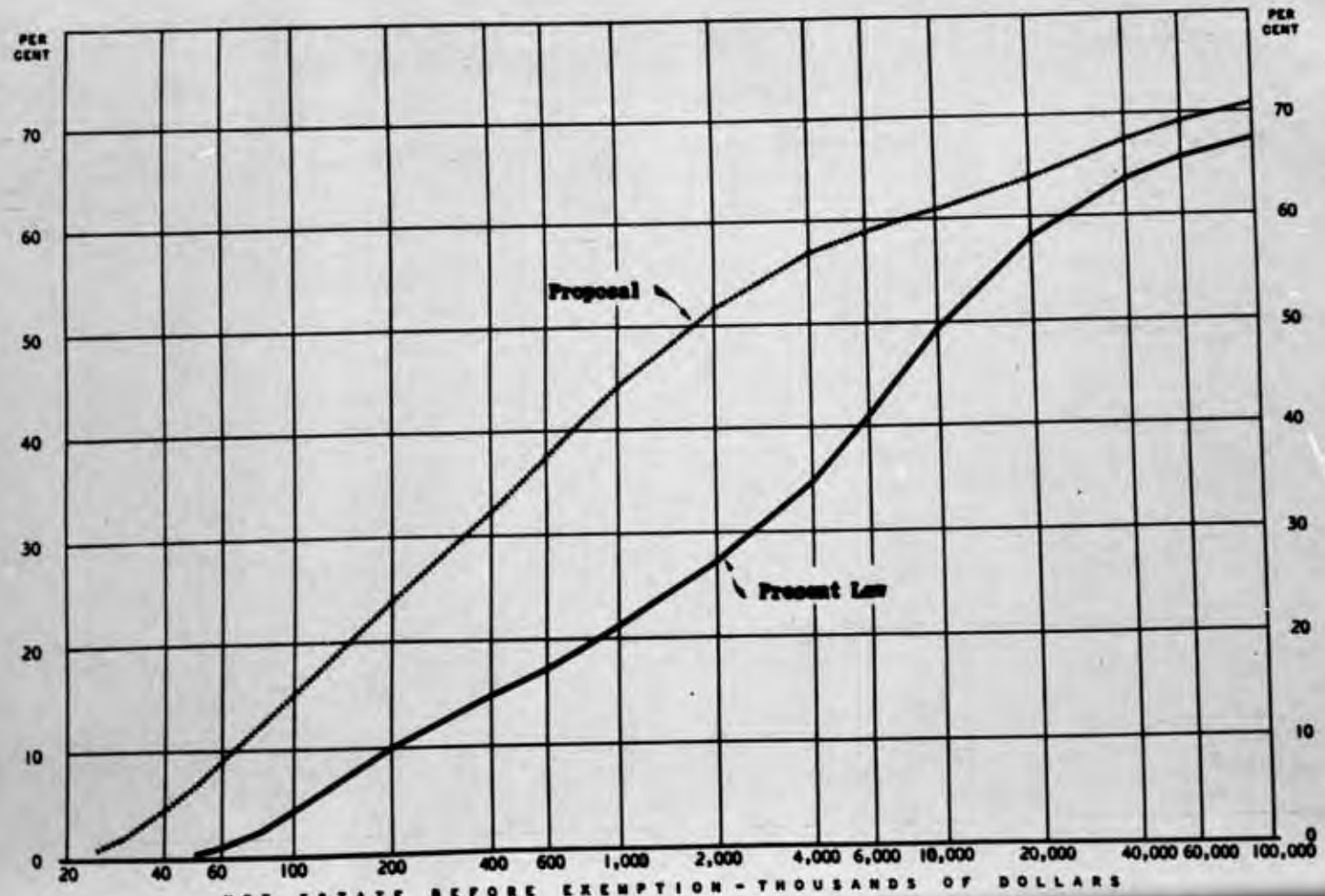


Exhibit F

Proposed individual income surtax rate schedule

Amount of surtax net income: (In thousands)	Rate of tax (Percent)	Total surtax cumulative
0 - .5	-	-
.5 - 1	2	10
1 - 2	3	40
2 - 3	5	90
3 - 6	7	300
6 - 8	10	500
8 - 10	12	740
10 - 12	15	1,040
12 - 14	18	1,400
14 - 16	21	1,820
16 - 18	25	2,320
18 - 20	29	2,900
20 - 22	33	3,560
22 - 24	37	4,300
24 - 28	41	5,940
28 - 34	45	8,640
34 - 40	49	11,580
40 - 48	53	15,820
48 - 56	56	20,300
56 - 64	58	24,940
64 - 72	60	29,740
72 - 80	62	34,700
80 - 90	64	41,100
90 - 100	65	47,600
100 - 150	66	80,600
150 - 200	67	114,100
200 - 300	68	182,100
300 - 500	69	320,100
500 - 750	70	495,100
750 - 1,000	72	675,100
1,000 - 2,000	73	1,405,100
2,000 - 5,000	74	3,625,100
5,000 and up	75	

EXHIBIT G-1.

Single person with no dependents: Comparison of the amount of income tax liability and effective rate of tax under present law and under proposal

Selected net income (thousands of dollars)	Amount of tax 1/		Effective rate	
	Present law	Proposal 2/	Present law	Proposal 2/
$ .5	-	-	-	-
1	-	$ 7	-	0.7%
2	$ 32	59	1.6%	3.0
2.5	50	92	2.0	3.7
3	68	129	2.3	4.3
6	216	431	3.6	7.2
8	378	679	4.7	8.5
10	560	975	5.6	9.8
12	762	1,323	6.4	11.0
14	984	1,731	7.0	12.4
16	1,234	2,204	7.7	13.8
18	1,514	2,752	8.4	15.3
20	1,834	3,380	9.2	16.9
22	2,194	4,088	10.0	18.6
24	2,594	4,876	10.8	20.3
28	3,454	6,644	12.3	23.7
34	4,854	9,552	14.3	28.1
40	6,384	12,700	16.0	31.8
48	8,714	17,228	18.2	35.9
56	11,394	22,004	20.3	39.3
64	14,514	26,948	22.7	42.1
72	18,074	32,052	25.1	44.5
80	22,034	37,316	27.5	46.6
90	27,494	44,100	30.5	49.0
100	33,354	50,992	33.4	51.0
150	64,324	85,984	42.9	57.3
200	96,304	121,476	48.2	60.7
250	129,284	157,468	51.7	63.0
300	163,264	193,468	54.4	64.5
400	233,244	266,460	58.3	66.6
500	305,224	339,460	61.0	67.9
750	490,204	524,452	65.4	69.9
1,000	680,184	714,436	68.0	71.4
2,000	1,450,174	1,484,428	72.5	74.2
5,000	3,790,164	3,824,420	75.8	76.5

1/ Maximum earned income allowed.
2/ Basis of tax computation for proposal: Personal exemption $600 allowed as a deduction for both normal and surtax; earned income credit of 10 percent and the lower and upper earned income limits of $3,000 and $14,000 maximum, computed on net income after deducting personal exemption; proposed increased surtax rates; and normal tax 4 percent.

EXHIBIT G-2.

Married person with two children: Comparison of the amount of income tax liability and effective rate of tax under present law and under proposal

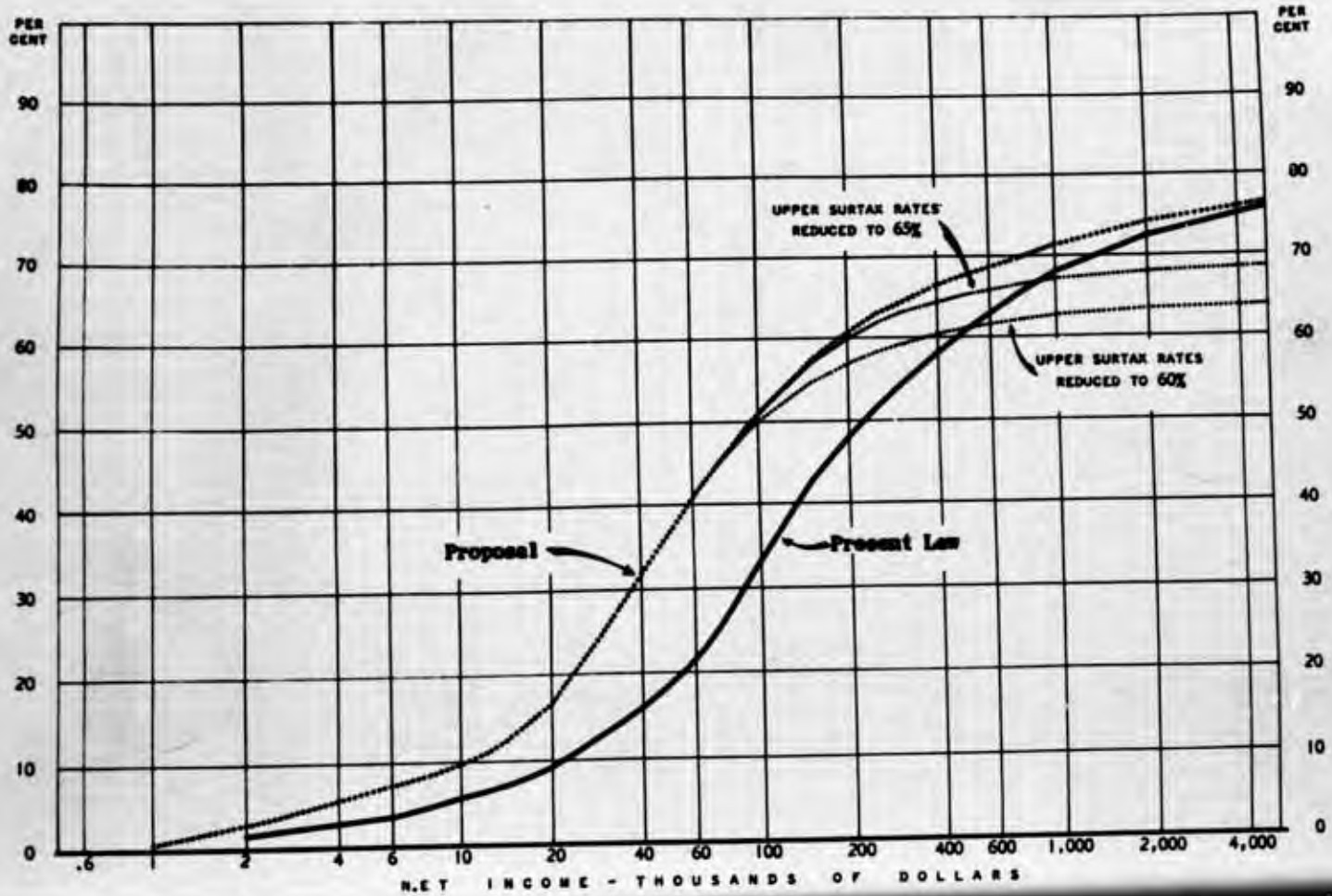
Selected net income (thousands of dollars)	Amount of tax 1/		Effective rate	
	Present law	Proposal 2/	Present law	Proposal 2/
$ .5	-	-	-	-
1	-	-	-	-
2	-	-	-	-
2.5	-	-	-	-
3	-	$ 7	-	0.2%
6	$ 84	219	1.4%	3.7
8	184	431	2.3	5.4
10	343	679	3.4	6.8
12	522	975	4.4	8.1
14	721	1,323	5.2	9.5
16	948	1,731	5.9	10.8
18	1,195	2,204	6.6	12.2
20	1,469	2,752	7.3	13.8
22	1,783	3,380	8.1	15.4
24	2,137	4,088	8.9	17.0
28	2,951	5,744	10.5	20.5
34	4,305	8,572	12.7	25.2
40	5,779	11,640	14.4	29.1
48	8,001	16,088	16.7	33.5
56	10,589	20,804	18.9	37.2
64	13,577	25,708	21.2	40.2
72	16,993	30,772	23.6	42.7
80	20,861	35,996	26.1	45.0
90	26,229	42,740	29.1	47.5
100	31,997	49,612	32.0	49.6
150	62,898	84,584	41.9	56.4
200	94,832	120,056	47.4	60.0
250	127,766	156,028	51.1	62.4
300	161,700	192,028	53.9	64.0
400	231,634	265,000	57.9	66.3
500	303,568	338,000	60.7	67.6
750	488,502	522,972	65.1	69.7
1,000	678,436	712,916	67.8	71.3
2,000	1,448,403	1,482,888	72.4	74.1
5,000	3,788,370	3,822,860	75.8	76.5

1/ Maximum earned income allowed.
2/ Basis of tax computation for proposal: Personal exemption $2,000 allowed as a deduction for both normal and surtax; earned income credit of 10 percent and the lower and upper earned income limits of $3,000 and $14,000 maximum, computed on net income after deducting personal exemption and credit for dependents; proposed increased surtax rates; and normal tax 4 percent.

421 Exhibit H-1

EFFECTIVE INDIVIDUAL INCOME TAX RATES, PRESENT LAW AND PROPOSAL

Single Person with No Dependents



422 Exhibit H-2

EFFECTIVE INDIVIDUAL INCOME TAX RATES, PRESENT LAW AND PROPOSAL

Married Person with Two Dependents

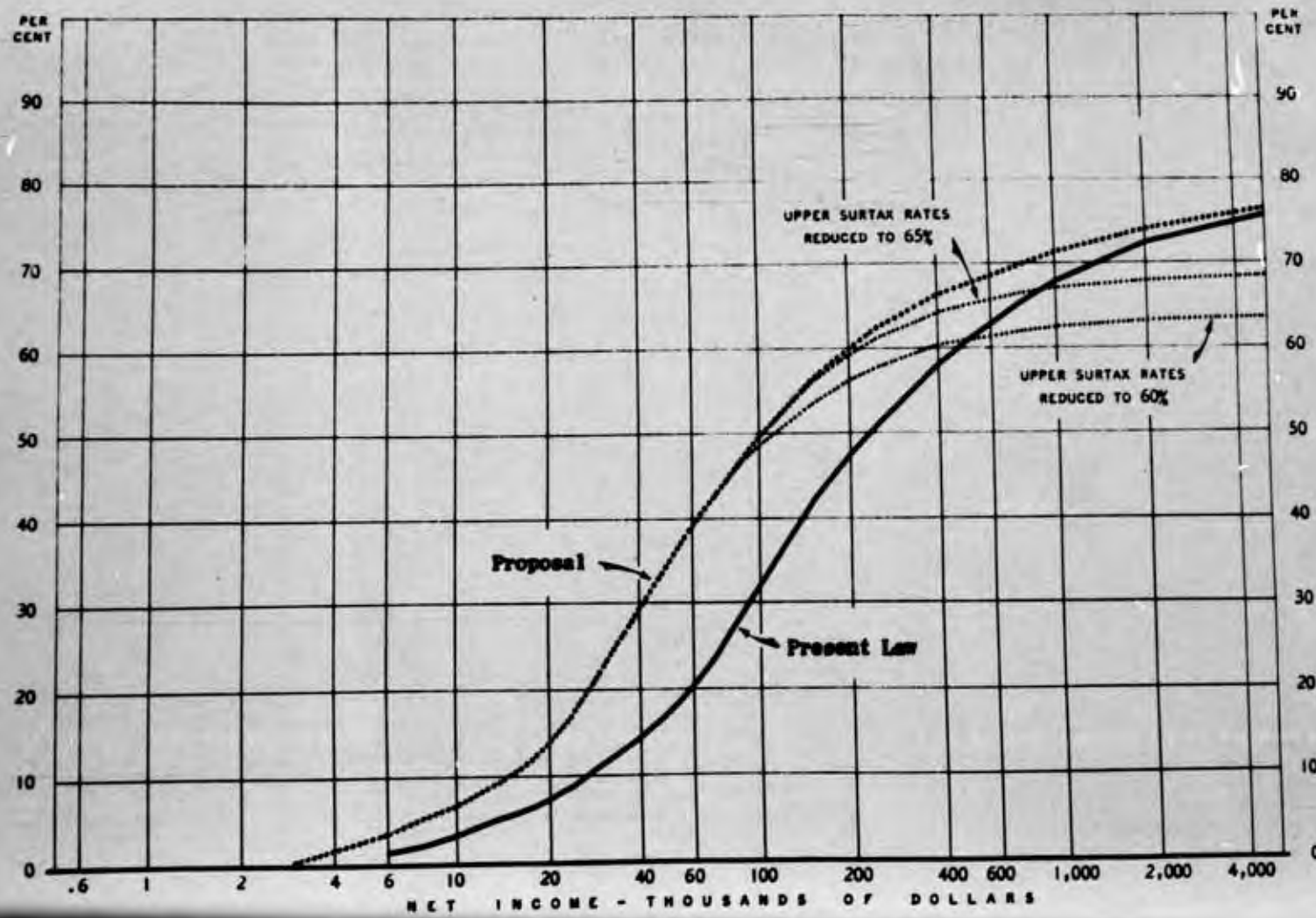


Exhibit I

Comparison of proposed tax base and present tax base for corporations with net income, 1935

Industrial groups	Privilege tax net income--proposed base	Net income 1/	Ratio of proposed to present base
	(In millions of dollars)		
Agriculture	97	45	2.2
Mining and quarrying	320	167	1.9
Manufacturing:			
Food	618	326	1.9
Liquors	297	108	2.8
Tobacco	188	101	1.9
Textiles	337	172	2.0
Leather	73	48	1.5
Rubber	91	31	2.9
Forest products	81	39	2.1
Paper, pulp, etc.	176	93	1.9
Printing, etc.	237	142	1.7
Chemicals, etc.	829	390	2.1
Stone, clay, etc.	151	91	1.7
Metal, etc.	1,532	900	1.7
Manufacturing n.e.c.	164	110	1.5
Total manufacturing	4,772	2,551	1.9
Construction	87	49	1.8
Transportation	2,908	957	3.0
Trade	1,665	776	2.1
Service	361	128	2.8
Finance	2,004	713	2.8
Nature of business not given	1	-	-
Grand total	12,216	5,389	2.3

Source: "Statistics of Income".

1/ Income reported plus 15 percent of dividends from domestic corporations; such dividends having been made taxable on incomes after 1935.

Exhibit 2. Estimates of revenue effects [illegible] included in the memorandum

The estimates are arranged and numbered in the same order in which the memorandum [illegible] in the memorandum. The figures given below are revenue estimates prepared by the Bureau of Research and Statistics, Treasury Department, except those [illegible]. The latter figures are only intelligent guesses and may be wholly in error.

Detailed estimates	Estimated increase in revenue: First full year 1/	Estimated increase in revenue: Fiscal year 1940	Summary: Estimated increase in revenue: First full year 1/	Summary: Estimated increase in revenue: Fiscal year 1940
	(Millions of dollars)			
I. Estate tax				
1. Change the specific exemption from $40,000 to a specific exemption determined by aggregating the following exemptions allowable as a deduction from the gross estate irrespective of the actual nature of the distribution of the estate to the beneficiaries. If the decedent is survived by: (a) A widow, $30,000; (b) a widower, $15,000; (c) one orphan under 21, $10,000; (d) each other child under 21, $5,000. A minimum specific exemption of $10,000 should, however, be allowed irrespective of the number and type of beneficiaries	27.1	5.1		
2. Increase the estate tax rates by adopting the rate schedule shown in Exhibit C	216.6	43.8		
3. Eliminate the $40,000 estate tax insurance exclusion	4.3	4		
4. Pass a joint resolution in February 1939 eliminating the provision which allows a decedent to value an estate as of the date one year after the decedent's death, and restricting the period for filing estate tax returns to twelve months instead of fifteen months after death as at present	7.0	24.5	254.5	66.4
5. The effect of the estate tax, items 1 - 4 in combination				
II. Gift tax				
1. Decrease the annual allowance of tax free gifts per donee from $4,000 to $2,500	1.2	.4		
2. Reduce the specific gift tax exemption from $40,000 to $15,000	10.1	5.4		
3. Increase the gift tax rates to the same level as those proposed for the estate tax (see Exhibit C)	43.5	30.1		
4. The effect of the gift tax, items 1 - 3 in combination			89.5	60.1
III. Income tax				
A. Individual income tax				
1. Reduce personal exemptions to $800 for single individual and $2,000 for married person and head of family	50.0	28.3		
2. Compute both the earned income credit and limits on net income after deducting personal exemption and credit for dependents instead of before such deduction as at present	20.0	11.6		
3. Increase the surtax rates by adopting the rate schedule shown in Exhibit B	425.5 2/	240.0 2/		
4. Disallow the deduction for taxes paid, other than business taxes and State personal net income taxes	11.0	17.8		
5. Restore the exemption of dividends from the normal Federal income tax as under the revenue data prior to 1936	- 54.1	- 54.7		
6. Tax husbands and wives as units by aggregating their income though permitting, at their option, the filing of separate returns	150.0	85.1		
7. Impose income normal tax and surtax on: (a) Salaries of State and local officials and employees	15.0	8.7		
(b) Interest from future issues of Federal, State and local obligations	0 3/	0 3/		
8. Amend Section 117(c) providing alternative taxes in capital gains and losses by substituting 50 percent for 30 percent	- 14.0 4/	- 8.1 4/		
9. Amend Section 105 changing the limiting rate to 50 percent	-	-		
10. Change the treatment of capital losses: (a) By providing a carry-forward of long-term losses (net offset against long-term gains or other income) for a period of three years against long-term gains	- 10.0 5/	0		
(b) By extending the short-term carry-over of losses to three years	- 20.0 5/	0		
11. Change the basis for determining capital gains for property transmitted at death (section 113(a)(5)) so that the basis shall be the basis of property in the hands of the decedent instead of the fair market value at the time of acquisition. The basis for determining loss should be the basis so determined or the fair market value of the property at the time of death, whichever is lower	10.0	0		
12. Allow net business losses of individuals (to include losses from partnerships) and fiduciaries to be carried forward for a period of five years (from year of origin of loss) to be offset against business income but not other income	- 10.0	0		
13. The effect of individual income tax, items 1 - 12 in combination			631.8	195.3
B. Corporation income tax				
1. Allow a net loss carry-over for purposes of all corporate income taxes for a period of five years after the year of origin. In computing the carry-over adjust the net loss by disallowing all depletion deduction and based on cost or March 1, 1913 value and adding tax-exempt interest and (the remaining) 85 percent of dividends received. The first year of origin should be the taxable year beginning during calendar year 1939	- 60.7 6/	0		
2. Increase the corporation income tax rates to produce at least enough revenue to offset the effects of the loss carry-over (1. above), in an average year:				
Special class income corporations:				
Subject to flat rate — 17 3/4 percent				
Under $5,000 net income:				
$ 0 - 5,000 — 13½ "				
5,000 - 20,000 — 15 "				
20,000 - 25,000 — 17 "				
General rule corporations:				
Tentative tax rate — 20½ "				
Dividends received credit — 17 3/4 "				
Dividends paid credit — 2½ "	64.7 6/	55.0		
3. Lower the percentages for depletion deduction from 27½ percent of gross income in the case of gas and oil properties to 13½ percent; from 23 percent of gross income in the case of sulphur mines or deposits to 11½ percent; from 15 percent of gross income in the case of metal mines to 7½ percent; and from 5 percent of gross income in the case of coal mines to 2½ percent	11.6	5.3		
4. Impose corporation income tax on interest from future issues of Federal, State, and local obligations	0 3/	0 3/		
5. The effects of the corporation income tax, items 1 - 4 in combination			15.6	27.5
2. Temporary income tax on individuals on income tax due for the taxable year 1939 as 18 percent to obtain in fiscal year 1940; the full year's effect of the changes in III A. above	-	246.5	-	246.5
Total individual, corporation and temporary individual income tax (the sum of A, B and C)			647.4	669.3
IV. Other business taxes				
A. Capital stock and excess profits taxes. Repeal the capital stock taxes effective for the July 1940 payment and the excess profits tax effective for the taxable year ending after June 30, 1940	- 155.0	0		
B. Unincorporated business privilege tax. Impose a 2 percent tax on "privilege net income" of unincorporated business enterprises payable March 15 and June 15 (see IV B of memorandum)	25.0	25.0		
C. Corporation privilege tax. Impose a 4 percent tax on privilege net income of corporations payable March 15 and June 15 (see IV C of memorandum)	472.1	461.5 2/		
Total other business taxes (sum of A, B and C)			372.1	486.5
V. Excise taxes				
1. Increase the tax on beer from $5 per barrel to $7	89.2	89.2		
2. Increase the excise tax on distilled spirits except brandy from $2.25 per gallon to $2.50 per gallon, and levy a corresponding floor stock tax	25.0	25.0		
3. Shift the present tax on radio parts to a tax on completed radios and increase the rate to 10 percent	5.0	5.0		
4. Impose a tax on the gross receipts of radio broadcasting companies	25.0	25.0		
5. Increase by 50 percent the rates of tax on the manufacture of cigars, tobacco, and snuff				
6. For the period from date of enactment to June 30, 1940, increase the gasoline tax from 1 cent per gallon to 2 cents per gallon, and thereafter decrease the rate from 2 cents per gallon to 1½ cents per gallon	91.5	171.1		
7. Substitute for the present taxes on the transfer of bonds and stocks, a tax based on the sale price thereof at the rate of 1/8 of 1 percent in both instances	[illegible]	[illegible]		
8. Repeal the electric tax which lapsed December 31, 1938	[illegible]	[illegible]		
9. Reduce the present exemptions under the 10 percent admissions tax from 40 cents to 20 cents	90.0	90.0		
Total of excise tax, items 1 - 9			386.7	486.3
Grand total of I - V			1,909.6	1,680.8

Treasury Department, Division of Tax Research

October 25, 1938.

1/ For income tax and other business taxes the basis of estimate is calendar year 1939; and for other taxes the basis of estimate is fiscal year 1940.
2/ If the top bracket rate were limited to 50 percent the figures would be 397.9 and 230.6, respectively; if limited to 65 percent the figures become 416.3 and 240.7, respectively.
3/ The annual additional income tax revenue from this proposal would increase gradually as the exempt tax exempt securities were redeemed and replaced by new issues without exempt features.
4/ This is based on an estimate that inflation increases issued in 1938 will slightly exceed long-term gains. In years when such gains exceed the losses the change will yield additional revenue; and in years when such gains are less than the losses the change will result in less revenue.
5/ Figures are for an average year, giving full effect to the three-year carry-forward.
6/ This figure is for an average year. The revenue loss from the carry-forward of losses and the revenue gain from the increase in rates over the rates in the Revenue Act of 1938 will vary from year to year, resulting sometimes in a net gain of revenue and sometimes in a net loss of revenue, depending upon business conditions.
7/ Full year tax liability reduced by an estimated allowance for deferred payments.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE May 8, 1939.

TO Secretary Morgenthau

FROM Mr. Haas

Subject: Major wheat export sales, as reported by Federal Surplus Commodities Corporation.

This brings up to date through May 4 the table of major wheat export sales given in my memorandum to you of May 3.

		Bushels
April 26:	Argentina to United Kingdom	150,000
	Australia to United Kingdom	150,000
	Australia to Shanghai	500,000
April 27:	Canada to Greece	750,000
	Australia to United Kingdom	200,000
	Australia to China	500,000
April 28:	Canada to United Kingdom	1,500,000
	Australia to United Kingdom	250,000
May 1:	Canada to United Kingdom	500,000
	Australia to United Kingdom	250,000
	Australia to China	250,000
May 2:	Canada to United Kingdom	1,500,000
	Argentina to United Kingdom	500,000
	Australia to United Kingdom	500,000
	Australia to China	500,000
May 3:	Canada -- total export sales	250,000
	Australia to China	300,000
May 4:	United Kingdom bought about	1,500,000

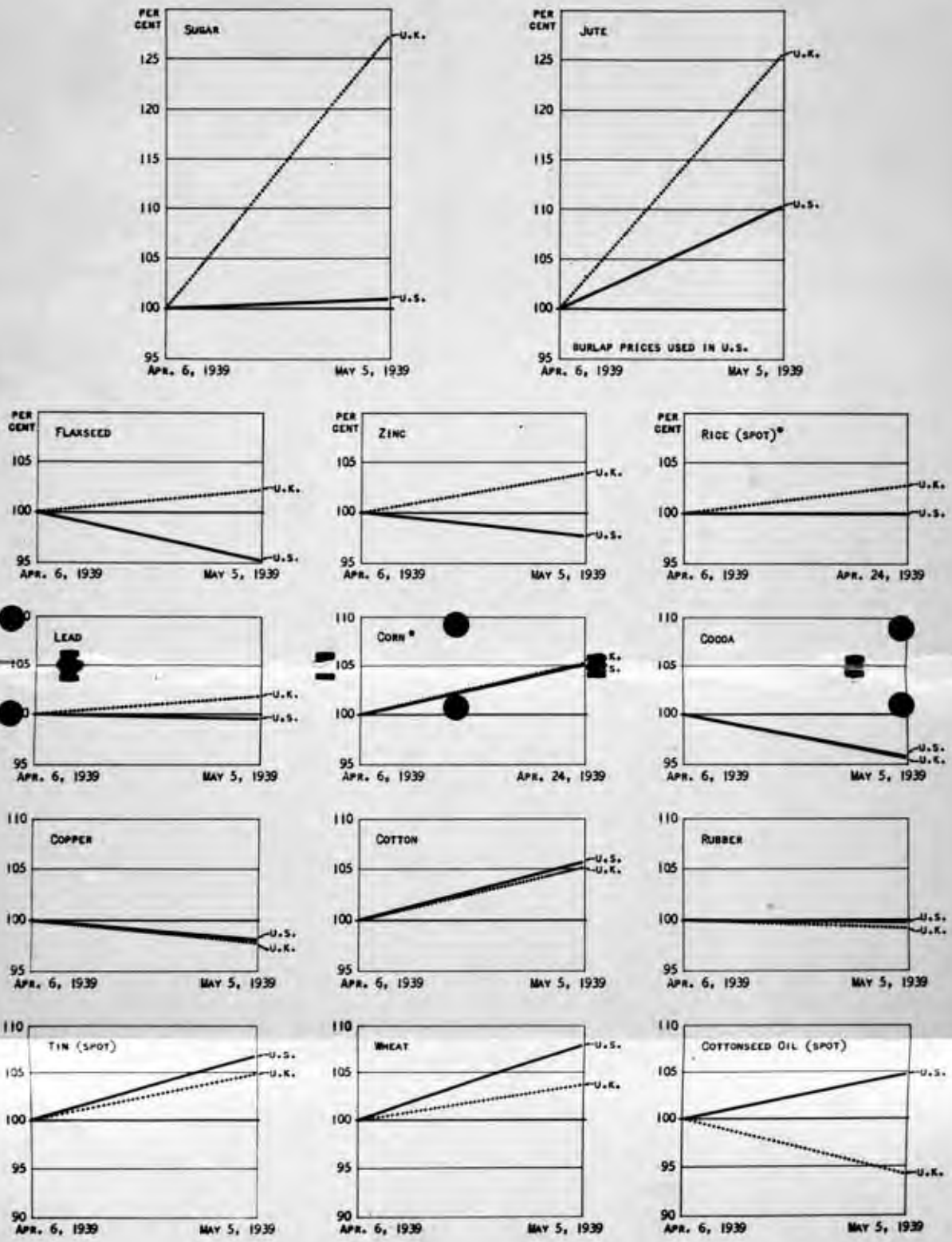
Supplied by:	
Australia	750,000
Argentina	250,000
Canada	300,000
Liverpool spot wheat	200,000
Total	1,500,000

Non-European countries reported to have contracted to take about 10,000,000 bushels of wheat and flour from Australia between May 1 and July 1, mostly expected to go to Shanghai.

CHANGES IN FUTURE PRICES OF SELECTED COMMODITIES IN U.S. AND U.K.

April 6, to May 5, 1939 *

APRIL 6, 1939 = 100



* FINAL PRICE IS FOR APRIL 24, 1939

Office of the Secretary of the Treasury
Division of Research and Statistics

Chart

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE May 8, 1939.

TO Secretary Morgenthau

FROM Mr. Haas

Subject: The commodity price situation.

The background

Commodity prices in the United States during 1938 were subjected to strongly conflicting forces. In the first six months of that year (See Chart 1) prices of sensitive commodities drifted gradually downward, chiefly in response to (1) a weakening in industrial demand, which resulted in some piling up of supplies, and (2) deflationary foreign developments, which were reflected in a declining trend of sterling exchange.

For a brief period during June and July 1938, the sharp increase in industrial demand then developing caused a rapid improvement in prices, particularly for industrial materials. The rise, however, was soon brought to a halt by the increasingly serious political situation in Europe, which had various deflationary influences on commodity prices. A crisis was passed at the time of the Munich agreement in early October; but prices made no further gains, since the strengthening influence of an improving domestic demand (as indicated in Chart 1) was nullified by a further weakening in the foreign situation.

Early in 1939 the situation was reversed. European developments began to take a somewhat more favorable part in the price situation. (1) Early in January, the decline in the sterling-dollar rate was effectively halted. (2) Increasing industrial demand in Great Britain and France, and an intensified demand for armament materials, provided support to commodity prices. (3) During February and early March, a marked improvement in long-term confidence among the European democracies was a factor contributing to a temporary price upturn at that time.

The domestic situation, on the other hand, had become an influence in depressing prices, owing to the downturn in business activity which set in early in December, and which has not yet been definitely halted. While the improving situation abroad offset for a time the effect of the domestic situation, Hitler's seizure of Czechoslovakia in March abruptly removed that support, and sensitive prices (as represented by the BLS index of 30 commodities shown in Chart 1) declined to the lowest level since the previous June.

Recent developments

During the past several weeks, renewed price support has come from abroad in the form of increased buying of armament materials and food supplies, while the inflationary significance of the latest intensified stage of the British rearmament program, to be financed in large part with borrowed funds, is apparently beginning to attract speculative buying. The resulting upturn in prices of sensitive commodities in Great Britain has begun to affect prices in this country.

In Chart 2, a comparison is made of the recent trends of sensitive commodity prices in Great Britain (as represented by Reuter's index) and in the United States (as represented by the Dow-Jones index and Moody's index). In this comparison, one must keep in mind the following:

Reuter's -- Largely futures prices for 21 speculative commodities in Great Britain. Includes gold, silver, and 4 other metals. Weighted by importance of each commodity in international trade.

Dow-Jones -- Futures prices for 11 commodities, mostly agricultural. No metals. Weighted approximately by speculative importance.

Moody's -- Weighted spot index of 15 sensitive commodities. Includes 4 metals. Only 6 commodities -- wheat, cotton, sugar, corn, rubber, cocoa -- are common to all three indexes.

With reference to recent price trends, Reuter's index has been influenced by marked upturns in prices of tin and jute, which are not included in the two American indexes, while

Moody's index has been held down by a decline in steel scrap, and until recently by a decline in hogs, neither of which is included in Reuter's index. Wheat prices, which are very heavily weighted in all three indexes, went up first in this country, and recently have gone up sharply in England.

Influence of British armament program

The intensified British rearmament drive now under way seems likely to affect commodity prices in two ways:

(1) Through the actual increase in demand for war materials and food supplies, which is already becoming effective as a market factor;

(2) Through the potential inflationary effect of British deficit expenditures at a time of near-capacity industrial activity. The effect of the latter influence alone on prices in the United States will depend on whether or not sterling declines; it would have no effect if sterling weakened proportionately.

The actual increase in commodity demand should continue to strengthen prices in the United States, particularly if sterling does not decline. It would also doubtless be accompanied by a rising volume of speculative buying. It may be recalled that the price boom of early 1937 was credited in large part to actual and speculative buying resulting from the early stages of British and French rearmament.

Of the total expenditures contemplated under the British rearmament and defense program, which amount to £630,000,000 (including recent provisions for doubling the Territorial Army), it is planned to borrow £380,000,000. This sum, according to J. M. Keynes, in proportion to national income, is equal to nearly twice the maximum United States deficit of any recent year, excluding the veterans' bonus.* It means, he concludes, that during the 1939-40 fiscal year the problem of abnormal unemployment in Great Britain will cease to exist, and that the various industrial problems of the last war -- an acute shortage of skilled labor, Government priorities, curtailment of unessential services -- are around the corner. Demands for imports, he says, will surely increase, and the avoidance of inflation will be a real and important problem.

* We calculate that the prospective British deficit will amount to about 8 per cent of their national income. Our own deficits, excluding veterans' bonus and debt retirement, have approximated the following percentages of our national income: 1934, 8 per cent; 1935, 5 per cent; 1936, 4 per cent; 1937, 2 per cent; 1938, 4 per cent.

Individual commodities

In Chart 3 we compare the changes in prices of 14 selected commodities in the United States and Great Britain over the period of the recent upturn, April 6 to May 3. The pronounced price rises for sugar and jute in Great Britain have been due directly to war buying. Sugar is being accumulated by various North European countries as a war reserve, according to trade reports, while jute is being used in large quantities for sandbags in air raid precautions. Flaxseed, zinc, lead, and rice have also risen appreciably more in Great Britain than in the United States.

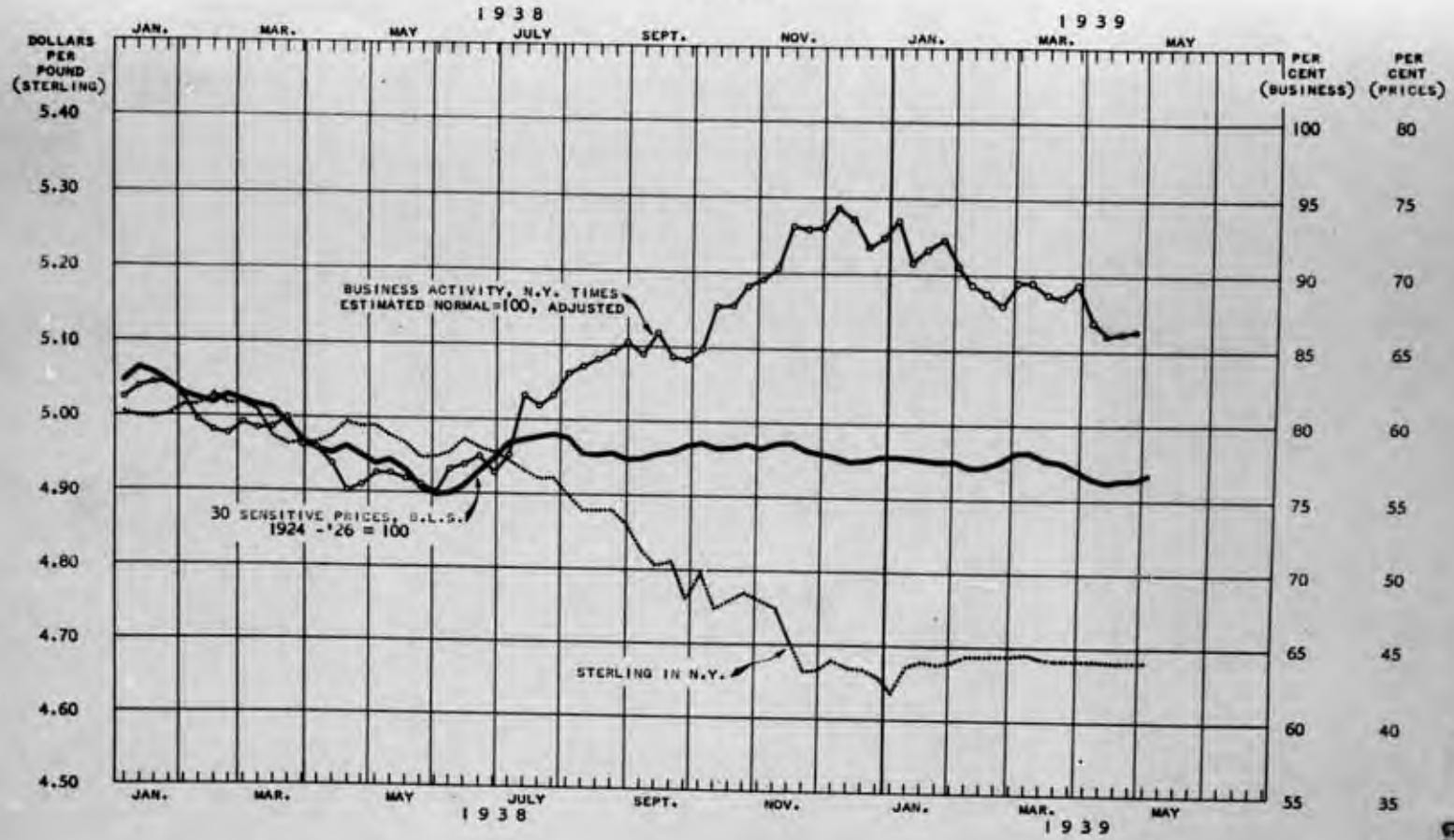
Wheat, cotton, and tin are other important commodities that have risen substantially in Great Britain, but for various reasons the United States prices have shown even greater improvement. The rise in wheat prices (affecting corn also) originated on a crop scare in the United States, and prices here have consequently been stronger than in other world markets. In the past few days, however, British wheat prices have gone up more rapidly than American, while Great Britain has bought wheat heavily in exporting countries outside the United States. Cotton prices in England have advanced less than in the United States because of foreign apprehension over the effects of the proposed export subsidy on American cotton. The rise in tin prices, according to reports from London, originated in heavy buying orders from the United States, stimulated by war fears and by the proposed Government barter arrangement for accumulation of tin stocks.

Copper and rubber prices have held about unchanged in both countries, since supplies apparently remain ample for present requirements. British prices for certain other commodities not so essential as war materials, such as cocoa and cottonseed oil, have declined in price. An increased demand for wool and hides for army requirements abroad has recently been a factor in raising prices of these raw materials in the United States.

The net effect of the increasing armament demand has been to bring an upturn in sensitive commodity prices at a time when the decline in business activity in this country and continued political tension abroad ordinarily would have tended to weaken prices. This indication that bullish price forces are coming into the picture may play an important part in improving business confidence in the United States.

COMMODITY PRICES, BUSINESS ACTIVITY AND STERLING EXCHANGE

Weekly



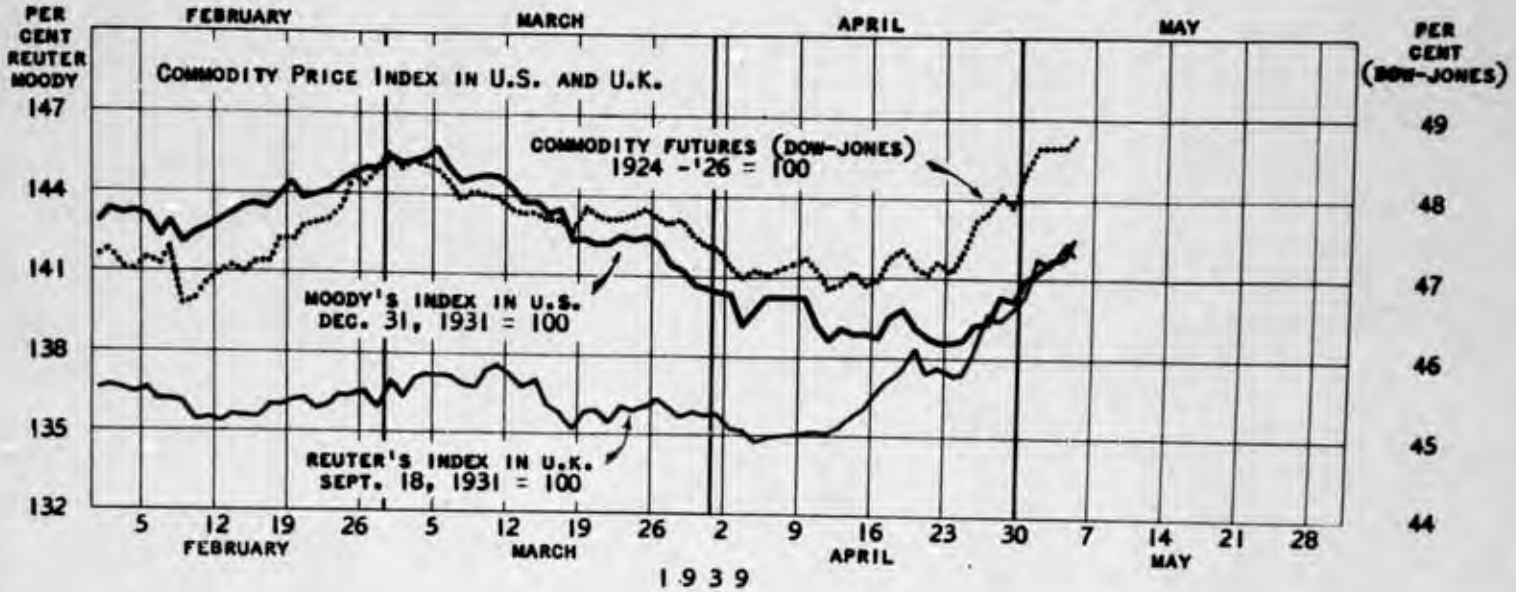
Office of the Secretary of the Treasury
Division of Research and Statistics

P - 172

Chart 1.

432

COMMODITY PRICE INDEXES, DAILY



Office of the Secretary of the Treasury
Division of Research and Statistics

P - 176 - 1

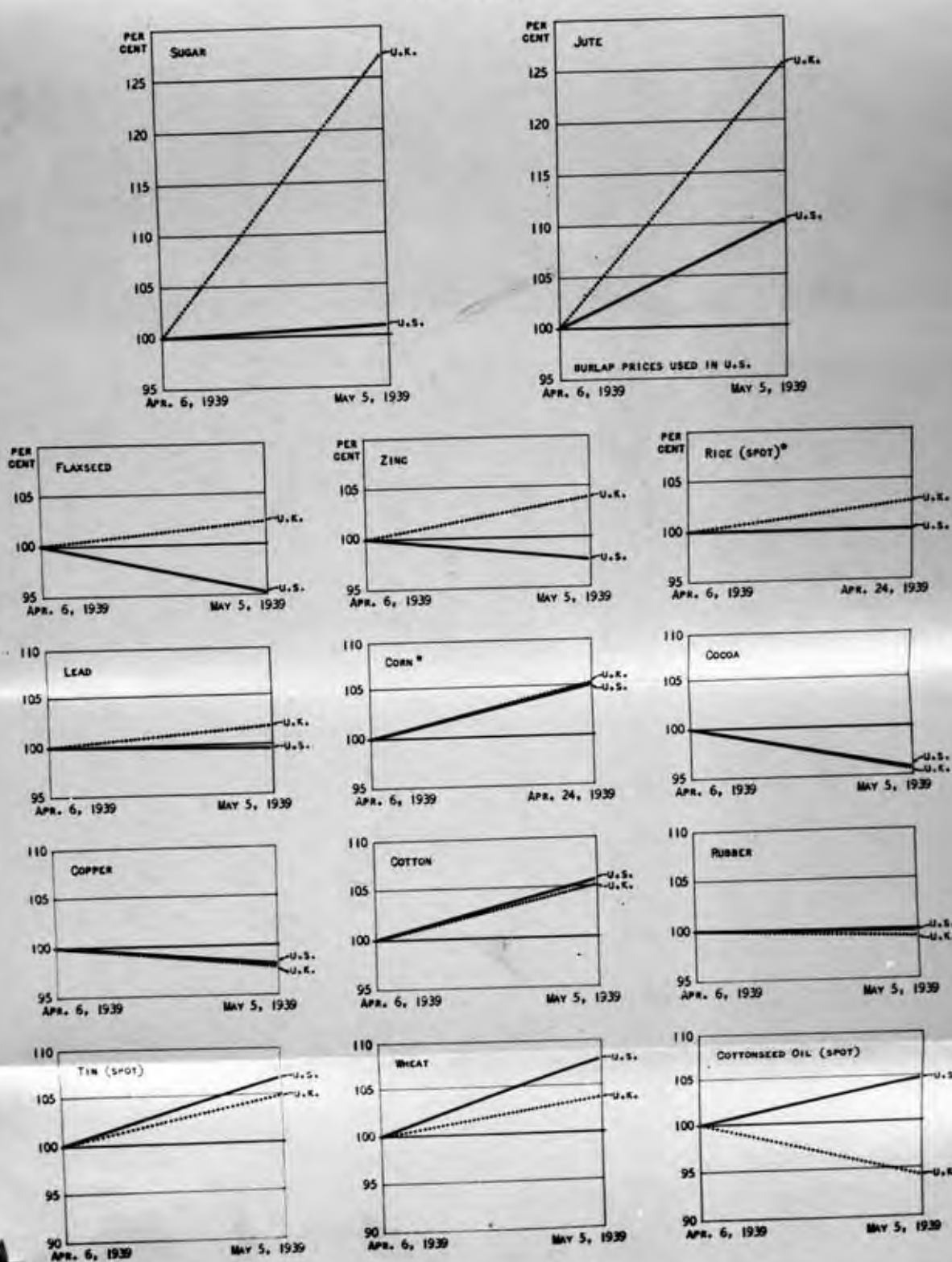
433

Chart 2.

CHANGES IN FUTURE PRICES OF SELECTED COMMODITIES IN U.S. AND U.K.

April 6, to May 5, 1939 *

APRIL 6, 1939 = 100



*FINAL PRICE IS FOR APRIL 24, 1939

Office of the Secretary of the Treasury
Division of Research and Statistics

P - 177

434

Chart 3

5-8-39

Major wheat export sales, as reported by
Federal Surplus Commodities Corporation,
April 26 through May 8

		Bushels
April 26:	Argentina to United Kingdom	150,000
	Australia to United Kingdom	150,000
	Australia to Shanghai	500,000
April 27:	Canada to Greece	750,000
	Australia to United Kingdom	200,000
	Australia to China	500,000
April 28:	Canada to United Kingdom	1,500,000
	Australia to United Kingdom	250,000
May 1:	Canada to United Kingdom	500,000
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Liverpool spot wheat	200,000
Total	1,500,000

Non-European countries reported to have contracted to take about 10,000,000 bushels of wheat and flour from Australia between May 1 and July 1, mostly expected to go to Shanghai.

		Bushels
May 5:	Australia to United Kingdom	600,000
	Demand in Winnipeg not so strong and not over 250,000 bushels sold for export.	
	Argentina extends 2-year credit to Spain for sale of 400,000 tons of wheat, which is double the amount under original arrangement.	
May 6: (Saturday)	Continued good demand reported, but no data on export sales.	
May 8:	Demand for cash wheat in world markets fell off considerably, with hardly any purchases reported from any territory.	

May 8, 1939
Monday

Re: Nicaragua

A meeting to discuss possible financial assistance for Nicaragua was held in the office of Mr. Jesse Jones today. Attending were:

For Export-Import Bank: Mr. Jesse Jones
Mr. Warren Pierson
Mr. Arey

For State Department: Mr. Collado
Mr. Dugan

For Treasury Department: Mr. Lochhead

President Somoza was accompanied by Dr. De Bayle.

President Somoza stated that he had recently been elected for a six-year term, which, together with the two years remaining on his unexpired term, gave him an eight-year tenure of office, during which time he wished to develop Nicaragua's commerce and industry along sound lines.

Mr. Jesse Jones asked him what particular projects he had in mind for which he needed help from the United States.

He stated:

(1) He would like a credit for the Banco National de Nicaragua, to be used to meet any emergency which might arise to protect their currency. He stated that their budget was balanced at present but he thought they should have this credit as an additional reserve;

(2) Although some work was being done on that portion of the Pan American Highway running through Nicaragua, he would like financial assistance to complete this road;

Re: Nicaragua

(3) He would like to develop the hydroelectric resources of the Republic and electrify the state railways, as well as supply cheap light and power to the people of Nicaragua.

Mr. Jones suggested that he submit specific data on each of these projects to Mr. Pierson and arrange for another meeting to discuss the details within the next two or three days.

After the meeting Mr. Jones indicated that although he would be glad to consider the loan to the bank, and funds to construct the Pan American Highway, he did not look with favor on hydroelectric projects.

The President of Nicaragua did not discuss the canalization of the river at this meeting, but Mr. Dugan, of the State Department, understood that he had discussed this project with President Roosevelt and apparently felt that the project was already approved.

AL

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE

TO Secretary Morgenthau May 8, 1939

FROM E. H. Foley, Jr.

This afternoon I conferred with Messrs. Graves and Klaus regarding the Sokol claim testimony which Mr. Graves is to give tomorrow. We went over your file and found nothing to indicate that Mr. Taylor made any recommendations with regard to the settlement. Mr. Graves stated what he proposed to say to the Subcommittee and I concurred in his proposal. He said he would state that Sokol did not contribute to the settlement of the Consolidated Distilleries case, the subject matter of his present claim; that the Treasury acted as investigating agency, but that the litigation aspects were in the hands of Mr. Whitaker of the Department of Justice; that the settlement was based on consideration of the difficulties of proving the facts, obtaining jurisdiction of the parties and enforcing collection of any judgment, and that since there was grave doubt on each of these points the settlement was a good one.

It was determined that Mr. Whitaker of the Department of Justice would be referred to in the event that the Subcommittee wished to know more details with regard to the basis for the settlement, although Mr. Graves would attempt to answer all questions himself so far as feasible. The State Department participation will not be brought up by Mr. Graves.

E. H. F.

TREASURY DEPARTMENT

WASHINGTON

May 8, 1939

TO THE SECRETARY:

The action thus far taken by Congress on the appropriation bills does not materially differ from the Budget estimates except on the bills for the following activities:

	Budget estimates	Last action by Congress	Increase (+) or Decrease (-)
	(In millions of dollars)		
Independent Offices	$1,689.9	$ 1,678.8	- $11.1
Agriculture ...	938.9	1,311.4	+ 372.5
Navy	790.4	770.5	- 19.9
Treasury	2,576.0	2,550.0	- 26.0

The only serious difference between the Budget estimates and the last action taken by Congress on such estimates is that reported by the Senate Appropriation Committee which increases the expenditures under agricultural activities by $372,500,000.

Independent Offices

The reduction in the Independent Offices estimates is represented by a $7,300,000 reduction in the Civil Aeronautics Authority estimates on account of a training program which the Committee thought should be put through in legislative form rather than in an appropriation bill, and $2,000,000 representing the estimates for the Federal Communications Commission which was eliminated temporarily pending any action that Congress might take on the McNinch report and recommendations.

Navy

The reduction of $19,900,000 was due to a decrease of $5,000,000 in the amount of money that the Budget asked to be made available for the purchase of airplanes, but the Committee added this back in the form of a contract authorization. It also reduced the amount of the estimate for replacement of naval vessels by the amount of $16,000,000. These vessels are all under construction and if the amount of money made available by

the Committee is not sufficient to meet the program as it develops during the year a supplemental will be required.

Treasury

The reduction in the Treasury estimates as submitted by the Budget in the amount of $26,000,000 is due to a decrease of $20,000,000 in the Old-Age Reserve Account; the elimination of the Alley Dwelling Authority appropriation of $1,000,000; advances to Railroad Unemployment Insurance Account of $1,250,000; refunds of customs and internal revenue of $2,000,000; and expenses of collecting internal revenue by $800,000. There were other miscellaneous decreases making up the difference, offset, however, by an increase of $2,000,000 in the amount provided in the Budget for venereal disease investigation.

It will be seen that these reductions are more apparent than real because in most cases the money will have to be appropriated either in 1940 or early in 1941.

Agriculture Department

The increase in the Agriculture Budget estimates is made up as follows:

Parity payments	$ 225,000,000
Surplus Commodities	113,000,000
Farm Tenant Act (Title I) ..	25,000,000
Miscellaneous items	9,000,000
Total increase	$ 372,000,000

As to parity payments, you will recall that when the Agricultural Adjustment Act of 1938 was under consideration in Congress, the matter of providing for parity payments was taken up by the President with the Democratic leaders, which resulted in a gentlemen's agreement to the effect that parity payments would not be provided for unless and until the additional revenue necessary to finance them was provided. Nevertheless, a rider was attached to the Emergency Relief Appropriation Act of June 21, 1938, which appropriated $212,000,000 for the making of parity payments during the fiscal year 1939. When the 1940 Budget was under consideration in the Appropriation Committee of the House,

the Committee provided for $250,000,000 additional funds for parity payments for the fiscal year 1940, stating that:

> "The committee believes its duty is clear to provide in this bill the funds necessary for a continuation of that policy. (Referring to the previous policy of appropriating for parity payments.) The committee also believes the Congress will, in due time, according to its wisdom, decide whether the continuation of the policy which it inaugurated a year ago, of making parity payments, shall be contingent upon the provision of specific revenues earmarked for the specific purpose, or whether the problem of raising the needed additional revenues shall be embodied with the general problem of finding new sources of income for the expanded activities in all branches of the Government."

This additional amount was eliminated on the floor of the House. Now the Senate Agriculture Appropriation Committee has added $225,000,000 for parity payments in 1940. It certainly has been the President's intention from the beginning that additional revenue should be provided to pay for parity payments.

The Senate Committee has also added $113,000,000 to be used by the Secretary of Agriculture to dispose of Surplus Commodities. This sum is in addition to the amount appropriated by Section 32 of the Agricultural Adjustment Act which you will recall appropriates an amount equal to 30% of the customs duties. The amount in the Budget for this purpose for 1940 is $90,000,000.

The Senate also added the sum of $25,000,000 to increase the amount available for loans to tenant farmers with which they might purchase farms under the provisions of the Bankhead-Jones Farm Tenant Act. For this purpose there is $25,000,000 available in 1939 and the Budget contained an item of the same amount for the fiscal year 1940. This addition by the Senate would make $50,000,000 available for this purpose in 1940.

DWB

MR. BERNARD

443

Please file all this together under date of 7/8/39

May 8, 1939

My dear Mr. Thomas:

Receipt is acknowledged of your telegram and your letter of May 5, 1939 with regard to H. R. 4022, a bill concerning the claim of Harry Sokol.

Mr. Harold Graves, Assistant to the Secretary, will appear before you pursuant to your request at 2 o'clock, Tuesday, May 9, 1939.

Yours very truly,

Secretary

Hon. J. Parnell Thomas
House of Representatives

SK:s Typed 5/8/39

S. E.M.H.

PARNELL THOMAS
7TH DISTRICT N. J.

445

COMMITTEES:
MILITARY AFFAIRS
CLAIMS
CENSUS

Congress of the United States
House of Representatives
Washington, D. C.

May 5, 1939

Honorable Stephen B. Gibbons,
Assistant Secretary of the Treasury,
Washington, D. C.

My dear Mr. Gibbons:

In reply to your letter of May 4th, which arrived here this afternoon and which was written by you in response to my request of of May 3rd that all available files in the Bureau of Customs relating to the Canadian distilleries cases be turned over to me, I am at a loss to understand why you believe that "the disclosure of those files would not be in the public interest."

As you know, my request for these files was made in order to get the complete facts relating to a claim of an informer in the so-called Canadian distilleries cases. This claim for $50,000 is incorporated in the bill HR 4022 referred by the Speaker of the House of Representatives to the Claims Committee of the House and in turn referred by the Chairman of the Claims Committee of the House to me as a subcommittee. Based on your own investigation of the entire matter, you know that not only the facts relating to the information given by the informer who introduced the claim are complex, but that there is a real difference of opinion among various individuals in your own office as to whether such a claim should be granted. In fact you, yourself, informed me that originally you were in favor of the claim and then after receiving additional information you changed your mind. Further, you informed me that the first memorandum written by you on the subject was in favor of the claim, so is it any wonder that I find it necessary for me not only to interrogate individuals who have had contact with this matter, but also that I should examine all the records pertaining to it?

For these reasons, both the Chairman of the Claims Committee of the House and myself as the subcommittee considering the bill, believe it necessary that the subcommittee examine the files in order to make a thorough study of the claim and intelligently determine whether or not the claim should be approved. I, therefore, requested that you supply all of the available files in the Bureau of Customs relating to the Canadian distilleries cases, and regardless of your letter to me of this afternoon, I must again assert the prerogative of the subcommittee considering HR 4022 by insisting that you deliver the files in question to my office, Suite 318 Old House Office Building not later than twelve o'clock noon, Monday, May 8th, 1939.

Very truly yours,

Parnell Thomas

P. S. I am informed by Mr. Kennedy, Chairman of the Claims Committee of the House that he too will request of you by telephone this afternoon that you deliver the files.

Hand to Mr. Gibbons
when Mr. Foley comes
in Sat. a.m.

446

Treasury Department

TELEGRAPH OFFICE

447

6PO FO 31 GOVT

1939 MAY 5 PM 4 12

HF WASHINGTON DC 347P MAY 5-39

HON STEPHEN B GIBBONS

ASST SECRY TREASURY DEPT WASHNDC

PLEASE HAVE MR HAROLD N GRAVES APPEAR BEFORE ME AT TWO PM TUESDAY MAY NINTH NINETEEN THIRTY NINE. THIS IN CONNECTION WITH HR FOUR OUGHT TWO TWO. LETTER REFILES FOLLOWS

J PARNELL THOMAS MC

410P

MAY 5 1939

My dear Mr. Thomas:

Reference is made to your telegram dated May 3, 1939, addressed to me ~~Hon. Stephen B. Gibbons~~ as Acting Secretary of the Treasury. In that telegram you request the delivery of all available files in the Bureau of Customs relating to the Canadian Distilleries cases.

I regret to say that I must respectfully decline to comply with your request because the disclosure of these files, in my judgment, would not be in the public interest.

Very truly yours,

(Signed) Stephen B. Gibbons

Acting Secretary of the Treasury.

Hon. J. Parnell Thomas,
House of Representatives.

MED/svp
Typed: 5/4/39.

Treasury Department

TELEGRAPH OFFICE

449

6PO FO 43 GOVT

HF WASHINGTON DC 1939 MAY 3 PM 3 17 1939 MAY 3 PM

HONORABLE STEPHEN B GIBBONS

ACTING SECRETARY TREASURY DEPT WASHNDC

PLEASE DELIVER ALL AVAILABLE FILES IN CUSTOMS RELATING TO CANADIAN DISTILLERIES CASES TO MY OFFICE SUITE THREE ONE EIGHT OLD HOUSE OFFICE BUILDING THIS AFTERNOON. THESE REQUIRED IN CONNECTION WITH SOKOL CLAIM. BELIEVE IT WOULD BE BETTER TO DELIVER IN EXISTING FILING CABINETS.

J PARNELL THOMAS MC

315P

Copy given Mr. Foley

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE 5-8-39

TO Secretary Morgenthau

FROM Mr. White

Subject: United States Currency is Being Hoarded and Used by Foreigners.

1. Currency is being exported in large amounts. A partial survey of the banks in the New York area indicates that United States currency is being shipped abroad in large amounts. During March and April alone it is estimated that over $70 million of United States currency was shipped abroad. The currency from New York is being shipped chiefly to Netherlands, England, France, Switzerland and Belgium.

In 1937 and 1938 there was virtually no reported outward movement, but it became heavy in the Munich period ($25 million flowing out during September and October) and again during March and April of this year. Cable from North China reports that United States currency is being eagerly sought for circulation in North China.

2. Currency hoarding seems to be increasing. Bills of large denomination ($50 or more) have increased over $200 million during the past year. This is an increase of 15 percent as compared with an increase of approximately 5 percent on the coins and smaller denominations of currency which comprise 4/5 of the total circulation outstanding. This would seem to indicate an increase in hoarding. There are two possible explanations for this increase in hoarding:

(a) Foreigners fearful of having their foreign balances sequestered by their government and unable to keep gold in the United States are converting their dollar balances into dollar bills and keeping them in safety deposit vaults either here or abroad.

(b) That domestic owners of balances are converting their deposits into cash in order to avoid the necessity of paying the tax on deposits. This latter explanation doesn't seem to be the more

reasonable one in view of the fact that the tax has existed for several years whereas the sharp increase in circulation of notes of large denomination has taken place chiefly during the past year.

3. Currency purchases by foreigners may account for as much as two or three hundred million dollars of gold imports during the past year. If we had accurate figures -- which we do not -- of currency which foreigners have bought and either taken out of the country or kept in safety deposit vaults in the United States, we might well find that during the last couple of years several hundred million dollars of gold was imported into this country in exchange for our currency. Part of the residual item ($470 million in 1938) may be explained by this purchase of our currency by foreigners.

4. Foreigners are taking our paper money and giving up gold to the value of 100 percent. Certainly no one could object to that exchange.

May 8, 1939

MEMORANDUM FOR THE SECRETARY:

Attached are two copies of the memorandum of October 24, 1938, which served as the basis of a conference which you and Mr. Hanes had with the President about that time.

The summary of the tax changes, together with the revenue increases and decreases, are shown on the folded last page, Exhibit J.

Roy Blough

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE October 24, 1938.

TO Mr. Eanes

FROM Mr. Blough RB

Subject: Methods of raising additional tax revenues.

To raise the specified sum of $2,000,000,000 additional annual revenue will probably necessitate all of the tax increases described below or their equivalents, unless business and national income increase substantially over present levels. A brief summary of the changes is shown in Exhibit A.

Whether the increased rates and new taxes described will in fact produce the required $2,000,000,000 is problematical, for three reasons: (1) The Division of Research and Statistics has found it physically impossible to prepare the estimates of yield for some of the taxes within the necessary time limit; (2) the estimates made thus far are for taxes considered each by itself without reference to the impact of one tax on the revenues from the others; and, most important, (3) the basis of the estimates has of necessity been the economy as it was situated before the imposition of the taxes, while in actual fact the shock of such a large increase in taxes in so short a time might so disrupt business and reduce the national income as to seriously affect the tax-producing capacity of the whole tax system. 1/

It is deemed impossible to increase the revenue by $2,000,000,000 in the current fiscal year 1938-39. Substantial increases in revenue might be secured for that year either by passing tax legislation at a special session of Congress before the end of the calendar year 1938, or by passing tax measures in the early months of 1939 retroactive to 1938. The disadvantages of either method are perhaps too obvious to require comment.

If the continuing tax changes described herein were passed during the regular 1939 session of Congress, substantial parts of the increases would be effective for the fiscal year 1939-40, but the program as a whole would not have its full effect on revenues until fiscal 1940-41, and in minor respects the full effect would be delayed until fiscal 1941-42 (due mainly to fiscal year income tax returns and delayed estate tax returns). To produce the desired revenue for fiscal 1939-40, special temporary legislation would accordingly be necessary. A brief summary of legislation to accomplish this result is shown in Exhibit B.

1/ Since the above was written, estimates and intelligent guesses of revenue yields indicate that the added revenue likely to be received from the described tax changes in a full year, at the probable 1939-40 level, would be short of $2 billions by about $200 millions. See Exhibit J.

In choosing among the limited number of possible tax sources an important objective has been to avoid as much as possible harmful repercussions on the economy. It is believed that this can be attained best by increasing the estate and gift taxes and the individual income tax before resorting to additional taxes on business, and by imposing additional general business taxes before resorting to sales and excise taxes. However, it has proved necessary to provide increased rates and new taxes even for the more undesirable tax types. In the following description of sources of additional revenue, the sources are listed roughly in what is believed to be their order of merit under existing conditions.

Estimates of yields of individual taxes and tax changes insofar as they are now available are shown in Exhibit J.

I. Estate Tax

1. Change the specific exemption from $40,000 to a specific exemption determined by aggregating the following exemptions allowable as a deduction from the gross estate. If the decedent is survived by:

(a)	A widow	$30,000
(b)	A widower	15,000
(c)	One orphan under 21	30,000
(d)	Each other child under 21	5,000

For administrative purposes a minimum specific exemption of $10,000 should, however, be allowed, irrespective of the number and type of beneficiaries. It is estimated that on average the effect of this proposal will be to reduce the specific exemption from $40,000 to between $20,000 and $25,000.

2. Increase the estate tax rates by adopting the rate schedule shown in Exhibit C. The combined effects of the changes in exemptions and rates are tabulated in Exhibit D and shown in graphic form in Exhibit E.

3. Eliminate the $40,000 estate tax insurance exclusion.

4. Pass a joint resolution in February 1939 eliminating the provision which allows an executor to value an estate as of the date one year after the decedent's death, and restricting the period for filing estate tax returns to twelve months instead of fifteen months after death as at present. The effect of this resolution would be to augment the revenues for the fiscal year 1939-40 to the extent that payment of estate taxes on the estates of decedents dying during the period April-June 1939 would otherwise have been deferred until after June 30,1940. 1/

II. Gift Tax

1. Decrease the annual allowance of tax-free gifts per donee from $4,000 to $2,500.

2. Reduce the specific gift tax exemption from $40,000 to $25,000.

1/ After the estimates were prepared it would appear that the revenue increase in 1940 would not be great enough to warrant a special joint resolution.

3. Increase the gift tax rates to the same level as those proposed for the estate tax.

III. Income Tax

A. Individual income tax.

1. Reduce personal exemption to $800 for single individual and $2,000 for married person and head of family.

2. Compute both the normal tax credit of 10 percent of earned income and the lower and upper earned income limits of $3,000 and $14,000, respectively, on the amount of net income after deducting the personal exemption and credit for dependents, instead of before such deduction, as at present.

3. Increase the surtax rates by adopting the rate schedule shown in Exhibit F. The combined effects of the changes in exemptions, normal tax credit and rates are tabulated in Exhibit G-1 and G-2 and shown in graphic form in Exhibit H-1 and H-2.

4. Disallow the deduction for taxes paid other than business taxes and State personal net income taxes.

5. Restore the exemption of dividends from normal Federal income tax as under the Revenue Acts prior to 1936. This will act to reduce revenues but is deemed an important factor in tax equity in view of increases in individual and corporation rates.

6. Tax husbands and wives as units by aggregating their income, though permitting, at their option, the filing of separate returns. Under present law husbands and wives may file joint returns, or, at their option, separate returns. In the latter case the husband and the wife may each report and be taxed on such income as is viewed to be theirs under State property laws. In community property States the usual division is one-half of the community income to each spouse; the practice followed in other States is less uniform. This results in interstate variations of Federal income tax burden. In addition, the use of separate returns enables wealthy husbands and wives to avoid high surtax rates, which would otherwise be applicable. If the incomes of husbands and wives be considered as properly constituting a unit, existing practice is inequitable. To overcome such inequity the tax liability may be determined on the basis of the aggregate income of husband and wife, the liability then being prorated to each according to the amount of his income. Since many people believe equity would thus be increased and since the change would produce very substantial revenue, the proposal is included here.

7. Impose income normal tax and surtax on (a) salaries of State and local officials and employees, and (b) interest from future issues of Federal, State and local obligations.

8. Amend section 117(c), providing alternative taxes on capital gains and losses, by substituting 50 percent for 30 percent wherever it appears, so that capital gains will bear their due share in the increased individual income tax rates.

9. Change the limit on surtax on gains from sale of oil and gas properties prospected by individuals from 30 percent of sale price to 50 percent of sale price. (Section 105, Revenue Act of 1938.)

10. Change the treatment of capital losses (a) by providing a carry-forward of long-term losses (not offset against long-term gains or other income) for a period of three years, against long-term gains; and (b) by extending the short-term carry-over of losses to three years.

11. The basis for determining capital gains for property previously transmitted at death (Section 113(a)(5) shall be the basis of the property in the hands of the decedent instead of the fair market value at the time of acquisition. The basis for determining loss shall be the basis so determined or the fair market value of the property at the time of death, whichever is lower. This procedure for determining capital gains and losses is the same as that now in force for property acquired by gift. Capital gains not previously realized or subject to income tax would thus become taxable to the beneficiary if the property were sold or exchanged, eliminating in part a tax loophole for capital gains in the present income tax law.

12. Allow net business losses of individuals (to include losses from partnerships) and fiduciaries to be carried forward for a period of three or more years (from year of origin of loss) to be offset against business income but not other income. The first possible year of origin should be the taxable year beginning during 1939. This change will therefore not affect the revenues for the fiscal year 1940. The purpose of the change is to reduce the inequity in taxing fluctuating incomes now present in the law, which inequity becomes very serious with high rates of tax.

B. Corporation income tax.

1. Allow a net loss carry-over for purposes of all corporate income taxes for a period of three or more years from the year of origin. In computing the carry-over, adjust the net loss by disallowing all depletion deduction not based on cost or March 1, 1913 value and adding tax-exempt interest and the remaining 85 percent of dividends received. The first year of origin should be the taxable year beginning during 1939. This change reduces the revenue but in view of increased business taxes it is deemed desirable to reduce the inequity involved in taxing fluctuating incomes by allowing the carry-over. This change will not affect the revenues for the fiscal year 1940.

2. Increase the corporate income tax rates sufficiently to produce at least enough revenue to offset the effects of the loss carry-over (1. above), in an average year.

3. Lower the percentages for depletion deduction from 27½ percent of gross income in the case of gas and oil properties to 13-3/4 percent; from 23 percent of gross income in the case of sulphur mines or deposits to 11½ percent; from 15 percent for gross income in the case of metal mines to 7½ percent; and from 5 percent in the case of coal mines to 2½ percent.

4. Impose corporation income tax on interest from future issues of Federal, State and local obligations.

C. Temporary income tax.

The increased revenues derived from changes in income taxes will be reflected only in part in the fiscal year 1939-40. With respect to corporations the discrepancy between the full year's application of the changes and their fiscal year 1940 effects is negligible. If, however, the revenue from individual income taxes in that year is to be equal to the revenue resulting from a full year's application of the changes, an additional income tax may be imposed payable on March 15 and June 15, 1940, only, this tax to be a sufficient percentage of the income tax due for the taxable year 1939 to make up the revenue deficiency.

This tax will be necessary only if it is desired to secure full revenue increases in the fiscal year 1939-40.

IV. Other Business Taxes

A. Capital stock and excess profits taxes.

Repeal the capital stock tax, effective for the July 1940 payment, and the excess profits tax, effective for the taxable year ending after June 30, 1940. The repeal of these taxes reduces the revenue, but because of the undesirable nature of the taxes, it is deemed desirable to supply the revenue from the business privilege tax discussed in C below.

B. Unincorporated business privilege tax.

Impose a 2 percent tax on "privilege net income" of unincorporated business enterprises including any trade or business which, if conducted or engaged in by a corporation, would be taxable under the income tax, but

excluding the professions and any cases in which more than 80 percent of the gross income is derived from the personal services rendered by the individual or the members of the partnership or other entity in which capital is not a material income-producing factor. "Privilege net income" is defined in all respects in the same manner as the net income of corporations is defined under the Revenue Act of 1938 except that (a) tax-exempt interest on Government obligations held in connection with carrying on trade or business shall be included in the taxable base; (b) deductions shall not be allowed for (1) rent paid on business property, (2) taxes paid on business property, (3) interest paid for capital engaged in the business, and (4) depreciation of buildings; and (c) the deduction on account of the personal service of an individual or member of a partnership shall in no case exceed $5,000 per such individual or member. A specific exemption of $5,000 is allowed for each enterprise.

C. Corporation privilege tax.

Impose a 4 percent tax on the privilege net income of corporations defined as in (1) above, except for the limitation in (c) which does not apply. A specific exemption of $5,000 is allowed.

A comparison of the base for the corporation privilege tax and the corporation income tax by major industrial groups is shown in Exhibit I.

The taxes ~~proposed in (1) and (C) above~~ shall be payable in two installments on March 15 and June 15. The purpose of these payment dates is to secure additional needed revenue in fiscal 1939-40; otherwise four installments might be allowed as in the income tax.

V. Excise Taxes

1. Increase the excise tax on beer from $5 per barrel to $7.

2. Increase the excise tax on distilled spirits, except brandy, from $2.25 per gallon to $2.50 per gallon, and levy a corresponding floor stock tax.

3. Shift the present tax on radio parts to a tax on completed radios and increase the rate to 10 percent.

4. Impose a tax on the gross receipts of radio broadcasting companies.

5. Increase by 50 percent the rates of tax on the manufacture of cigars, tobacco, and snuff. The present rates on cigars are from 75 cents per thousand to $13.50 per thousand, depending upon the weight; and on tobacco and snuff, 18 cents per pound.

6. For the period from date of enactment to June 30,1940, increase the gasoline tax from 1 cent per gallon to 2 cents per gallon, and thereafter decrease the rate from 2 cents per gallon to 1½ cents per gallon.

7. Substitute for the present taxes on the transfer of bonds and stocks, a tax based on the sale price thereof at the rate of 1/4 of 1 percent in both instances. The present rates are

Bonds - 4 cents per $100 face value;
Stocks- 4 cents per $100 par or face value or fraction, or if without par or face value, 4 cents per share. However, if selling price is $20 or over, whether with or without par or face value, the rate is 5 cents instead of 4 cents.

8. Reenact the check tax which lapsed December 31, 1934. The rate of this tax was 2 cents per check or draft.

9. Reduce the present exemption under the 10 percent admission tax from 40 cents to 20 cents.

Exhibit A

Summary Statement of Described Methods of Increasing Tax Revenues

Estate Tax

Decreased exemptions
Greatly increased rates, except in top brackets
Elimination of deduction of insurance
Other changes

Gift Tax

Decreased exemptions
Increased rates to equal new estate tax rates

Income Taxes

Greatly increased personal surtax rates, except in top brackets
Decreased personal and family exemptions
Aggregation of family incomes for tax computation
Imposition of Federal personal and corporation income taxes on: (1) interest from future issues of Federal, State, and local bonds; (2) exempt State and local salaries
Increased corporation income tax rates (to be offset in future years by loss carryover)
Other changes

New business privilege tax on corporations and unincorporated business (present capital stock and excess profits taxes to be repealed)

Excise Taxes: increased rates on

Beer
Distilled spirits
Tobacco (other than cigarettes)
Gasoline
Transfers of stocks and bonds
Admissions (by decreasing exemptions)
Radios

New excise taxes on

Checks
Radio broadcasting companies

Exhibit B

Additional Tax Changes to Increase Revenues in Fiscal Year 1939-1940

Estate Tax

Joint resolution to be passed in February 1939 eliminating the provision which allows an executor the option of valuing an estate as of the date one year after the decedent's death, and restricting the period of filing estate tax returns to 12 months instead of 15 months after death as at present.

Income Taxes

Temporary emergency tax on individuals and corporations computed as a percentage of the income tax on 1939 incomes, payable March 15 and June 15, 1940.

Excise Taxes

Additional 1/2 cent a gallon on gasoline for the fiscal year 1939-1940 only.

Exhibit C

Proposed estate tax rate schedule

Taxable base: net estate after specific exemption 1/ (dollars in thousands)	Size of bracket (dollars in thousands)	Bracket rate	Cumulative tax
$ 0 - $ 5	$ 5	4	$ 200
5 - 10	5	8	600
10 - 20	10	12	1,800
20 - 30	10	16	3,400
30 - 40	10	20	5,400
40 - 60	20	23	10,000
60 - 80	20	26	15,200
80 - 100	20	29	21,000
100 - 150	50	32	37,000
150 - 200	50	35	54,500
200 - 250	50	38	73,500
250 - 300	50	41	94,000
300 - 400	100	44	138,000
400 - 500	100	47	185,000
500 - 600	100	50	235,000
600 - 800	200	53	341,000
800 - 1,000	200	56	453,000
1,000 - 2,000	1,000	59	1,043,000
2,000 - 5,000	3,000	62	2,903,000
5,000 - 10,000	5,000	64	6,103,000
10,000 - 15,000	5,000	66	9,403,000
15,000 - 20,000	5,000	68	12,803,000
20,000 - 30,000	10,000	70	19,803,000
30,000 - 50,000	20,000	72	34,203,000
50,000 and over		73	

Treasury Department, Division of Tax Research October 24, 1938

1/ The specific exemption is the sum of the following: For a widow, $30,000; a widower, $15,000; first orphan under 21, $30,000; and each other child under 21, $5,000.

EXHIBIT D.

Estate tax: Comparison of amounts of tax and effective rates on selected sizes of net estate (before exemption) under the present law and under the proposal

Net estate before exemption 1/ (in thousands)	Amounts of tax: Present law	Amounts of tax: Proposal	Effective rates: Present law	Effective rates: Proposal
$ 25	-	$ 200	-	.8%
30	-	600	-	2.0
40	-	1,800	-	4.5
50	$ 200	3,400	.4%	6.8
60	600	5,400	1.0	9.0
80	2,000	10,000	2.5	12.5
100	4,200	15,200	4.2	15.2
200	19,800	47,500	9.9	23.8
400	58,600	129,200	14.7	32.3
600	103,400	225,000	17.2	37.5
800	154,200	330,400	19.3	41.3
1,000	211,000	441,800	21.1	44.2
2,000	543,600	1,031,200	27.2	51.6
4,000	1,388,800	2,270,600	34.7	56.8
6,000	2,460,200	3,530,200	41.0	58.8
8,000	3,658,200	4,810,200	45.7	60.1
10,000	4,936,600	6,090,200	49.4	60.9
20,000	11,635,800	12,789,400	58.2	63.9
40,000	25,435,000	26,988,600	63.6	67.5
60,000	39,334,600	41,488,400	65.6	69.1
100,000	67,334,600	70,688,400	67.3	70.7

1/ The exemption under the proposal on the basis of 1936 data is on average $21,132. For the purpose of this computation, however, a $20,000 exemption was assumed.

Exhibit F

464

EFFECTIVE ESTATE TAX RATES PRESENT LAW AND PROPOSAL

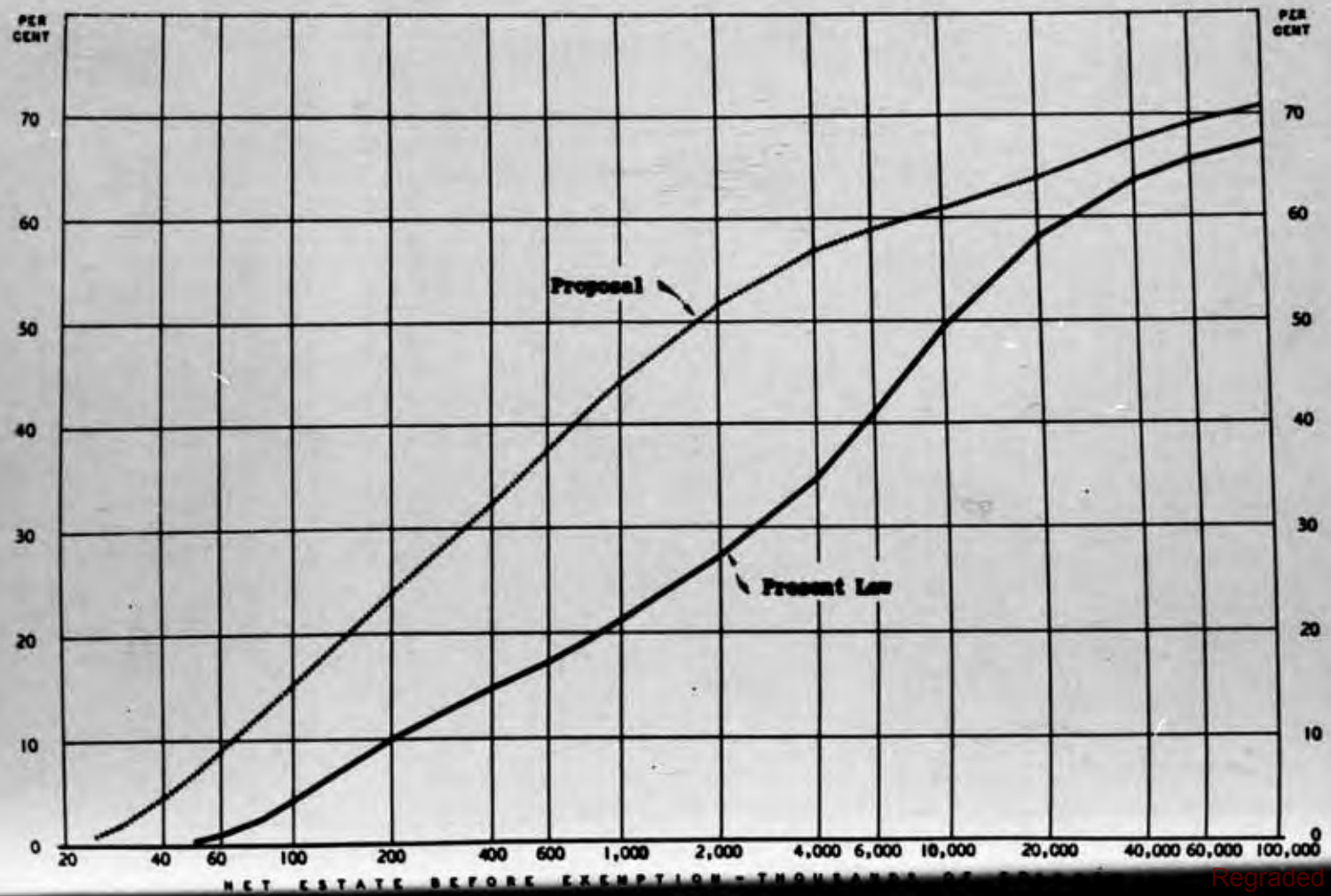


Exhibit F

Proposed individual income surtax rate schedule

Amount of surtax net income (In thousands)	Rate of tax (Percent)	Total surtax cumulative
0 - .5	-	-
.5 - 1	2	10
1 - 2	3	40
2 - 3	5	90
3 - 6	7	300
6 - 8	10	500
8 - 10	12	740
10 - 12	15	1,040
12 - 14	18	1,400
14 - 16	21	1,820
16 - 18	25	2,320
18 - 20	29	2,900
20 - 22	33	3,560
22 - 24	37	4,300
24 - 28	41	5,940
28 - 34	45	8,640
34 - 40	49	11,580
40 - 48	53	15,820
48 - 56	56	20,300
56 - 64	58	24,940
64 - 72	60	29,740
72 - 80	62	34,700
80 - 90	64	41,100
90 - 100	65	47,600
100 - 150	66	80,600
150 - 200	67	114,100
200 - 300	68	182,100
300 - 500	69	320,100
500 - 750	70	495,100
750 - 1,000	72	675,100
1,000 - 2,000	73	1,405,100
2,000 - 5,000	74	3,625,100
5,000 and up	75	

EXHIBIT G-1.

Single person with no dependents: Comparison of the amount of income tax liability and effective rate of tax under present law and under proposal

Selected net income (thousands of dollars)	Amount of tax 1/		Effective rate	
	Present law	Proposal 2/	Present law	Proposal 2/
$ .5	-	-	-	-
1	-	$ 7	-	0.7%
2	$ 32	59	1.6%	3.0
2.5	50	92	2.0	3.7
3	68	129	2.3	4.3
6	216	431	3.6	7.2
8	378	679	4.7	8.5
10	560	975	5.6	9.8
12	762	1,323	6.4	11.0
14	984	1,731	7.0	12.4
16	1,234	2,204	7.7	13.8
18	1,514	2,752	8.4	15.3
20	1,834	3,380	9.2	16.9
22	2,194	4,088	10.0	18.6
24	2,594	4,876	10.8	20.3
28	3,454	6,644	12.3	23.7
34	4,854	9,552	14.3	28.1
40	6,384	12,700	16.0	31.8
48	8,714	17,228	18.2	35.9
56	11,394	22,004	20.3	39.3
64	14,514	26,948	22.7	42.1
72	18,074	32,052	25.1	44.5
80	22,034	37,316	27.5	46.6
90	27,494	44,100	30.5	49.0
100	33,354	50,992	33.4	51.0
150	64,324	85,984	42.9	57.3
200	96,304	121,476	48.2	60.7
250	129,284	157,468	51.7	63.0
300	163,264	193,468	54.4	64.5
400	233,244	266,460	58.3	66.6
500	305,224	339,460	61.0	67.9
750	490,204	524,452	65.4	69.9
1,000	680,184	714,436	68.0	71.4
2,000	1,450,174	1,484,428	72.5	74.2
5,000	3,790,164	3,824,420	75.8	76.5

1/ Maximum earned income allowed.
2/ Basis of tax computation for proposal: Personal exemption $600 allowed as a deduction for both normal and surtax; earned income credit of 10 percent and the lower and upper earned income limits of $3,000 and $14,000 maximum, computed on net income after deducting personal exemption; proposed increased surtax rates; and normal tax 4 percent.

EXHIBIT G-2.

Married person with two children: Comparison of the amount of income tax liability and effective rate of tax under present law and under proposal

Selected net income (thousands of dollars)	Amount of tax 1/		Effective rate	
	Present law	Proposal 2/	Present law	Proposal 2/
$ .5	-	-	-	-
1	-	-	-	-
2	-	-	-	-
2.5	-	-	-	-
3	-	$ 7	-	0.2%
6	$ 84	219	1.4%	3.7
8	184	431	2.3	5.4
10	343	679	3.4	6.8
12	522	975	4.4	8.1
14	721	1,323	5.2	9.5
16	948	1,731	5.9	10.8
18	1,195	2,204	6.6	12.2
20	1,469	2,752	7.3	13.8
22	1,783	3,380	8.1	15.4
24	2,137	4,088	8.9	17.0
28	2,951	5,744	10.5	20.5
34	4,305	8,572	12.7	25.2
40	5,779	11,640	14.4	29.1
48	8,001	16,088	16.7	33.5
56	10,589	20,804	18.9	37.2
64	13,577	25,708	21.2	40.2
72	16,993	30,772	23.6	42.7
80	20,861	35,996	26.1	45.0
90	26,229	42,740	29.1	47.5
100	31,997	49,612	32.0	49.6
150	62,898	84,584	41.9	56.4
200	94,832	120,056	47.4	60.0
250	127,766	156,028	51.1	62.4
300	161,700	192,028	53.9	64.0
400	231,634	265,000	57.9	66.3
500	303,568	338,000	60.7	67.6
750	488,502	522,972	65.1	69.7
1,000	678,436	712,916	67.8	71.3
2,000	1,448,403	1,482,888	72.4	74.1
5,000	3,788,370	3,822,860	75.8	76.5

1/ Maximum earned income allowed.
2/ Basis of tax computation for proposal: Personal exemption $2,000 allowed as a deduction for both normal and surtax; earned income credit of 10 percent and the lower and upper earned income limits of $3,000 and $14,000 maximum, computed on net income after deducting personal exemption and credit for dependents; proposed increased surtax rates; and normal tax 4 percent.

Exhibit V-1

168

EFFECTIVE INDIVIDUAL INCOME TAX RATES, PRESENT LAW AND PROPOSAL

Single Person with No Dependents

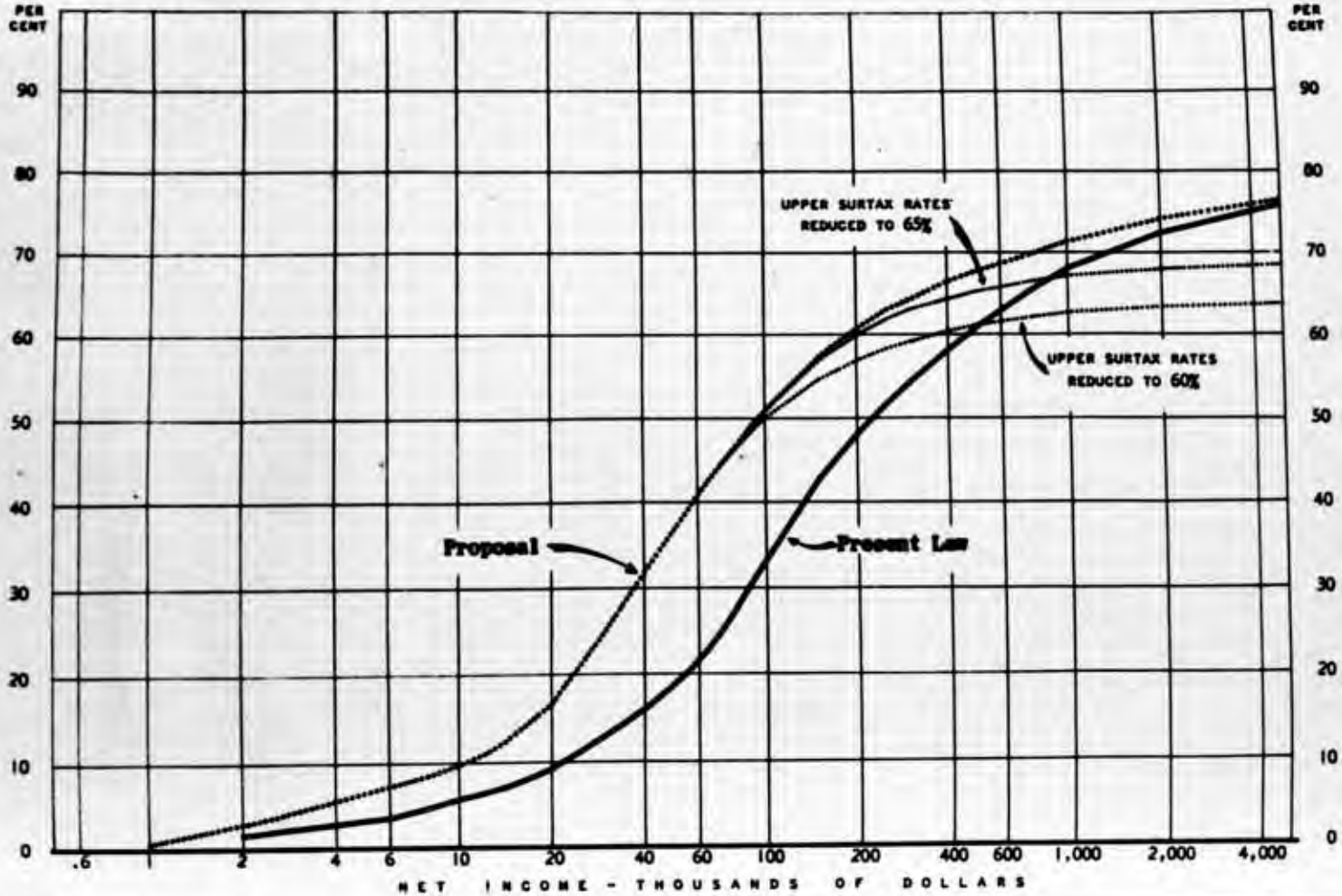


Exhibit H-2

469

EFFECTIVE INDIVIDUAL INCOME TAX RATES, PRESENT LAW AND PROPOSAL

Single Person with No Dependents

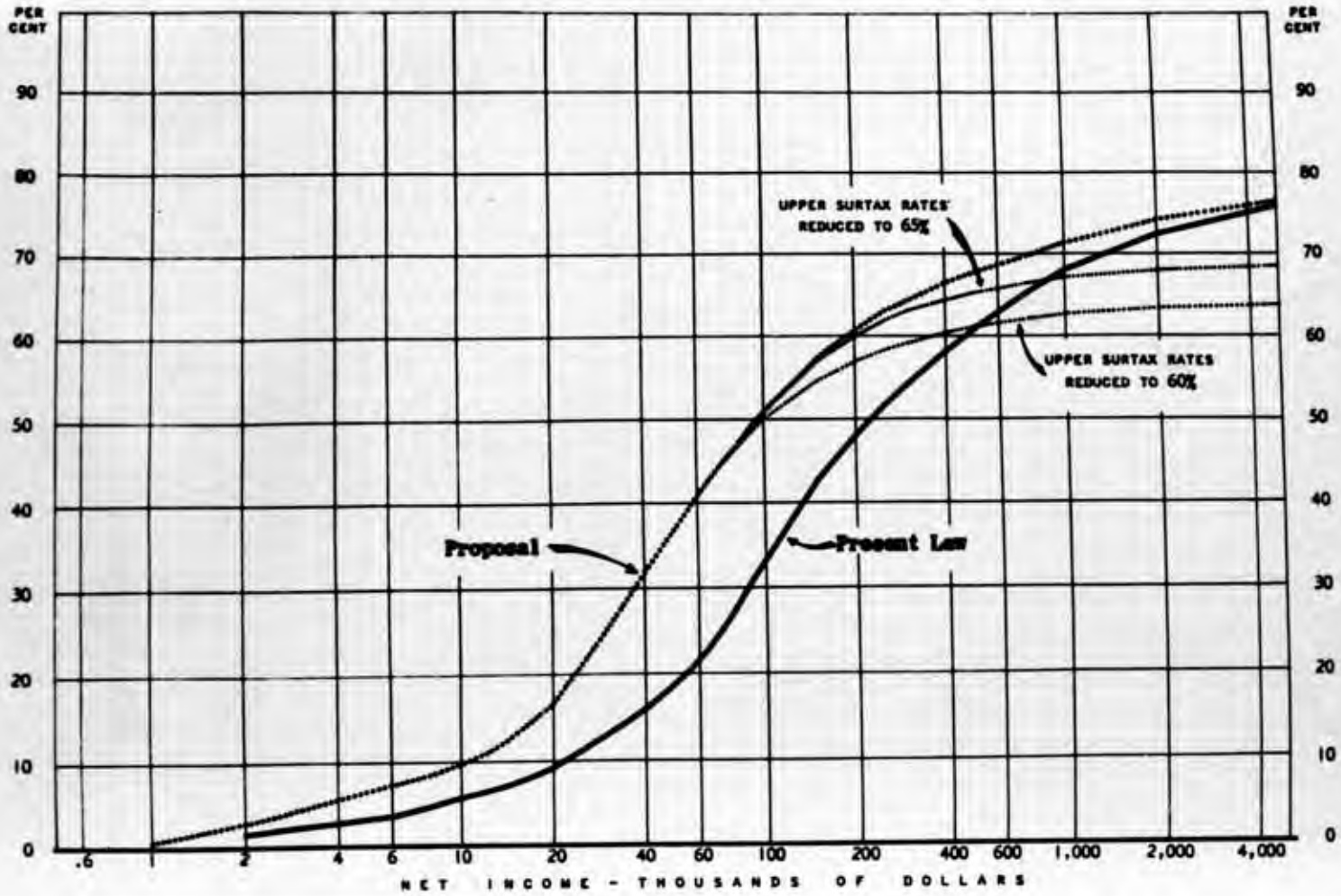


Exhibit I

Comparison of proposed tax base and present tax base for corporations with net income, 1935

Industrial groups	Privilege tax net income--proposed base	Net income 1/	Ratio of proposed to present base
	(In millions of dollars)		
riculture	97	45	2.2
ning and quarrying	320	167	1.9
nufacturing:			
Food	618	326	1.9
Liquors	297	108	2.8
Tobacco	188	101	1.9
Textiles	337	172	2.0
Leather	73	48	1.5
Rubber	91	31	2.9
Forest products	81	39	2.1
Paper, pulp, etc.	176	93	1.9
Printing, etc.	237	142	1.7
Chemicals, etc.	829	390	2.1
Stone, clay, etc.	151	91	1.7
Metal, etc.	1,532	900	1.7
Manufacturing n.e.c.	164	110	1.5
Total manufacturing	4,772	2,551	1.9
nstruction	87	49	1.8
nsportation	2,908	957	3.0
de	1,665	776	2.1
vice	361	128	2.8
nance	2,004	713	2.8
ure of business not given	1	-	-
Grand total	12,216	5,389	2.3

rce: "Statistics of Income".

Income reported plus 15 percent of dividends from domestic corporations; such dividends having been made taxable on incomes after 1935.

Detailed estimates of revenue effects of the proposals included in the memorandum

The estimates are arranged and numbered in the same order in which the proposals appear in the memorandum. The figures given below are revenue estimates prepared by the Division of Research and Statistics, Treasury Department, except those bracketed in red. The latter figures are only intelligent guesses and may be widely in error.

Detailed schedule	Estimated increase in revenue: First full year 1/	Estimated increase in revenue: Fiscal year 1940	Summary: Estimated increase in revenue: First full year 1/	Summary: Estimated increase in revenue: Fiscal year 1940
	(Millions of dollars)			
I. Estate tax				
1. Change the specific exemption from $40,000 to a specific exemption determined by aggregating the following exemptions allowable as a deduction from the gross estate irrespective of the actual nature of the distribution of the estate to the beneficiaries: (a) a widow, $50,000; (b) a widower, $15,000; (c) one orphan under 21, $30,000; (d) each other child under 21, $5,000. A minimum specific exemption of $10,000 should, however, be allowed irrespective of the number and type of beneficiaries	27.1	2.7		
2. Increase the estate tax rates by adopting the rate schedule shown in Exhibit 2	236.0	23.6		
3. Eliminate the $40,000 estate tax insurance exclusion	8.3	.8		
4. Pass a joint resolution in February 1939 eliminating the provision which allows an executor to value an estate as of the date one year after the decedent's death, and restricting the period for filing estate tax returns to twelve months instead of fifteen months after death as at present	3.0	24.3		
5. The effect of the estate tax, items 1 - 4 in combination			322.9	54.4
II. Gift tax				
1. Increase the annual allowance of tax free gifts per donee from $4,000 to $2,500	1.8	.6		
2. Reduce the specific gift tax exemption from $40,000 to $15,000	10.7	5.1		
3. Increase the gift tax rates to the same level as those proposed for the estate tax (see Exhibit 2)	63.5	30.1		
4. The effect of the gift tax, items 1 - 3 in combination			69.9	40.3
III. Income tax				
A. Individual income tax				
1. Reduce personal exemptions to $800 for single individual and $2,000 for married person and head of family	50.0	28.9		
2. Compute both the earned income credits and limits on net income after deducting personal exemption and credit for dependents instead of before such deduction as at present	[20.0]	[11.6]		
3. Increase the surtax rates by adopting the rate schedule shown in Exhibit 3	425.5 2/	246.0 2/		
4. Disallow the deduction for taxes paid, other than business taxes and State personal net income taxes	31.0	17.9		
5. Restore the exemption of dividends from the normal Federal income tax as under the Revenue Act prior to 1936	- 98.1	- 56.7		
6. Tax husbands and wives as units by aggregating their income through permitting, at their option, the filing of separate returns	[150.0]	[86.7]		
7. Impose income normal tax and surtax on: (a) Salaries of State and local officials and employees	15.0	8.7		
(b) Interest from future issues of Federal, State and local obligations	0 3/	0 3/		
8. Amend Section 117(c) providing alternative taxes in capital gains and losses by substituting 50 percent for 30 percent	[- 14.0] 4/	[- 8.1] 4/		
9. Amend Section 105 changing the limiting rate to 50 percent	-	-		
10. Change the treatment of capital losses: (a) By providing a carry-forward of long-term losses (net offset against long-term gains or other income) for a period of three years against long-term gains	[- 10.0] 5/	0		
(b) By extending the short-term carry-over of losses to three years	[- 20.0] 5/	0		
11. Change the basis for determining capital gains for property transmitted at death (Section 113(a)(5) so that the basis shall be the basis of property in the hands of the decedent instead of the fair market value at the time of acquisition. The basis for determining loss should be the basis as determined or the fair market value of the property at the time of death, whichever is lower	[10.0]	0		
12. Allow net business losses of individuals (to include losses from partnerships) and fiduciaries to be carried forward for a period of five years (from year of origin of loss) to be offset against business income but not other income	[- 10.0]	0		
13. The effect of individual income tax, items 1 - 12 in combination			[511.8]	[385.3]
B. Corporation income tax				
1. Allow a net loss carry-over for purposes of all corporate income taxes for a period of five years after the year of origin. In computing the carry-over adjust the net loss by disallowing all depletion deduction and based on cost or March 1, 1913 value and adding tax-exempt interest and (the remaining) 85 percent of dividends received. The first year of origin should be the taxable year beginning during calendar year 1939	- 60.7 6/	0		
2. Increase the corporation income tax rates to produce at least enough revenue to offset the effects of the loss carry-over (1. above), in an average year:				
Special class income corporations:				
Subject to flat rate — 17 3/4 percent				
Under $25,000 net income:				
$ 0 - 5,000 — 13½ "				
5,000 - 20,000 — 15 "				
20,000 - 25,000 — 17 "				
General rule corporations:				
Basic tax rate — 20½ "				
Dividends received credit — 17 3/4 "				
Dividends paid credit — 2½ "	60.7 6/	22.0		
3. Lower the percentages for depletion deduction from 27½ percent of gross income in the case of gas and oil properties to 15½ percent; from 23 percent of gross income in the case of sulphur mines or deposits to 11½ percent; from 15 percent of gross income in the case of metal mines to 7½ percent; and from 5 percent of gross income in the case of coal mines to 2½ percent	11.4	5.3		
4. Impose corporation income tax on interest from future issues of Federal, State, and local obligations	0 3/	0 3/	11.4	27.3
5. The effects of the corporation income tax, items 1 - 4 in combination				
C. Temporary income tax on individuals on income tax due for the taxable year 1939 at 18 percent as shown in fiscal year 1940 the full year's effect of the changes in III A. above	-	[246.5]	-	[246.5]
Total individual, corporation and temporary individual income tax (the sum of A. B and C)			[643.2]	[699.1]
IV. Other business taxes				
A. Capital stock and excess profits taxes. Repeal the capital stock taxes effective for the July 1940 payment and the excess profits tax effective for the taxable year ending after June 30, 1940	- 125.0	0		
B. Unincorporated business privilege tax. Impose a 2 percent tax on "privilege net income" of unincorporated business enterprises payable March 15 and June 15 (see IV B of memorandum)	[25.0]	[25.0]		
C. Corporation privilege tax. Impose a 4 percent tax on privilege net income of corporations payable March 15 and June 15 (see IV C of memorandum)	478.1	441.5 2/		
Total other business taxes (sum of A. B and C)			[378.1]	[466.5]
V. Excise taxes				
1. Increase the tax on beer from $5 per barrel to $7	85.2	85.2		
2. Increase the excise tax on distilled spirits except brandy from $2.25 per gallon to $2.50 per gallon, and levy a corresponding floor stock tax	[25.5]	[25.5]		
3. Shift the present tax on radio parts to a tax on completed radios and increase the rate to 10 percent	[8.0]	[8.0]		
4. Impose a tax on the gross receipts of radio broadcasting companies	[25.0]	[25.0]		
5. Increase by 50 percent the rates of tax on the manufacture of cigars, tobacco, and snuff	91.5	171.1		
6. Put the period from date of enactment to June 30, 1940, increase the gasoline tax from 1 cent per gallon to 2 cents per gallon, and thereafter decrease the rate from 2 cents per gallon to 1½ cents per gallon	56.2	56.2		
7. Substitute for the present taxes on the transfer of bonds and stocks, a tax based on the sale price thereof at the rate of 1/4 of 1 percent to both instances	54.3	54.3		
8. Repeal the check tax which lapsed December 31, 1938	50.0	50.0		
9. Reduce the present exemptions under the 10 percent admissions tax from 40 cents to 20 cents			[385.7]	[466.5]
Total of excise tax, items 1 - 9			[1,025.8]	[1,640.8]
Grand total of I - V				

October 25, 1938.

Treasury Department, Division of Tax Research

1/ For income tax and other business taxes the basis of estimate is calendar year 1939; and for other taxes the basis of estimate is fiscal year 1940.
2/ If the top amount rate were limited to 60 percent the figures would be 382.7 and 230.6, respectively; if limited to 65 percent the figures become 414.4 and 240.7, respectively.
3/ If the top amount rate were limited to 60 percent the figures would increase produce only on the existing tax amount securities were redeemed and replaced by new issues without exempt feature.
4/ The normal additional income tax revenue from this proposal would increase produce only on the existing tax amount securities were redeemed and replaced by new issues without exempt feature.
5/ Rate is based on an estimate that individuals long-term losses in 1939 will slightly exceed long-term gains. In years when such gains exceed the losses the change will yield additional revenue; and in years when such gains are less than the losses the change will result in less revenue.
6/ Figures are for an average year, giving full effect to the three-year carry-forward.
7/ This figure is for an average year. The revenue loss from the carry-forward of losses and the revenue gain from the increase in rates over the rates in the revenue act of 1936 will vary from year to year, resulting sometimes in a net gain of revenue and sometimes in a net loss of revenue, depending upon business conditions.
8/ Full year tax liability reduced by an estimated allowance for deferred payments.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE October 24, 1938.

TO Mr. Hanes

FROM Mr. Blough RB

Subject: Methods of raising additional tax revenues.

To raise the specified sum of $2,000,000,000 additional annual revenue will probably necessitate all of the tax increases described below or their equivalents, unless business and national income increase substantially over present levels. A brief summary of the changes is shown in Exhibit A.

Whether the increased rates and new taxes described will in fact produce the required $2,000,000,000 is problematical, for three reasons: (1) The Division of Research and Statistics has found it physically impossible to prepare the estimates of yield for some of the taxes within the necessary time limit; (2) the estimates made thus far are for taxes considered each by itself without reference to the impact of one tax on the revenues from the others; and, most important, (3) the basis of the estimates has of necessity been the economy as it was situated before the imposition of the taxes, while in actual fact the shock of such a large increase in taxes in so short a time might so disrupt business and reduce the national income as to seriously affect the tax-producing capacity of the whole tax system. 1/

It is deemed impossible to increase the revenue by $2,000,000,000 in the current fiscal year 1938-39. Substantial increases in revenue might be secured for that year either by passing tax legislation at a special session of Congress before the end of the calendar year 1938, or by passing tax measures in the early months of 1939 retroactive to 1938. The disadvantages of either method are perhaps too obvious to require comment.

If the continuing tax changes described herein were passed during the regular 1939 session of Congress, substantial parts of the increases would be effective for the fiscal year 1939-40, but the program as a whole would not have its full effect on revenues until fiscal 1940-41, and in minor respects the full effect would be delayed until fiscal 1941-42 (due mainly to fiscal year income tax returns and delayed estate tax returns). To produce the desired revenue for fiscal 1939-40, special temporary legislation would accordingly be necessary. A brief summary of legislation to accomplish this result is shown in Exhibit B.

1/ Since the above was written, estimates and intelligent guesses of revenue yields indicate that the added revenue likely to be received from the described tax changes in a full year, at the probable 1939-40 level, would be short of $2 billions by about $200 millions. See Exhibit J.

In choosing among the limited number of possible tax sources an important objective has been to avoid as much as possible harmful repercussions on the economy. It is believed that this can be attained best by increasing the estate and gift taxes and the individual income tax before resorting to additional taxes on business, and by imposing additional general business taxes before resorting to sales and excise taxes. However, it has proved necessary to provide increased rates and new taxes even for the more undesirable tax types. In the following description of sources of additional revenue, the sources are listed roughly in what is believed to be their order of merit under existing conditions.

Estimates of yields of individual taxes and tax changes insofar as they are now available are shown in Exhibit J.

I. Estate Tax

1. Change the specific exemption from $40,000 to a specific exemption determined by aggregating the following exemptions allowable as a deduction from the gross estate. If the decedent is survived by:

(a)	A widow	$30,000
(b)	A widower	15,000
(c)	One orphan under 21	30,000
(d)	Each other child under 21	5,000

For administrative purposes a minimum specific exemption of $10,000 should, however, be allowed, irrespective of the number and type of beneficiaries. It is estimated that on average the effect of this proposal will be to reduce the specific exemption from $40,000 to between $20,000 and $25,000.

2. Increase the estate tax rates by adopting the rate schedule shown in Exhibit C. The combined effects of the changes in exemptions and rates are tabulated in Exhibit D and shown in graphic form in Exhibit E.

3. Eliminate the $40,000 estate tax insurance exclusion.

4. Pass a joint resolution in February 1939 eliminating the provision which allows an executor to value an estate as of the date one year after the decedent's death, and restricting the period for filing estate tax returns to twelve months instead of fifteen months after death as at present. The effect of this resolution would be to augment the revenues for the fiscal year 1939-40 to the extent that payment of estate taxes on the estates of decedents dying during the period April-June 1939 would otherwise have been deferred until after June 30,1940. 1/

II. Gift Tax

1. Decrease the annual allowance of tax-free gifts per donee from $4,000 to $2,500.

2. Reduce the specific gift tax exemption from $40,000 to $15,000.

1/ After the estimates were prepared it would appear that the revenue increase in 1940 would not be great enough to warrant a special joint resolution.

3. Increase the gift tax rates to the same level as those proposed for the estate tax.

III. Income Tax

A. Individual income tax.

1. Reduce personal exemption to $800 for single individual and $2,000 for married person and head of family.

2. Compute both the normal tax credit of 10 percent of earned income and the lower and upper earned income limits of $3,000 and $14,000, respectively, on the amount of net income after deducting the personal exemption and credit for dependents, instead of before such deduction, as at present.

3. Increase the surtax rates by adopting the rate schedule shown in Exhibit F. The combined effects of the changes in exemptions, normal tax credit and rates are tabulated in Exhibit G-1 and G-2 and shown in graphic form in Exhibit H-1 and H-2.

4. Disallow the deduction for taxes paid other than business taxes and State personal net income taxes.

5. Restore the exemption of dividends from normal Federal income tax as under the Revenue Acts prior to 1936. This will act to reduce revenues but is deemed an important factor in tax equity in view of increases in individual and corporation rates.

6. Tax husbands and wives as units by aggregating their income, though permitting, at their option, the filing of separate returns. Under present law husbands and wives may file joint returns, or, at their option, separate returns. In the latter case the husband and the wife may each report and be taxed on such income as is viewed to be theirs under State property laws. In community property States the usual division is one-half of the community income to each spouse; the practice followed in other States is less uniform. This results in interstate variations of Federal income tax burden. In addition, the use of separate returns enables wealthy husbands and wives to avoid high surtax rates, which would otherwise be applicable. If the incomes of husbands and wives be considered as properly constituting a unit, existing practice is inequitable. To overcome such inequity the tax liability may be determined on the basis of the aggregate income of husband and wife, the liability then being prorated to each according to the amount of his income. Since many people believe equity would thus be increased and since the change would produce very substantial revenue, the proposal is included here.

7. Impose income normal tax and surtax on (a) salaries of State and local officials and employees, and (b) interest from future issues of Federal, State and local obligations.

8. Amend section 117(c), providing alternative taxes on capital gains and losses, by substituting 50 percent for 30 percent wherever it appears, so that capital gains will bear their due share in the increased individual income tax rates.

9. Change the limit on surtax on gains from sale of oil and gas properties prospected by individuals from 30 percent of sale price to 50 percent of sale price. (Section 105, Revenue Act of 1938.)

10. Change the treatment of capital losses (a) by providing a carry-forward of long-term losses (not offset against long-term gains or other income) for a period of three years, against long-term gains; and (b) by extending the short-term carry-over of losses to three years.

11. The basis for determining capital gains for property previously transmitted at death (Section 113(a)(5) shall be the basis of the property in the hands of the decedent instead of the fair market value at the time of acquisition. The basis for determining loss shall be the basis so determined or the fair market value of the property at the time of death, whichever is lower. This procedure for determining capital gains and losses is the same as that now in force for property acquired by gift. Capital gains not previously realized or subject to income tax would thus become taxable to the beneficiary if the property were sold or exchanged, eliminating in part a tax loophole for capital gains in the present income tax law.

12. Allow net business losses of individuals (to include losses from partnerships) and fiduciaries to be carried forward for a period of three or more years (from year of origin of loss) to be offset against business income but not other income. The first possible year of origin should be the taxable year beginning during 1939. This change will therefore not affect the revenues for the fiscal year 1940. The purpose of the change is to reduce the inequity in taxing fluctuating incomes now present in the law, which inequity becomes very serious with high rates of tax.

B. Corporation income tax.

1. Allow a net loss carry-over for purposes of all corporate income taxes for a period of three or more years from the year of origin. In computing the carry-over, adjust the net loss by disallowing all depletion deduction not based on cost or March 1, 1913 value and adding tax-exempt interest and the remaining 85 percent of dividends received. The first year of origin should be the taxable year beginning during 1939. This change reduces the revenue but in view of increased business taxes it is deemed desirable to reduce the inequity involved in taxing fluctuating incomes by allowing the carry-over. This change will not affect the revenues for the fiscal year 1940.

2. Increase the corporate income tax rates sufficiently to produce at least enough revenue to offset the effects of the loss carry-over (1. above), in an average year.

3. Lower the percentages for depletion deduction from 27½ percent of gross income in the case of gas and oil properties to 13-3/4 percent; from 23 percent of gross income in the case of sulphur mines or deposits to 11½ percent; from 15 percent for gross income in the case of metal mines to 7½ percent; and from 5 percent in the case of coal mines to 2½ percent.

4. Impose corporation income tax on interest from future issues of Federal, State and local obligations.

C. Temporary income tax.

The increased revenues derived from changes in income taxes will be reflected only in part in the fiscal year 1939-40. With respect to corporations the discrepancy between the full year's application of the changes and their fiscal year 1940 effects is negligible. If, however, the revenue from individual income taxes in that year is to be equal to the revenue resulting from a full year's application of the changes, an additional income tax may be imposed payable on March 15 and June 15, 1940 only, this tax to be a sufficient percentage of the income tax due for the taxable year 1939 to make up the revenue deficiency.

This tax will be necessary only if it is desired to secure full revenue increases in the fiscal year 1939-40.

IV. Other Business Taxes

A. Capital stock and excess profits taxes.

Repeal the capital stock tax, effective for the July 1940 payment, and the excess profits tax, effective for the taxable year ending after June 30,1940. The repeal of these taxes reduces the revenue, but because of the undesirable nature of the taxes, it is deemed desirable to supply the revenue from the business privilege tax discussed in C below.

B. Unincorporated business privilege tax.

Impose a 2 percent tax on "privilege net income" of unincorporated business enterprises including any trade or business which, if conducted or engaged in by a corporation, would be taxable under the income tax, but

excluding the professions and any cases in which more than 50 percent of the gross income is derived from the personal services rendered by the individual or the members of the partnership or other entity in which capital is not a material income-producing factor. "Privilege net income" is defined in all respects in the same manner as the net income of corporations is defined under the Revenue Act of 1938 except that (a) tax-exempt interest on Government obligations held in connection with carrying on trade or business shall be included in the taxable base; (b) deductions shall not be allowed for (1) rent paid on business property, (2) taxes paid on business property, (3) interest paid for capital engaged in the business, and (4) depreciation of buildings; and (c) the deduction on account of the personal service of an individual or member of a partnership shall in no case exceed $5,000 per such individual or member. A specific exemption of $5,000 is allowed for each enterprise.

C. Corporation privilege tax.

Impose a 4 percent tax on the privilege net income of corporations defined as in (1) above, except for the limitation in (c) which does not apply. A specific exemption of $5,000 is allowed.

A comparison of the base for the corporation privilege tax and the corporation income tax by major industrial groups is shown in Exhibit I.

The taxes ~~proposed in (1) and (2) above~~ shall be payable in two installments on March 15 and June 15. The purpose of these payment dates is to secure additional needed revenue in fiscal 1939-40; otherwise four installments might be allowed as in the income tax.

V. Excise Taxes

1. Increase the excise tax on beer from $5 per barrel to $7.

2. Increase the excise tax on distilled spirits, except brandy, from $2.25 per gallon to $2.50 per gallon, and levy a corresponding floor stock tax.

3. Shift the present tax on radio parts to a tax on completed radios and increase the rate to 10 percent.

4. Impose a tax on the gross receipts of radio broadcasting companies.

5. Increase by 50 percent the rates of tax on the manufacture of cigars, tobacco, and snuff. The present rates on cigars are from 75 cents per thousand to $13.50 per thousand, depending upon the weight; and on tobacco and snuff, 18 cents per pound.

6. For the period from date of enactment to June 30,1940, increase the gasoline tax from 1 cent per gallon to 2 cents per gallon, and thereafter decrease the rate from 2 cents per gallon to 1½ cents per gallon.

7. Substitute for the present taxes on the transfer of bonds and stocks, a tax based on the sale price thereof at the rate of 1/4 of 1 percent in both instances. The present rates are

Bonds - 4 cents per $100 face value;
Stocks- 4 cents per $100 par or face value or fraction, or if without par or face value, 4 cents per share. However, if selling price is $20 or over, whether with or without par or face value, the rate is 5 cents instead of 4 cents.

8. Reenact the check tax which lapsed December 31, 1934. The rate of this tax was 2 cents per check or draft.

9. Reduce the present exemption under the 10 percent admission tax from 40 cents to 20 cents.

Exhibit A

Summary Statement of Described Methods of Increasing Tax Revenues

Estate Tax

Decreased exemptions
Greatly increased rates, except in top brackets
Elimination of deduction of insurance
Other changes

Gift Tax

Decreased exemptions
Increased rates to equal new estate tax rates

Income Taxes

Greatly increased personal surtax rates, except in top brackets
Decreased personal and family exemptions
Aggregation of family incomes for tax computation
Imposition of Federal personal and corporation income taxes on: (1) interest from future issues of Federal, State, and local bonds; (2) exempt State and local salaries
Increased corporation income tax rates (to be offset in future years by loss carryover)
Other changes

New business privilege tax on corporations and unincorporated business (present capital stock and excess profits taxes to be repealed)

Excise Taxes: increased rates on

Beer
Distilled spirits
Tobacco (other than cigarettes)
Gasoline
Transfers of stocks and bonds
Admissions (by decreasing exemptions)
Radios

New excise taxes on

Checks
Radio broadcasting companies

Exhibit B

Additional Tax Changes to Increase Revenues in Fiscal Year 1939-1940

Estate Tax

Joint resolution to be passed in February 1939 eliminating the provision which allows an executor the option of valuing an estate as of the date one year after the decedent's death, and restricting the period of filing estate tax returns to 12 months instead of 15 months after death as at present.

Income Taxes

Temporary emergency tax on individuals and corporations computed as a percentage of the income tax on 1939 incomes, payable March 15 and June 15, 1940.

Excise Taxes

Additional 1/2 cent a gallon on gasoline for the fiscal year 1939-1940 only.

Exhibit C

Proposed estate tax rate schedule

Taxable base: net estate after specific exemption 1/ (dollars in thousands)	Size of bracket (dollars in thousands)	Bracket rate	Cumulative tax
$ 0 - $ 5	$ 5	4	$ 200
5 - 10	5	8	600
10 - 20	10	12	1,800
20 - 30	10	16	3,400
30 - 40	10	20	5,400
40 - 60	20	23	10,000
60 - 80	20	26	15,200
80 - 100	20	29	21,000
100 - 150	50	32	37,000
150 - 200	50	35	54,500
200 - 250	50	38	73,500
250 - 300	50	41	94,000
300 - 400	100	44	138,000
400 - 500	100	47	185,000
500 - 600	100	50	235,000
600 - 800	200	53	341,000
800 - 1,000	200	56	453,000
1,000 - 2,000	1,000	59	1,043,000
2,000 - 5,000	3,000	62	2,903,000
5,000 - 10,000	5,000	64	6,103,000
10,000 - 15,000	5,000	66	9,403,000
15,000 - 20,000	5,000	68	12,803,000
20,000 - 30,000	10,000	70	19,803,000
30,000 - 50,000	20,000	72	34,203,000
50,000 and over		73	

Treasury Department, Division of Tax Research — October 24, 1938

1/ The specific exemption is the sum of the following: For a widow, $30,000; a widower, $15,000; first orphan under 21, $30,000; and each other child under 21, $5,000.

EXHIBIT D.

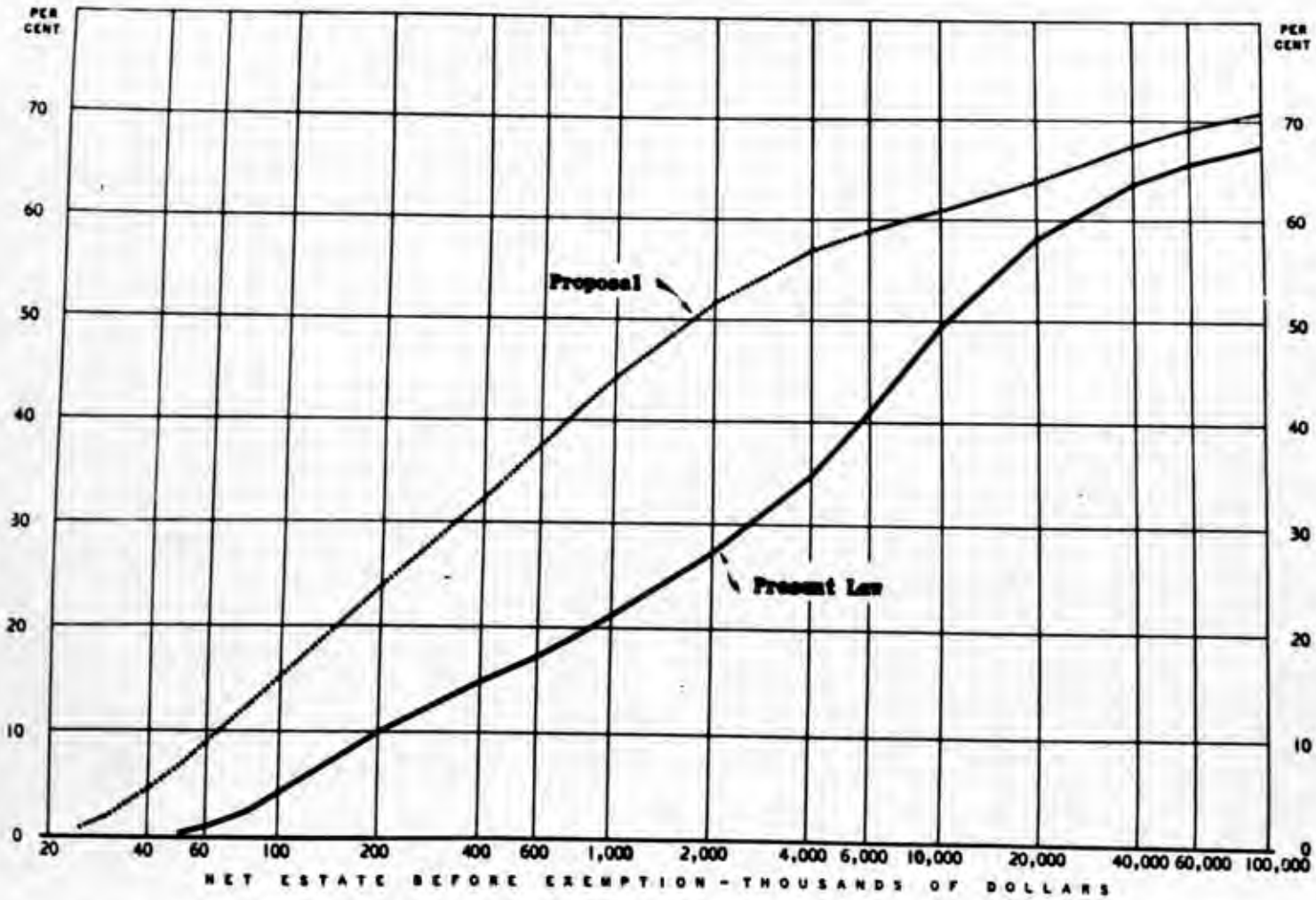
Estate tax: Comparison of amounts of tax and effective rates on selected sizes of net estate (before exemption) under the present law and under the proposal

Net estate before exemption 1/ (in thousands)	Amounts of tax: Present law	Amounts of tax: Proposal	Effective rates: Present law	Effective rates: Proposal
$ 25	-	$ 200	-	.8%
30	-	600	-	2.0
40	-	1,800	-	4.5
50	$ 200	3,400	.4%	6.8
60	600	5,400	1.0	9.0
80	2,000	10,000	2.5	12.5
100	4,200	15,200	4.2	15.2
200	19,800	47,500	9.9	23.8
400	58,600	129,200	14.7	32.3
600	103,400	225,000	17.2	37.5
800	154,200	330,400	19.3	41.3
1,000	211,000	441,800	21.1	44.2
2,000	543,600	1,031,200	27.2	51.6
4,000	1,388,800	2,270,600	34.7	56.8
6,000	2,460,200	3,530,200	41.0	58.8
8,000	3,658,200	4,810,200	45.7	60.1
10,000	4,936,600	6,090,200	49.4	60.9
20,000	11,635,800	12,789,400	58.2	63.9
40,000	25,435,000	26,988,600	63.6	67.5
60,000	39,334,600	41,488,400	65.6	69.1
100,000	67,334,600	70,688,400	67.3	70.7

1/ The exemption under the proposal on the basis of 1936 data is on average $21,132. For the purpose of this computation, however, a $20,000 exemption was assumed.

Exhibit E

EFFECTIVE ESTATE TAX RATES PRESENT LAW AND PROPOSAL



Office of the Secretary of the Treasury

Exhibit F

Proposed individual income surtax rate schedule

Amount of surtax net income: (In thousands)	Rate of tax (Percent)	Total surtax cumulative
0 - .5	-	-
.5 - 1	2	10
1 - 2	3	40
2 - 3	5	90
3 - 6	7	300
6 - 8	10	500
8 - 10	12	740
10 - 12	15	1,040
12 - 14	18	1,400
14 - 16	21	1,820
16 - 18	25	2,320
18 - 20	29	2,900
20 - 22	33	3,560
22 - 24	37	4,300
24 - 28	41	5,940
28 - 34	45	8,640
34 - 40	49	11,580
40 - 48	53	15,820
48 - 56	56	20,300
56 - 64	58	24,940
64 - 72	60	29,740
72 - 80	62	34,700
80 - 90	64	41,100
90 - 100	65	47,600
100 - 150	66	80,600
150 - 200	67	114,100
200 - 300	68	182,100
300 - 500	69	320,100
500 - 750	70	495,100
750 - 1,000	72	675,100
1,000 - 2,000	73	1,405,100
2,000 - 5,000	74	3,625,100
5,000 and up	75	

EXHIBIT G-1.

Single person with no dependents: Comparison of the amount of income tax liability and effective rate of tax under present law and under proposal

Selected net income (thousands of dollars)	Amount of tax 1/		Effective rate	
	Present law	Proposal 2/	Present law	Proposal 2/
$ .5	-	-	-	-
1	-	$ 7	-	0.7%
2	$ 32	59	1.6%	3.0
2.5	50	92	2.0	3.7
3	68	129	2.3	4.3
6	216	431	3.6	7.2
8	378	679	4.7	8.5
10	560	975	5.6	9.8
12	762	1,323	6.4	11.0
14	984	1,731	7.0	12.4
16	1,234	2,204	7.7	13.8
18	1,514	2,752	8.4	15.3
20	1,834	3,380	9.2	16.9
22	2,194	4,088	10.0	18.6
24	2,594	4,876	10.8	20.3
28	3,454	6,644	12.3	23.7
34	4,854	9,552	14.3	28.1
40	6,384	12,700	16.0	31.8
48	8,714	17,228	18.2	35.9
56	11,394	22,004	20.3	39.3
64	14,514	26,948	22.7	42.1
72	18,074	32,052	25.1	44.5
80	22,034	37,316	27.5	46.6
90	27,494	44,100	30.5	49.0
100	33,354	50,992	33.4	51.0
150	64,324	85,984	42.9	57.3
200	96,304	121,476	48.2	60.7
250	129,284	157,468	51.7	63.0
300	163,264	193,468	54.4	64.5
400	233,244	266,460	58.3	66.6
500	305,224	339,460	61.0	67.9
750	490,204	524,452	65.4	69.9
1,000	680,184	714,436	68.0	71.4
2,000	1,450,174	1,484,428	72.5	74.2
5,000	3,790,164	3,824,420	75.8	76.5

1/ Maximum earned income allowed.
2/ Basis of tax computation for proposal: Personal exemption $800 allowed as a deduction for both normal and surtax; earned income credit of 10 percent and the lower and upper earned income limits of $3,000 and $14,000 maximum, computed on net income after deducting personal exemption; proposed increased surtax rates; and normal tax 4 percent.

EXHIBIT G-2.

Married person with two children: Comparison of the amount of income tax liability and effective rate of tax under present law and under proposal

Selected net income (thousands of dollars)	Amount of tax 1/		Effective rate	
	Present law	Proposal 2/	Present law	Proposal 2/
$ .5	-	-	-	-
1	-	-	-	-
2	-	-	-	-
2.5	-	-	-	-
3	-	$ 7	-	0.2%
6	$ 84	219	1.4%	3.7
8	184	431	2.3	5.4
10	343	679	3.4	6.8
12	522	975	4.4	8.1
14	721	1,323	5.2	9.5
16	948	1,731	5.9	10.8
18	1,195	2,204	6.6	12.2
20	1,469	2,752	7.3	13.8
22	1,783	3,380	8.1	15.4
24	2,137	4,088	8.9	17.0
28	2,951	5,744	10.5	20.5
34	4,305	8,572	12.7	25.2
40	5,779	11,640	14.4	29.1
48	8,001	16,088	16.7	33.5
56	10,589	20,804	18.9	37.2
64	13,577	25,708	21.2	40.2
72	16,993	30,772	23.6	42.7
80	20,861	35,996	26.1	45.0
90	26,229	42,740	29.1	47.5
100	31,997	49,612	32.0	49.6
150	62,898	84,584	41.9	56.4
200	94,832	120,056	47.4	60.0
250	127,766	156,028	51.1	62.4
300	161,700	192,028	53.9	64.0
400	231,634	265,000	57.9	66.3
500	303,568	338,000	60.7	67.6
750	488,502	522,972	65.1	69.7
1,000	678,436	712,916	67.8	71.3
2,000	1,448,403	1,482,888	72.4	74.1
5,000	3,788,370	3,822,860	75.8	76.5

1/ Maximum earned income allowed.
2/ Basis of tax computation for proposal: Personal exemption $2,000 allowed as a deduction for both normal and surtax; earned income credit of 10 percent and the lower and upper earned income limits of $3,000 and $14,000 maximum, computed on net income after deducting personal exemption and credit for dependents; proposed increased surtax rates; and normal tax 4 percent.

487 Exhibit 21-1

EFFECTIVE INDIVIDUAL INCOME TAX RATES, PRESENT LAW AND PROPOSAL

Married Person with Two Dependents

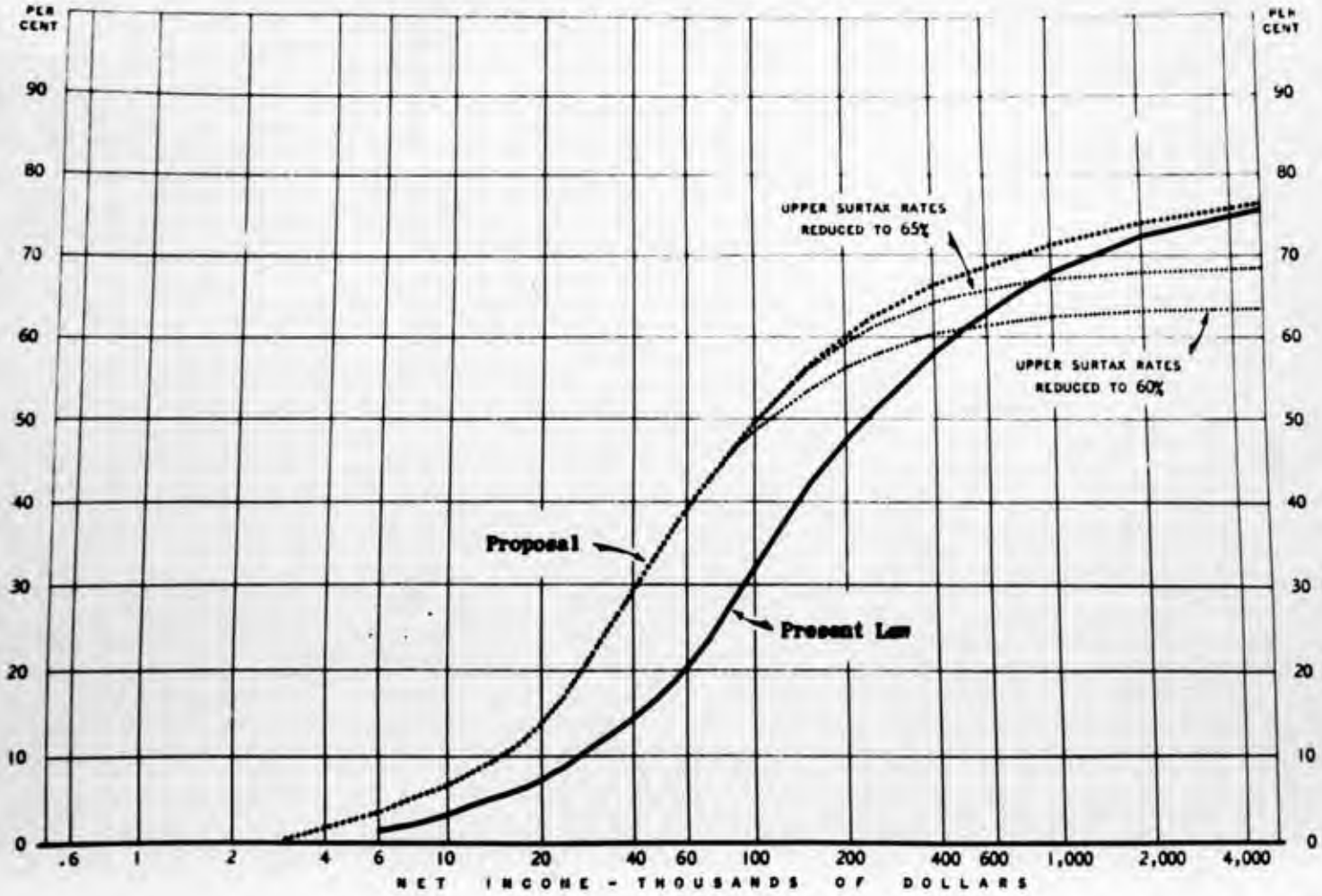


Exhibit H-2

488

EFFECTIVE INDIVIDUAL INCOME TAX RATES, PRESENT LAW AND PROPOSAL

Married Person with Two Dependents

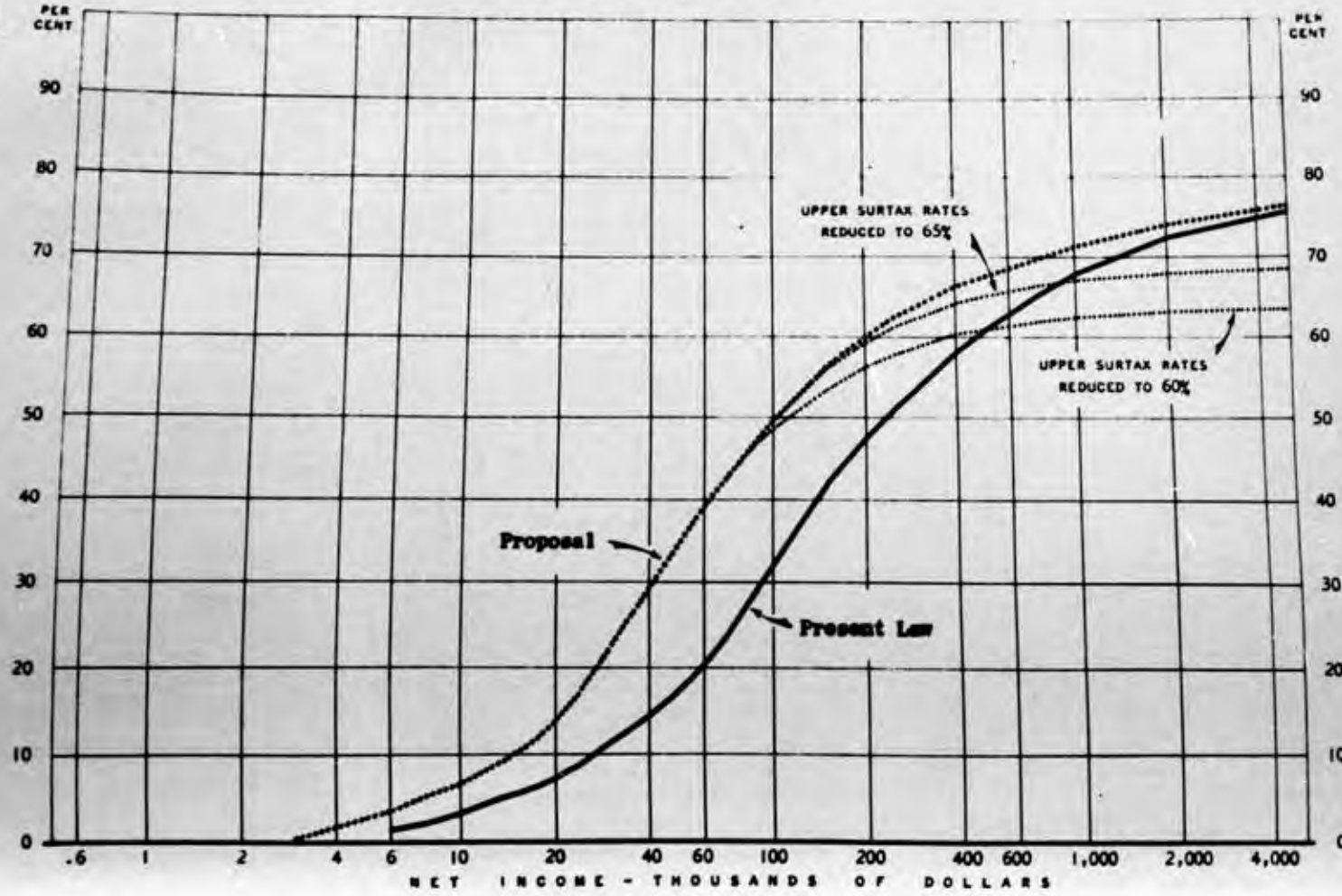


Exhibit I

Comparison of proposed tax base and present tax base for corporations with net income, 1935

Industrial groups	Privilege tax net income--proposed base	Net income 1/	Ratio of proposed to present base
	(In millions of dollars)		
Agriculture	97	45	2.2
Mining and quarrying	320	167	1.9
Manufacturing:			
Food	618	326	1.9
Liquors	297	108	2.8
Tobacco	188	101	1.9
Textiles	337	172	2.0
Leather	73	48	1.5
Rubber	91	31	2.9
Forest products	81	39	2.1
Paper, pulp, etc.	176	93	1.9
Printing, etc.	237	142	1.7
Chemicals, etc.	829	390	2.1
Stone, clay, etc.	151	91	1.7
Metal, etc.	1,532	900	1.7
Manufacturing n.e.c.	164	110	1.5
Total manufacturing	4,772	2,551	1.9
Construction	87	49	1.8
Transportation	2,908	957	3.0
Trade	1,665	776	2.1
Service	361	128	2.8
Finance	2,004	713	2.8
Nature of business not given	1	-	-
Grand total	12,216	5,389	2.3

Source: "Statistics of Income".

1/ Income reported plus 15 percent of dividends from domestic corporations; such dividends having been made taxable on incomes after 1935.

Exhibit 2 - Estimates of revenue effects of the proposals contained in the memorandum

The estimates are arranged and numbered in the same order in which the proposals appear in the memorandum. The figures given below are revenue estimates prepared by the Division of Research and Statistics, Treasury Department, except those enclosed in [ ]. The latter figures are only intelligent guesses and may be widely in error.

Detailed schedule	Estimated increase in revenue: First full year 1/	Estimated increase in revenue: Fiscal year 1940	Summary: Estimated increase in revenue: First full year 1/	Summary: Estimated increase in revenue: Fiscal year 1940
		(Millions of dollars)		
I. Estate tax				
1. Change the specific exemption from $40,000 to a specific exemption determined by aggregating the following exemptions allowable as a deduction from the gross estate irrespective of the actual nature of the distribution of the estate to the beneficiaries. If the decedent is survived by: (a) A widow, $30,000; (b) a widower, $15,000; (c) one orphan under 21, $10,000; (d) each other child under 21, $5,000. A minimum specific exemption of $10,000 should, however, be allowed, irrespective of the number and type of beneficiaries	27.1	6.7		
2. Increase the estate tax rates by adopting the rate schedule shown in Exhibit 2	238.0	83.8		
3. Eliminate the $40,000 estate tax insurance exclusion	8.3	.8		
4. Pass a joint resolution in February 1939 eliminating the provision which allows an executor to value an estate as of the date one year after the decedent's death, and restricting the period for filing estate tax returns to twelve months instead of fifteen months after death as at present	3.0	24.3		
5. The effect of the estate tax, items 1 - 4 in combination			302.9	54.8
II. Gift tax				
1. Decrease the annual allowance of tax free gifts per donee from $4,000 to $2,500	1.2	.5		
2. Reduce the specific gift tax exemption from $40,000 to $15,000	10.7	3.1		
3. Increase the gift tax rates to the same level as those proposed for the estate tax (see Exhibit 2)	63.5	30.1		
4. The effect of the gift tax, items 1 - 3 in combination			69.9	30.3
III. Income tax				
A. Individual income tax				
1. Reduce personal exemptions to $800 for single individual and $2,000 for married person and head of family	50.0	22.9		
2. Compute both the earned income credits and limits on net income after deducting personal exemptions and credit for dependents instead of before such deduction as at present	[20.0]	[11.6]		
3. Increase the surtax rates by adopting the rate schedule shown in Exhibit 2	485.5 2/	[240.0 2/]		
4. Disallow the deduction for taxes paid, other than business taxes and State personal net income taxes	31.0	17.9		
5. Restore the exemption of dividends from the normal Federal income tax as under the Revenue Acts prior to 1936	- 94.1	- 56.7		
6. Tax husbands and wives as units by aggregating their income through permitting, at their option, the filing of separate returns	[150.0]	[85.7]		
7. Impose income normal tax and surtax on: (a) Salaries of State and local officials and employees	15.0	8.7		
(b) Interest from future issues of Federal, State and local obligations	0 3/	0 3/		
8. Amend Section 117(c) providing alternative taxes in capital gains and losses by substituting 50 percent for 30 percent	- 14.0 4/	- 8.1 4/		
9. Amend Section 105 changing the limiting rate to 50 percent	-	-		
10. Change the treatment of capital losses: (a) By providing a carry-forward of long-term losses (net offset against long-term gains or other income) for a period of three years against long-term gains	- 10.0 5/	0		
(b) By extending the short-term carry-over of losses to three years	- 20.0 5/	0		
11. Change the basis for determining capital gains for property transmitted at death (Section 113(a)(5)) so that the basis shall be the basis of property in the hands of the decedent instead of the fair market value at the time of acquisition. The basis for determining loss should be the basis as determined or the fair market value of the property at the time of death, whichever is lower	[10.0]	0		
12. Allow net business losses of individuals (to include losses from partnerships) and fiduciaries to be carried forward for a period of five years (from year of origin of loss) to be offset against business income but not other income	- 10.0	0	[631.4]	[395.3]
13. The effect of individual income tax, items 1 - 12 in combination				
B. Corporation income tax				
1. Allow a net loss carry-over for purposes of all corporate income taxes for a period of five years after the year of origin. In computing the carry-over adjust the net loss by disallowing all depletion deduction not based on cost or March 1, 1913 value and adding tax-exempt interest and (the remaining) 85 percent of dividends received. The first year of origin should be the taxable year beginning during calendar year 1939	- 60.7 6/	0		
2. Increase the corporation income tax rates to produce at least enough revenue to offset the effects of the loss carry-over (1. above), in an average year:				
Special class income corporations:				
Subject to flat rate — 17 3/4 percent				
Under $25,000 net income:				
$ 0 - 5,000 — 13½ *				
5,000 - 20,000 — 15 *				
20,000 - 25,000 — 17 *				
General rule corporations:				
Tentative tax rate — 20½ *				
Dividends received credit — 17 3/4 *				
Dividends paid credit — 2½ *	60.7 6/	22.0		
3. Lower the percentages for depletion deduction from 27½ percent of gross income in the case of gas and oil properties to 13½ percent; from 23 percent of gross income in the case of sulphur mines or deposits to 11½ percent; from 15 percent of gross income in the case of metal mines to 7½ percent; and from 5 percent of gross income in the case of coal mines to 2½ percent	31.4	9.3		
4. Impose corporation income tax on interest from future issues of Federal, State, and local obligations	0 3/	0 3/	11.4	47.3
5. The effects of the corporation income tax, items 1 - 4 in combination				
C. Temporary income tax on individuals on income tax due for the taxable year 1939 at 18 percent to obtain in fiscal year 1940 the full year's effect of the changes in III A. above	-	[246.5]	-	[246.5]
			[643.2]	[699.1]
Total individual, corporation and temporary individual income tax (the sum of A, B and C)				
IV. Other business taxes				
A. Capital stock and excess profits taxes. Repeal the capital stock taxes effective for the July 1940 payment and the excess profits tax effective for the taxable year ending after June 30, 1940	- 185.0	0		
B. Unincorporated business privilege tax. Impose a 2 percent tax on "privilege net income" of unincorporated business enterprises payable March 15 and June 15 (see IV B of memorandum)	[25.0]	[25.0]		
C. Corporation privilege tax. Impose a 4 percent tax on privilege net income of corporations payable March 15 and June 15 (see IV C of memorandum)	479.1	441.5 1/		
			[319.1]	[466.5]
Total other business taxes (sum of A, B and C)				
V. Excise taxes				
1. Increase the tax on beer from $5 per barrel to $7	89.2	89.2		
2. Increase the excise tax on distilled spirits, except brandy from $1.25 per gallon to $1.50 per gallon, and levy a corresponding floor stock tax	[23.0]	23.0		
3. Shift the present tax on radio parts to a tax on completed radios and increase the rate to 10 percent	[5.0]	[5.0]		
4. Impose a tax on the gross receipts of radio broadcasting companies	[25.0]	[25.0]		
5. Increase by 50 percent the rates of tax on the manufacture of cigars, tobacco, and snuff	91.5	171.1		
6. For the period from date of enactment to June 30, 1940, increase the gasoline tax from 1 cent per gallon to 2 cents per gallon, and thereafter decrease the rate from 2 cents per gallon to 1½ cents per gallon	46.2	46.2		
7. Substitute for the present taxes on the transfer of bonds and stocks, a tax based on the sale price (based at the rate of 1/8 of 1 percent in both instances	64.3	64.3		
8. Amend the crude tax which lapsed December 31, 1938	50.0	50.0		
9. Reduce the present exemptions under the 10 percent wholesales tax from 40 cents to 20 cents			[385.7]	[426.3]
Total of excise tax, items 1 - 9			[1,809.6]	[1,640.8]
Grand total of I - V				

October 25, 1938

Treasury Department, Division of Tax Research

1/ For income tax and other business taxes the basis of estimate is calendar year 1939; and for other taxes the basis of estimate is fiscal year 1940.
2/ If the top bracket rate were reduced to 60 percent the figures would be 385.9 and 230.6, respectively; if limited to 65 percent the figures become 416.8 and 240.7, respectively.
3/ The exempt additional income tax revenue from this proposal would increase gradually as the outstanding tax exempt securities were redeemed and replaced by new issues without exempt features.
4/ This is based on an estimate that indefinite long-term losses in 1939 will slightly exceed long-term gains. In years when such gains exceed the losses the change will yield additional revenue; and in years when such gains are less than the losses the change will result in loss revenue.
5/ Figures are for an average year, giving full effect to the three-year carry-forward.
6/ This figure is for an average year. The revenue loss from the carry-forward of losses and the revenue gain from the increase in rates over the rates in the Revenue Act of 1938 will vary from year to year, resulting sometimes in a net gain of revenue and sometimes in a net loss of revenue, depending upon business conditions.
7/ Full year tax liability reduced by an estimated allowance for deferred payments.

JR

GRAY

London

Dated May 8, 1939

Rec'd 1:50 p.m.

Secretary of State,

Washington.

636, May 8, 6 p.m.

FOR TREASURY FROM BUTTERWORTH.

The announcement of the Italo-German military alliance was regarded in the city as merely giving a definition to the existing situation and the London Stock Exchange ignored this step and was somewhat strong in tendency. The foreign exchange market was extraordinarily inactive. For instance, the largest dealer in dollars had not done any spot business by noon. The British authorities continued to operate in the forward dollar market at 1-11/16 and later at 1-5/8. 91 bars were sold at gold fixing of which 17 were married, the British fund supplying a few.

KENNEDY

WWC:PEG