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GROUP MEETING

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June 1, 1939.
9:30 A. M.

PRESENT: Secretary Morgenthau
Mr. Hanes
Mr. McReynolds
Mr. Bell
Mr. White
Mr. Foley
Mr. Lochhead
Mr. Haas
Mr. Duffield
Mr. Gaston
Mr. Graves
Mrs. Klotz

H.M.Jr: Good morning everybody.

Foley: Good morning, sir.

H.M.Jr: Mac, I wish you would tell somebody -- who is looking after Customs these days?

McReynolds: Steve.

H.M.Jr: Well, anyway --

McReynolds: Unless it is Bill Johnson.

H.M.Jr: I want an investigation made as to how these auction sales of seized goods are made.

McReynolds: Yes.

H.M.Jr: And whether Treasury employees buy them, or Government employees.

McReynolds: There is a Treasury regulation covering that.

H.M.Jr: But Harry raised the question on that -- Harry Dorning -- a couple of weeks ago, and there is a memorandum being prepared on it.

H.M.Jr: Go back into the last half dozen auctions and see who bought the stuff, and also these seized Leica cameras. A good many of them are floating around the Treasury.

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McReynolds: Yes.

H.M.Jr: And find out who has them all.

McReynolds: Yes.

H.M.Jr: Get a list of these seized German cameras. I would like to know who has them. Let us go back on the auctions to January first of this year, of the Laica cameras or any other cameras since January first, and find out who got them all.

McReynolds: Yes, sir.

H.M.Jr: That is to say, take a list of the people who bought at those auctions and find out whether they are Government employees or not.

McReynolds: Of course, there are definite regulations --

H.M.Jr: I know.

McReynolds: That definitely prohibit that.

H.M.Jr: I know, Mac.

McReynolds: We will find out about it.

H.M.Jr: I think you will find some violations. Is there anything else?

McReynolds: No.

H.M.Jr: Will you get me a list of the vacancies in the Treasury now? Let us go after them. I mean Presidential appointments.

McReynolds: Yes.

H.M.Jr: Let us run down the list and check it every week. If you do not fill them now, you cannot fill them until January first, next year; is that right?

McReynolds: That is right.

H.M.Jr: Anything else?

McReynolds: That is all.

H.M.Jr: Dan?

Bell: I have nothing, except that you might be interested to know that we have just wound up the war loan deposit account that was involved in the banking holidays. We have run through these war loan accounts and they started, about sixty-six and one half billion idle dollars, and we have not lost one dollar. We just wound up the last one. We took cats and dogs as security, plus our prior rights, of course.

H.M.Jr: Why don't we get out a publicity statement?

Bell: All right.

H.M.Jr: Fix one up, will you?

Bell: Yes.

H.M.Jr: Anything else?

Bell: That is all.

H.M.Jr: Any change in the financing?

Bell: Yes. We are talking a little about the bonds, increasing the amount of the offering by a hundred million to trust account.

H.M.Jr: I thought of that, too, but I thought it was so piddling.

Bell: Well, that makes five hundred and fifty.

H.M.Jr: I mean, we will be criticized.

Bell: Why?

H.M.Jr: A hundred million dollars. You cannot sell me a bond.

Bell: I can't sell you a bond?

H.M.Jr: No, sir.

Bell: O.K., then. I do not want anything to the trust account.

H.M.Jr: No. I will not let you come between Eccles and me. We are together.

Bell: The only reason I did not want a bond particularly is because of the amount. \$400,000,000 is not large enough for a bond issue. I think we ought to add to it \$100,000,000 or \$150,000,000 for trust. Then I will be satisfied.-- five year callable to 8, and if it goes good, we could add to it by September. The market is very strong this morning; that is some indication that there is no --

H.M.Jr: Let me read you my Bible, the New York Tribune:

"Although it is plain that the Treasury does not need to raise any new money at the tax date two weeks from now, the executive committee of the Federal Open Market Committee met with Treasury officials yesterday to discuss the June financing. It appears that considerations touching other matters than the Treasury's immediate needs for cash were discussed by the authorities. These considerations doubtless include the question whether the Treasury should not anticipate its cash requirements by raising new money at this time. Doubtless, too, the strong rise in government security prices in the last month entered into the discussions. The heights to which prices of government issues have climbed are a just cause for concern. It is unquestionable that the prolonged rise in prices is storing up trouble. If a way could be devised for arresting the rise in prices without precipitating a crash, no time should be lost in putting the plan into effect. It is a question whether the offering of a new money issue would not put brakes on the rise through increasing the volume of issues available."

You cannot sell me, Dan, on a bond.

Bell: No?

H.M.Jr: No; I am sorry.

Bell: Then, I will withdraw my trust.

H.M.Jr: I thought a hundred million dollars in the Treasury at three-fourths and then kind of feed it out, mixed with five hundred thousand dollars worth of notes, but it looks to me so piddling that there would be criticism, and I don't think it is worth doing.

Bell: The \$200,000,000 is enough for the notes. I hate to pass up the opportunity of two and a half per cent money for twenty-five or thirty years.

H.M.Jr: I hate to see that bond go to ninety-seven, ninety-six or ninety-five.

Bell: There are a lot of others out that will go along with it.

H.M.Jr: Well, the older they are, the less sensitive my conscience is. (laughter).

White: And the less is your responsibility.

H.M.Jr: Yes. I can't see it, Dan. I'm sorry.

Bell: I just wanted you to consider it.

H.M.Jr: That is all right. That is all with the kindest feeling.

Bell: I do not feel bad about it.

H.M.Jr: I do not see how you can -- at three-fourths.

Bell: All right.

H.M.Jr: Harold?

Graves: Nothing.

H.M.Jr: Did that memorandum get to the Attorney General last night?

Graves: I assume it did. The letter was signed last night. I handed it to Mr. Irey to transmit.

Foley: I called Jim Morris, and he said he would take it up and put it on the A. G.'s desk.

H.M.Jr: Did he get it?

Foley: He said he would put it on his desk.

Graves: I am sure that he did.

H.M.Jr: Just check up on it, and if he did not, let me know.

Lochhead: The purchase side of the Stock Market yesterday was on the way down. The only other interesting thing is that France this week continued to purchase over on this side. The amount sold so far is nine million dollars, and that means a deposit made of twenty-four million dollars in gold.

H.M. Jr: Harry?

White: The memorandum you gave me yesterday we had seen before in modified form. I don't know whether you remember it.

H.M. Jr: I do not.

White: The last time we did not get the effect of it.

H.M. Jr: Will you give me an answer for the President.

White: Yes. It came to you a couple of months ago.

H.M. Jr: Through a different channel?

White: From the President.

H.M. Jr: Really?

White: We got it in French, we translated it here.

H.M. Jr: Maybe the next time it will come in Greek.

White: No. The Committee on gold met a couple of weeks ago, and there was a difference of opinion in regard to the daily figures. Archie and I talked it over and decided it was not worth making an issue of it, unless you wish to offer some reasons other than that.

H.M. Jr: For the rest of the summer I am picking my fights. I am very choosy.

White: We still get some uniformity in weekly figures.

H.M. Jr: Is that all?

Mrs. Klotz: So far, so good.

White: The Paraguay loan -- I do not know whether you want to know about it.

H.M. Jr: Yes; very definitely, because this is luncheon day at the White House.

White: Well, it was about a half a million dollar loan by the Export-Import bank, following the usual pattern, and will be used, among other things, to reduce and prevent seasonal fluctuations in exchange. Then, there is another portion of the loan which is very vague, and which merely promises that the Export-Import bank will cooperate with them, to see that they help them get commercial loans, not indicating whether they will underwrite them or insure them all, or what the amount will be, and Archie said it was purposely that way.

H.M. Jr: On loans not to exceed \$500,000 include me in the picture.

Lochhead: I think the idea was that five million dollars will be the top limit.

H.M. Jr: Incidentally I had a very nice letter from Gaffrey, saying that Dr. Goldenweiser is ill, and that is the reason why everything has been at a standstill.

White: Somebody sent me a book to give to you, which I believe is supposed to be a copy of the Red Book. I don't know the man. I don't know why he sent it to me, but he writes as though he does know me. (Handing a book to the Secretary).

H.M. Jr: Is there anything else, Harry?

White: No. Oh, did you mean that we should call that meeting, or that you were going to take care of it?

Lochhead: How is it, Gene?

White: Gene is taking care of it.

H.M. Jr: Good.

Mrs. Klotz: Gene knows nothing about it, but --

H.M. Jr: He was here yesterday.

Gibbons: It might be interesting to know that Senator Walsh wondered why he had not been in on the Governor Curley tax things; but I didn't know anything about it.

H.M.Jr: Well, I am not familiar with that.

Gibbons: He went on to say then that he had given a lot of money to charity.

H.M.Jr: Who is that?

Gibbons: The Governor. Who is quite interesting.

H.M.Jr: O.K. George?

Haas: I have nothing. The wires went out yesterday.

H.M.Jr: Yes.

Haas: And I talked to Goldenweiser He said one of the men was making an analysis, which is not completed yet.

H.M.Jr: You explained to Miss Lonagan why she has to go to Boston? Have you given her the background?

White: Yes. By the way, Senator Wagner said there was to be a meeting of the sub-committee tomorrow, and he hoped to get a favorable report.

H.M.Jr: Shall I call him?

Foley: We investigated that fellow Flesh that he wants appointed, and the investigator's reports are favorable.

H.M.Jr: Senator Wagner's office, please.

White: He is a little bit disturbed as to how the Treasury is cooperating with him on the Housing loans. I do not know the details.

Foley: He has written a long letter here, or which obviously was written for him, in reply to a draft of the report that we submitted to him in advance, the report was sent off, but you changed the report yesterday.

Bell: We are against that particular section.

Foley: That whole paragraph. We are against the underwriting provisions.

H.M.Jr: How much is this going to cost?

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Foley: A hundred million dollars -- and Flesh.

H.M.Jr: I will not stand for the pound of "Flesh". He is getting too close to the bone.

Gibbons: Incidentally, he said Herbert's appointment is a well deserved appointment. Then he turned and said "What is it going to get me?" I said, "Not a G. D. thing until I have to".

H.M.Jr: But he comes back on "Flesh"?

Gibbons: That was not in my capacity.

H.M.Jr: All right.

Gibbons: He was very complimentary, though.

H.M.Jr: Steve Early was most enthusiastic about it. George, are you all right?

Haas: Yes.

H.M.Jr: Foley, we will bring up those Straus letters at eleven o'clock.

Foley: Yes. Our Comptroller and Cy are going to be here at eleven o'clock.

Duffield: I have not asked them, but I will.

H.M.Jr: Will you, please?

Duffield: Yes.

Foley: I think it would be a good idea if the Comptroller talked to him about it.

H.M.Jr: In studying this thing, you might have use for the background. On this idea of loans to small business, the Federal Reserve will take the angle that they want it to go through them not through the RFC. Do you recall that?

Foley: No. I thought they were objecting to the re-discount provision.

Bell: That is the one hundred million dollar loan.

H.M.Jr: That is what they want to do. They want to take and

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recast that thing, grab it and put it through the Federal Reserve.

White: We might have that in mind.

Foley: Jones is going to testify tomorrow.

H.M.Jr: Eccles will testify on Monday. If you are going to have a lending agency, I think they had better have it all in one place, although I have not seen the order yet.

Foley: Surely.

H.M.Jr: It seems that way to me; but, after all, the Texas delegation is much bigger than the one from Utah or Idaho. We have to be practical.

Is everything all right until eleven o'clock?

Foley: I have a couple of little things.

H.M.Jr: All right. You will get a chance. I will make no outside appointments for this afternoon. Gene?

Duffield: I have nothing. Did you want anything?

H.M.Jr: I wanted to give you a message about going to the Comptroller's office.

Gaston: I have a friend, an Army officer, who is in the office of the Assistant Secretary of War. He brought over two of his associates yesterday. The message they wanted to get over was how thoroughly the Army was prepared in the matter of economic preparedness in case of war. They left a large mimeographed memorandum and book with me.

H.M.Jr: That is this book?

Gaston: Well, they left a revised plan, a 1939 revision of the preparedness plan. I have it on my desk. I also have a book that was written in collaboration with the Army on the same subject. They wanted you to know how well they had the thing worked out.

H.M.Jr: Are they out of Louis Johnson's office?

Gaston: They are out of Louis Johnson's office, and the visit was prompted by a visit to them by a man named

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Harris. They thought you did not fully realize how much they had done.

- H.M. Jr: Neither does the President, and neither does Colonel Watson.
- Gaston: I have another study right on that. I was told the other day by a man named Lewis of the unusual matters that come up, and he was surprised and shocked to see how little they had along this particular line.
- H.M. Jr: I hope it is as good as the plan which was to tie up all of the electric plants using overhead wires. I made the suggestion to Grossbeck that an aeroplane could take a piece of wire and just drop it over any of these high tensions and short-circuit the whole thing. They said they had not thought of that.
- Hanes: Did Johnson tell you --
- H.M. Jr: I saw him when he went down to see the President. We are here eighteen hours a day, off and on -- not always the same day, (laughter) but that was for Louis Johnson.
- Hanes: He said he would call and ask for an appointment.
- H.M. Jr: Good.
- Hanes: He said it was very important.
- Gaston: Mr. Anslinger sent to Mr. Wood some very confidential information, and after Mr. Gibbons sent Mr. Wood to me, I gave them to Harry. I don't know of how much interest they are. I read them only casually.
- H.M. Jr: Is there anything else?
- Gaston: That is all.
- H.M. Jr: Will Mac and Herbert and you, John, stay a minute.
(Conference concluded at 9:55 o'clock A.M.)

JUN 1 1939

Sir:

Reference is made to Mr. Bell's letter of February 27, 1939, requesting an expression of the views of the Treasury Department with respect to S. 591, a bill to amend the United States Housing Act of 1937, and for other purposes, and enclosing a copy of a proposed report by the Administrator of the United States Housing Authority relative to this bill.

Section 1 of the bill would authorize the United States Housing Authority to enter into additional contracts which will provide for annual contributions aggregating not more than \$45,000,000 per annum. Under Section 2 the Authority is authorized to issue and sell its obligations in an amount not to exceed \$800,000,000 in addition to the amount of such obligations heretofore authorized, namely, \$800,000,000. Section 3 would amend Section 2 (10) of the United States Housing Act of 1937 defining the going Federal rate of interest. Section 4 of the Bill would permit national banks and State member banks of the Federal Reserve System to underwrite

*File to Thompson
(given to H.M. G. to be taken
to Bell)*

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by purchase bonds of public housing agencies which are secured by a pledge of payments under annual contributions contracts with the Authority, without regard to the limitations and restrictions provided in section 5136 of the Revised Statutes of 1937, as amended (U.S.C., Supp. IV, title 12, sec. 24).

The Treasury Department is in sympathy with the proposal to extend and broaden the program of the United States Housing Authority. The low-rent housing program not only furnishes safe and sanitary dwelling facilities for the lowest income groups and eliminates the slums in which they now live, but in addition it serves as a much needed stimulus for the construction industry. Accordingly, the Department recommends that S. 591, with the exception of section 4, be enacted.

Section 4 of S. 591 provides that "The last sentence of paragraph seventh of section 5136 of the Revised Statutes, as amended, is amended by inserting before the colon, after the words 'obligations of national mortgage associations', a comma and the following: 'or such obligations of any public housing agency (as defined in section 2 (11) of the United States Housing Act of 1937, as amended) as are secured by a pledge of payments under an annual contributions contract between such agency and the United States Housing Authority'".

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With reference to this section the Administrator of the United States Housing Authority, in his proposed report, states that, "This section would amend the Banking Act so that national banks and (to the extent permitted by state laws) members of the Federal Reserve System will be enabled to underwrite or purchase bonds of public housing agencies which are secured by a pledge of payments under an annual contributions contract with the USHA".

Paragraph Seventh of section 5156 of the Revised Statutes of 1973, as amended (U.S.C., Sup. IV, title 12, sec. 24) provides in general that national banks (the restrictions are also extended to State member banks of the Federal Reserve System by section 2 of the Federal Reserve Act, as amended (U.S.C., title 12, sec. 335)) shall not deal in securities or stocks for their own account or underwrite securities or stock, but permits national banks to purchase for their own account "investment securities", under limitations and restrictions prescribed by the Comptroller of the Currency, provided that a bank shall not hold for its own account the investment securities of any one obligor or maker in excess of 10 per centum of the bank's unimpaired capital stock and 10 per centum of its unimpaired surplus. Paragraph Seventh provides further that the limitations and restrictions contained therein, as to dealing in, underwriting and purchasing of investment securities, shall not apply to certain types of obligations, including "obligations which

are issued by the Federal Housing Administrator pursuant to section 207 of the National Housing Act, if the debentures to be issued in payment of such issued obligations are guaranteed as to principal and interest by the United States*.

If the obligations of public housing agencies are "investment securities" under section 5156 of the Revised Statutes and the regulations of the Comptroller of the Currency issued pursuant thereto, national banks could under existing law purchase for their own account obligations of a local housing agency in an amount up to 10 per centum of the unimpaired capital and undepreciated surplus of the bank. The effect of the amendment to section 5156, proposed by section 4 of S. 501, would be to authorize national banks (and State member banks of the Federal Reserve System, if not prohibited by State law) to underwrite, and to purchase for their own account, obligations of a public housing agency in unlimited amounts, since such obligations would be exempted from the restrictions contained in section 5156.

The Administrator of the United States Housing Authority states that the amendment proposed by section 4 of S. 501 "would place bonds of local housing authorities in the same category as certain obligations issued in connection with private housing construction and insured by the Federal Housing Administration". It may be implied from his statement that obligations of public housing agencies should be exempted from the restrictions in section 5156 because they are of the

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same character as certain obligations insured by the Federal Housing Administration pursuant to section 207 of the National Housing Act, which are, at present, exempted from the restrictions in section 5136. The mortgages insured by the Federal Housing Administration pursuant to section 207 of the National Housing Act, as amended (U.S.C., Sup. IV, title 12, sec. 1715) are mortgages covering residential properties held by public or private agencies, for the purpose of rehabilitation of slum or blighted areas or providing housing for rent or sale, the rents or sales being regulated under housing laws or by the Federal Housing Administrator, and such mortgages may involve a principal obligation as large as \$5,000,000. It is these obligations which are expressly exempted from the limitations and restrictions contained in section 5136 of the Revised Statutes by the language therein covering "obligations which are insured by the Federal Housing Administrator, pursuant to section 207 of the National Housing Act, if the debentures to be issued in payment of such insured obligations are guaranteed as to principal and interest by the United States.". The effect of that exception is to remove obligations insured under section 207 of the National Housing Act from the restrictions contained in section 5136, including the 10 per centum limit on purchases by national banks, and further to remove them from any restrictions contained in regulations issued by the Comptroller of the Currency pursuant to section 5136.

In the opinion of this Department bonds of public housing agencies of

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are not of the same character, in so far as security is concerned, as obligations insured pursuant to section 207 of the National Housing Act. In case of default by the mortgagor under a mortgage insured pursuant to section 207, the mortgagee is entitled to exchange the mortgage for debentures which are fully and unconditionally guaranteed as to principal and interest by the United States. It should be noted that section 5136 of the Revised Statutes excepts obligations insured under section 207 of the National Housing Act, provided that "the debentures to be issued in payment of such insured obligations are guaranteed as to principal and interest by the United States."

(Underacoring supplied) On the other hand, bonds of public housing agencies, which it is proposed, by section 4 of S. 591, to except from the restrictions contained in section 5136 of the Revised Statutes, "are secured by a pledge of payments under an annual contributions contract between such agency and the United States Housing Authority".

It would seem clear that a pledge of payments under an annual contributions contract, made pursuant to section 601 of the United States Housing Act of 1937, as amended (U.S.C., Sup. IV, title 42, sec. 1410), would not be security equal in value to debentures "guaranteed as to principal and interest by the United States". The bonds of public housing agencies are not obligations of the United States, nor are they guaranteed as to the payment of principal or interest by the United States. Section 13 of the United States Housing Act of 1937,

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as amended (U.S.C., Sup. IV, title 42, sec. 1410) provides that the United States Housing Authority may make annual contributions to public housing agencies to assist in achieving and maintaining the low-rent character of their housing projects and the faith of the United States is pledged to the payment of all annual contributions contracted to be made by the Authority. Section 10 provides, further, that payments under annual contributions contracts shall be pledged as security for any loans obtained by public housing agencies to assist in the development of the housing projects to which the annual contributions relate, provided that annual contributions shall first be used to apply toward the payment of interest or principal as the same matures on any loan due to the Authority from the public housing agencies. Thus, under existing law annual contributions estimated and paid by the Authority are pledged toward the payment of public housing agencies' bonds, after matured principal and interest on loans owing to the Authority have been paid. This constitutes the basic security for the payment of such bonds, and it is understood that under the form of contract which the Authority contemplates entering into with public housing agencies it is intended that the annual contributions will be calculated in such a manner as to be sufficient to amortize the principal and interest on the public housing agencies' bonds.

Section 10 of the United States Housing Act of 1937, as amended,

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In addition to authorizing the Authority to determine the amount of the annual contributions payable to each public housing agency to assist in achieving and maintaining the low-rent character of the projects, gives the Authority very broad powers to modify a contract covering annual contributions and to reduce the amount of or terminate such contributions. That section provides that where a contract for annual contributions is made for a period exceeding 20 years, the Authority shall reserve the right to reexamine the status of the housing project involved at the end of 10 years and every 5 years thereafter. If the Authority is of the opinion that changed conditions so warrant it may modify the amount of subsequent annual contributions payable to assist in maintaining the low-rent character of the project.

Section 15(3) of the United States Housing Act of 1937, as amended (U.S.C., Sup. IV, title 42, sec. 1415(3)) provides that the Authority shall retain the right, in the event of a substantial breach of the conditions contained in a contract with a public housing agency providing for the maintenance of the low-rent character of the housing project involved, to reduce or terminate the annual contributions payable under such contracts. Also, in the event of the acquisition of such project by a third party the annual contributions shall terminate.

Accordingly, under existing law the basic security for the bonds

- 2 -

of public housing agencies is the annual contributions payable by the Authority to such agencies, which contributions are for the purpose of maintaining the low-rent character of the projects. Under the law the Authority has the power to change a contract providing for annual contributions and to reduce or terminate entirely such annual contributions. Thus, the basic security for these public housing agencies' bonds could be drastically altered.

It is understood that the Authority has prepared a proposed form of contract covering annual contributions under which it is contended that any doubt as to the validity or continuance of the annual contributions as security for the public housing agency bonds is almost entirely eliminated. This suggested contract is a very involved document, which it does not appear necessary to discuss in detail at this time. The contract raises a number of legal questions which it is understood are being referred by the Authority to the Attorney General for an opinion.

Even assuming that the Attorney General should hold that the proposed form of contract is legal, and assuming further that such a contract would assure that the annual contributions payable to a public housing agency would be sufficient to amortize the bonds of such agency and that such annual contributions would not be reduced or terminated until such bonds have been retired, it is possible that in the future the form of contract could be changed by the Authority

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in such a manner as to lessen the value of the annual contributions as security for a new bond issue. Such a new bond issue might be of a different character than a previous issue, in so far as the nature of the security for the bonds was concerned.

As already pointed out above, if section 5136 were amended as proposed in S. 591, not only would national banks be authorized to purchase for their own account obligations of public housing agencies without limit, but they could also be authorized to underwrite such obligations in unlimited amounts. It should be remembered that, in enacting the Banking Act of 1933, it was clearly the intention of Congress to divorce the commercial banking business from "the business of issuing, underwriting, selling, or distributing, at wholesale or retail, or through syndicate participation, stocks, bonds, debentures, notes, or other securities". (Section 21 of the Banking Act of 1933, as amended (U.S.C., Sup. IV, title 12, sec. 378)) In its report, the Senate Committee on Banking and Currency stated:

"National banks were never intended to undertake investment banking business on a large scale, and the whole tenor of legislation and administrative rulings concerning them has been away from recognition of such a growth in the direction of investment banking as legitimate. Nevertheless it has continued; and a very fruitful cause of bank failures, especially within the past three years, has been the fact that the funds of various institutions have been so extensively 'tied up' in long-term investments." (Senate Report No. 77, 73rd Cong. 1st Sess., p. 8)

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If the bonds of public housing agencies were exempted from the prohibition against underwriting contained in section 5136, the result might be the formation of a syndicate, including a number of national banks, for the purpose of underwriting these bonds. It is believed that it would not constitute a desirable tendency for national banks to participate in such an underwriting arrangement.

In view of all the facts, it is the opinion of the Treasury Department that it would be unwise to increase the existing exceptions to section 5136 of the Revised Statutes, by exempting from the restrictions and limitations contained therein the obligations of public housing agencies. Accordingly, this Department is of the opinion that section 4 should not be enacted.

The Treasury recommends that S. 591, with the exception of section 4, be enacted.

Very truly yours,

(Signed) H. Morgenthau, Jr.

Secretary of the Treasury.

The Director

Bureau of the Budget.

DJS:es typed 5.31.39

JUN 1 1939

Sir:

There are enclosed herewith for your consideration an original and one copy of a proposed letter to the Chairman of the House Committee on Banking and Currency, reporting on H. R. 2838, "To amend the United States Housing Act of 1937, and for other purposes".

It is requested that you advise whether the proposed legislation is in accordance with the program of the President.

By direction of the Secretary:

Very truly yours,

~~W. E. [unclear]~~
Administrative Assistant
to the Secretary.

The Director

Bureau of the Budget.

Enclosures.

DJS:ec typed 5.29.39

File to Thompson

*(Letter given to H. M. G. to be
Taken to D. W. Bell)*

JUN 1st 1939

My dear Mr. Chairman:

The attention of the Treasury Department has been called to H. R. 2886, A Bill "To amend the United States Housing Act of 1937, and for other purposes", which has been referred to your Committee. A similar bill, S. 591, was introduced in the Senate, and on May 22 the Senate Committee on Education and Labor reported S. 591 favorably with amendments (Report No. 463).

Section 1 of H. R. 2886 would authorize the United States Housing Authority to enter into additional contracts which will provide for annual contributions aggregating not more than \$45,000,000 per annum. Under Section 2 the Authority is authorized to issue and sell its obligations in an amount not to exceed \$800,000,000 in addition to the amount of such obligations heretofore authorized, namely, \$600,000,000. Section 3 would amend Section 2(10) of the United States Housing Act of 1937 defining the going Federal rate of interest. Section 4 of the Bill would permit national banks and State member banks

- 2 -

of the Federal Reserve System to underwrite or purchase bonds of public housing agencies which are secured by a pledge of payments under annual contributions contracts with the Authority, without regard to the limitations and restrictions provided in section 5136 of the Revised Statutes of 1873, as amended (U.S.C., Supp. IV, title 12, sec. 24).

The Treasury Department is in sympathy with the proposal to extend and broaden the program of the United States Housing Authority. The low-rent housing program not only furnishes safe and sanitary dwelling facilities for the lowest income groups and eliminates the slums in which they now live, but in addition it serves as a much needed stimulus for the construction industry. Accordingly, the Department recommends that H. R. 2886, with the exception of section 4, be enacted.

Section 4 of H. R. 2886 provides that "The last sentence of paragraph Seventh of section 5136 of the Revised Statutes, as amended, is amended by inserting before the colon, after the words 'obligations of national mortgage associations', a comma and the following: 'or such obligations of any public housing agency (as defined in section 2(11) of the United States Housing Act of 1937, as amended) as are secured by a pledge of payments under an annual contributions contract between such agency and the United States Housing Authority'".

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Paragraph Seventh of section 5136 of the Revised Statutes of 1873, as amended (U.S.C., Sup. IV, title 12, sec. 24) provides in general that national banks (the restrictions are also extended to State member banks of the Federal Reserve System by section 9 of the Federal Reserve Act, as amended (U.S.C., title 12, sec. 335)) shall not deal in securities or stocks for their own account or underwrite securities or stock, but permits national banks to purchase for their own account "investment securities", under limitations and restrictions prescribed by the Comptroller of the Currency, provided that a bank shall not hold for its own account the investment securities of any one obligor or maker in excess of 10 per centum of the bank's unimpaired capital stock and 10 per centum of its unimpaired surplus. Paragraph Seventh provides further that the limitations and restrictions contained therein, as to dealing in, underwriting and purchasing of investment securities, shall not apply to certain types of obligations, including "obligations which are insured by the Federal Housing Administrator pursuant to section 207 of the National Housing Act, if the debentures to be issued in payment of such insured obligations are guaranteed as to principal and interest by the United States".

If the obligations of public housing agencies are "investment securities" under section 5136 of the Revised Statutes and the regulations of the Comptroller of the Currency issued pursuant thereto, na-

- 4 -

tical banks could under existing law purchase for their own account obligations of a local housing agency in an amount up to 10 per centum of the unimpaired capital and unimpaired surplus of the bank. The effect of the amendment to section 5136, proposed by section 4 of H. R. 2886, would be to authorize national banks (and State member banks of the Federal Reserve System, if not prohibited by State law) to underwrite, and to purchase for their own account, obligations of a public housing agency in unlimited amounts, since such obligations would be exempted from the restrictions contained in section 5136.

It may be contended that obligations of public housing agencies should be exempted from the restrictions in section 5136 because they are of the same character as certain obligations insured by the Federal Housing Administration pursuant to section 207 of the National Housing Act, which are, at present, exempted from the restrictions in section 5136. The mortgages insured by the Federal Housing Administration pursuant to section 207 of the National Housing Act, as amended (U.S.C., Supp. IV, title 12, sec. 1715) are mortgages covering residential properties held by public or private agencies, for the purpose of rehabilitation of slum or blighted areas or providing housing for rent or sale, the rents or sales being regulated under housing laws or by the Federal Housing Administrator, and such mortgages may involve a principal obligation as large as \$5,000,000. It is these obligations which are expressly exempted from the limitations and restrictions con-

- 5 -

defined in section 5136 of the Revised Statutes by the language therein covering "obligations which are insured by the Federal Housing Administrator, pursuant to section 207 of the National Housing Act, if the debentures to be issued in payment of such insured obligations are guaranteed as to principal and interest by the United States.". The effect of that exception is to remove obligations insured under section 207 of the National Housing Act from the restrictions contained in section 5136, including the 10 per centum limit on purchases by national banks, and further to remove them from any restrictions contained in regulations issued by the Comptroller of the Currency pursuant to section 5136.

In the opinion of this Department bonds of public housing agencies are not of the same character, in so far as security is concerned, as obligations insured pursuant to section 207 of the National Housing Act. In case of default by the mortgagor under a mortgage insured pursuant to section 207, the mortgagee is entitled to exchange the mortgage for debentures which are fully and unconditionally guaranteed as to principal and interest by the United States. It should be noted that section 5136 of the Revised Statutes excepts obligations insured under section 207 of the National Housing Act, provided that "the debentures to be issued in payment of such insured obligations are guaranteed as to principal and interest by the United States." (Underlining supplied) On the other hand, bonds of public housing agencies, which it

- 6 -

is proposed, by section 4 of H. R. 2680, to exempt from the restrictions contained in section 5136 of the Revised Statutes, "are secured by a pledge of payments under an annual contributions contract between such agency and the United States Housing Authority".

It would seem clear that a pledge of payments under an annual contributions contract, made pursuant to section 610 of the United States Housing Act of 1937, as amended (U.S.C., Sup. IV, title 42, sec. 1410), would not be security equal in value to debentures "guaranteed as to principal and interest by the United States". The bonds of public housing agencies are not obligations of the United States, nor are they guaranteed as to the payment of principal or interest by the United States. Section 10 of the United States Housing Act of 1937, as amended (U.S.C., Sup. IV, title 42, sec. 1410) provides that the United States Housing Authority may make annual contributions to public housing agencies to assist in achieving and maintaining the low-rent character of their housing projects and the faith of the United States is pledged to the payment of all annual contributions contracted to be made by the Authority. Section 10 provides, further, that payments under annual contributions contracts shall be pledged as security for any loans obtained by public housing agencies to assist in the development of the housing projects to which the annual contributions relate, provided that annual contributions shall first be used to apply toward the payment of interest or principal as the same matures on any loan due to

the Authority from the public housing agencies. Thus, under existing law annual contributions estimated and paid by the Authority are pledged toward the payment of public housing agencies' bonds, after matured principal and interest on loans owing to the Authority have been paid. This constitutes the basic security for the payment of such bonds, and it is understood that under the form of contract which the Authority contemplates entering into with public housing agencies it is intended that the annual contributions will be allocated in such a manner as to be sufficient to amortize the principal and interest on the public housing agencies' bonds.

Section 10 of the United States Housing Act of 1937, as amended, in addition to authorizing the Authority to determine the amount of the annual contributions payable to each public housing agency to assist in achieving and maintaining the low-cost character of the projects, gives the Authority very broad powers to modify a contract covering annual contributions and to reduce the amount of or terminate such contributions. That section provides that where a contract for annual contributions is made for a period exceeding 20 years, the Authority shall reserve the right to reexamine the status of the housing project involved at the end of 10 years and every 5 years thereafter. If the Authority is of the opinion that changed conditions warrant it may modify the amount of subsequent annual contributions payable to assist in maintaining the low-cost character of the projects

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Section 15(3) of the United States Housing Act of 1937, as amended (U.S.C., Sup. IV, title 42, sec. 1415(3)) provides that the Authority shall retain the right, in the event of a substantial breach of the conditions contained in a contract with a public housing agency providing for the maintenance of the low-rent character of the housing project involved, to reduce or terminate the annual contributions payable under such contracts. Also, in the event of the acquisition of such project by a third party the annual contributions shall terminate.

The uncertain character of the annual contributions as security for, or a source of funds for the amortization of the principal and interest of, bonds of public housing agencies is indicated by the following language in the report of the Senate Committee on Education and Labor relative to S. 591 (Report No. 463):

"The annual contributions are intended to bridge the gap between the economic rent which is the rent which would otherwise have to be charged for this decent new housing (in order to meet debt service, maintenance, and operating expenses) and the social rent, which is the rent that families now living in the slums can now afford to pay.

"Under the terms of the present act, the annual contributions contracts, whenever made for a period exceeding 20 years, will be reviewed at least at the end of 10 years and every fifth year thereafter, in accordance with the statutory provisions that they be modified as warranted by changed economic conditions. The contributions, through such modifications, can never be raised above the maximum rate at which

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annual contributions may be contracted under the act. Although debt-service requirements (because necessarily fixed at the very outset for the life of the project) present a condition that will not change, other conditions will change, such as price or wage levels. Every analysis of normal rent and income trends in the past, and every reasonable estimate of probable trends in the future, reinforces the conviction that the annual contributions necessary to achieve rents within reach of 'low-income families,' and to insure the financial stability of housing projects, will gradually decline. For this reason it must not be presumed that the annual contributions to be contracted for will last for 60 years." (pp 3-4) (Underlining supplied)

Thus, under existing law the basic security for the bonds of public housing agencies is the annual contributions payable by the Authority to such agencies, which contributions are for the purpose of maintaining the low-rent character of the projects. Under the law the Authority has the power to change a contract providing for annual contributions and to reduce or terminate entirely such annual contributions. Thus, the basic security for these public housing agencies' bonds could be drastically altered.

As already pointed out above, if section 5136 were amended as proposed in H. R. 2688, not only would national banks be authorized to purchase for their own account obligations of public housing agencies without limit, but they would also be authorized to underwrite such obligations in unlimited amounts. It should be remembered that, in enacting the Banking Act of 1933, it was clearly the intention

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of Congress: to divorce the commercial banking business from "the business of issuing, underwriting, selling, or distributing, at wholesale or retail, or through syndicate participation, stocks, bonds, debentures, notes, or other securities". (Section 21 of the Banking Act of 1933, as amended (U.S.C., Supp. IV, title 12, sec. 370)) In its report on the Banking Act of 1933, the Senate Committee on Banking and Currency stated:

"* * * National banks were never intended to undertake investment banking business on a large scale, and the whole tenor of legislation and administrative rulings concerning them has been away from recognition of such a growth in the direction of investment banking as legitimate. Nevertheless it has continued, and a very fruitful cause of bank failures, especially within the past three years, has been the fact that the funds of various institutions have been so extensively 'tied up' in long-term investments." (Senate Report No. 77, 73rd Cong. 1st Sess., p. 8)

If the bonds of public housing agencies were exempted from the prohibition against underwriting contained in section 5136, the result might be the formation of a syndicate, including a number of national banks, for the purpose of underwriting these bonds. It is believed that it would not constitute a desirable tendency for national banks to participate in such an underwriting arrangement.

In view of all the facts, it is the opinion of the Treasury Department that it would be unwise to increase the existing exceptions to section 5136 of the Revised Statutes, by exempting from the restrictions

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and limitations contained therein the obligations of public housing agencies. Accordingly, this Department is of the opinion that section 4 should not be enacted.

The Treasury recommends that H. R. 2686, with the exception of section 4, be enacted.

Very truly yours,

(Signed) H. Morgenthau, Jr.

Secretary of the Treasury.

Hon. Henry E. Steagall,
Chairman, Committee on Banking
and Currency,
House of Representatives.

DJS:es typed 5.27.39
retyped 5.31.39

JUN 1st 1939

My dear Mr. Chairman:

Further reference is made to your letter of April 19, 1939, requesting the Treasury Department's opinion as to the merits of S. 2150, A Bill "To amend section 8 of the Act entitled 'An Act to supplement laws against unlawful restraints and monopolies, and for other purposes', particularly with reference to interlocking bank directorates, known as the Clayton Act".

The Treasury Department is not in possession of information establishing that there is any necessity for amending section 8 of the Clayton Act, as amended (U.S.C., Sup. IV, title 15, sec. 19), in order to postpone the effective date of that section, from February 1, 1939 to February 1, 1944, in so far as the prohibition contained therein relates to any director, officer, or employee of any member bank who was serving as a private banker or as a director, officer, or employee of any other bank on the date of enactment of the Banking Act of 1935. In the absence of such a showing of necessity it is the opinion of

15 Room 174

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the Treasury Department that S. 2180 should not be enacted.

The Department has been advised by the Bureau of the Budget that there is no objection to the submission of this report to your Committee.

Very truly yours,

(Signed) H. Morgenthau, Jr.

~~Secretary~~ Secretary of the Treasury.

Hon. Robert F. Wagner,
Chairman, Committee on Banking
and Currency,
United States Senate.

DJS:es typed 5.5.59

C O P Y

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UNITED STATES SENATE

Committee on Banking and Currency

April 19, 1939

BY MESSENGER

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

My dear Mr. Secretary:

I am enclosing a copy of S. 2150 which has recently been referred to the Committee on Banking and Currency.

The Committee would appreciate an early opinion as to the merits of this proposed legislation. Kindly send your reply in triplicate.

Very sincerely yours,

(Signed) Robert F. Wagner

Chairman.

Encl.

TREASURY DEPARTMENT

WASHINGTON, D. C.

OFFICE OF THE CHIEF
U. S. SECRET SERVICE

June 1, 1939

MEMORANDUM FOR THE SECRETARY,
FROM CHIEF, SECRET SERVICE.

Major Warner, of the New York State Police, telephoned me this morning stating that he would not be able to comply with the request I made yesterday for a permanent detail of State Troopers at Hyde Park. He expressed his regret, explaining at length the increasing demand for troopers and stated that because of the press of work he has had to eliminate all special details. He said he felt that it was advisable to have a permanent detail at the estate and that probably a detail would be furnished by the Government.

After receiving the above information from Major Warner, I informed Mrs. Klotz regarding same, advised her that I could arrange to choose three fine men from the Uniformed Treasury Department Guard Force to handle the assignment, and requested her to arrange a conference with you to discuss the proposal. Mrs. Klotz stated that it would be sometime this afternoon before I could see you.

About half an hour later, Agent Qualters called at my office, stating that this morning the President had again discussed the matter of the permanent detail with him and informed him that it

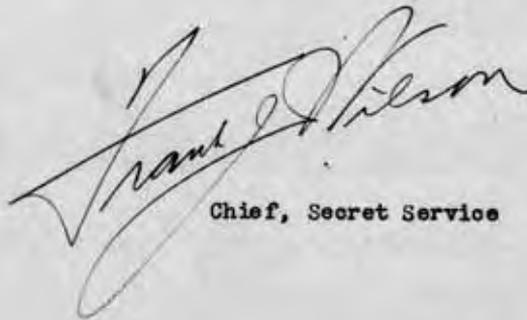
- 2 -

was likely that Major Warner would not approve the request for the detail. The President requested Agent Qualters to discuss with me the advisability of having three guards from the Interior Department, who protect public buildings, detailed to Hyde Park. I informed Agent Qualters that if guards were to be furnished I felt it would be much better to select three men from the Uniformed Force of the Secret Service for the detail as we could select three outstanding men who we know are reliable and would have complete control over them instead of a divided responsibility; also that we could appoint them as Special Employees on the Secret Service Emergency Relief Roll at \$1800 per year, establishing their post of duty at Hyde Park to eliminate subsistence and furnishing them with an automobile to provide for their transportation. As you were occupied with a conference this morning, I suggested to Qualters that he again discuss the situation with the President and inform him that if it was agreeable to him we would prefer to use our own guards. Agent Qualters has just returned from the White House and states that the President expressed his approval of the proposal to use the Treasury Department Guards directed by the Secret Service. The President did not deem it advisable to make any further effort to obtain a detail of State Troopers.

I will take special care in selecting men from the Uniformed Force of the Secret Service for this assignment. We will have a Secret Service agent detailed at Hyde Park for a few days to school them. During the times the White House Secret Service Detail is on duty at Hyde Park they

will function under the direction of Supervising Agent Starling and eliminate the necessity of sending the three Secret Service Agents from New York City who are frequently called upon to supplement the White House Detail at Hyde Park. During the periods the President is not at Hyde Park they will function under the direction of Supervising Agent Maloney of New York City who will receive daily reports from them and who will have an agent from New York City make unannounced inspections of the men at Hyde Park at irregular intervals, some of the inspections to be during the night and others during daylight.

I am making arrangements to have the detail report at Hyde Park in uniform and begin the assignment by 6 p.m. on June 2nd. If you desire to discuss this subject or have any suggestions with reference to same please advise me.

A handwritten signature in cursive script, reading "Frank J. Wilson". The signature is written in dark ink and is positioned above the typed name of the Chief of the Secret Service.

Chief, Secret Service

June 1, 1939

MEMORANDUM FOR THE SECRETARY,
FROM CHIEF, SECRET SERVICE.

Major Warner, of the New York State Police, telephoned me this morning stating that he would not be able to comply with the request I made yesterday for a permanent detail of State Troopers at Hyde Park. He expressed his regret, explaining at length the increasing demand for troopers and stated that because of the press of work he has had to eliminate all special details. He said he felt that it was advisable to have a permanent detail at the estate and that probably a detail would be furnished by the Government.

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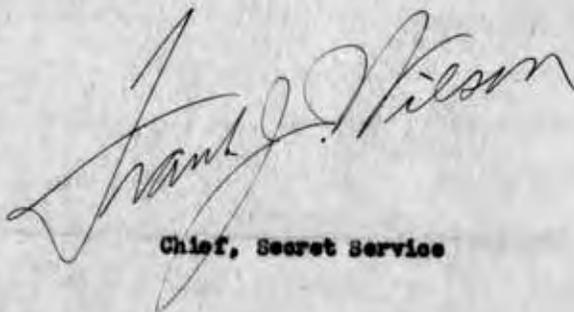
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A handwritten signature in cursive script, reading "Frank J. Wilson". The signature is written in dark ink and is positioned above the typed name.

Chief, Secret Service

June 1, 1939

Dear Ros:

I thought you would be interested in reading the inclosed copy of a letter from Mr. Robert E. Mathews and copy of my answer to the same.

I don't know whether this is something that you want or not, but if it is, here's wishing you good luck!

Yours sincerely,

Mr. Roswell Magill,
36 Claremont Avenue,
New York, N. Y.

June 1, 1939

Dear Ros:

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Mr. Roswell Magill,
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June 1, 1939

46

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I don't know whether this is something that you want or not, but if it is, here's wishing you good luck

Yours sincerely,

Mr. Roswell Magill,
25 Claremont Avenue,
New York, N. Y.

June 1, 1939

47

My dear Mr. Mathews:

In reply to your letter of May 26 I am delighted to tell you what I know about Mr. Roswell Magill.

While Mr. Magill was Under-Secretary of the Treasury, he rendered his Government unusual and distinguished service. He had the rare faculty of getting along extremely well with the Members of Congress and they were kind enough to say that he was the best representative that the Treasury had ever sent on the Hill to look after tax legislation.

I should think that Mr. Magill would make an excellent President of Ohio State University and I cheerfully recommend him for this place or any other position that he may be called upon to fill.

Yours sincerely,

Mr. Robert E. Mathews,
Ohio State University,
Columbus, Ohio.

June 1, 1939

48

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In reply to your letter of May 28 I am delighted to tell you what I know about Mr. Roswell Magill.

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Yours sincerely,

Mr. Robert E. Mathews,
Ohio State University,
Columbus, Ohio.

THE OHIO STATE UNIVERSITY

GEORGE W. RICHMOND, President

COLUMBUS

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COLLEGE OF LAW

May 26, 1939

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

Dear Mr. Morgenthau:

Some time ago the Board of Trustees of this institution asked a small committee of faculty members to suggest names of persons suitable for the presidency of this University. Among those under consideration is Mr. Roswell F. Magill.

While Mr. Magill is intimately known to me as a class-mate and long time friend in Chicago back in the "twenties", I am anxious to procure comments from others upon his qualifications. His association with you in recent years, has led me to take the liberty of inquiring whether you would feel free to add your own observations to those which we have already gathered. In case you find it possible to do this, I can assure you of our great appreciation. I might add that your remarks would be kept in confidence among the members of the committee and the Board of Trustees.

Very sincerely yours,


Robert E. Mathews

REM:RE

June 1, 1939
9:28 a.m.

HMJr: Hello. Hello.
P. W.
Parker: Hello.
HMJr: Is this Parker?
P: Good morning, Mr. Secretary.
HMJr: How are you?
P: Fine, thanks.
HMJr: I asked General Craig to check up on this General that you suggested, but he hasn't heard from him yet.
P: I see.
HMJr: And he also has his doubts about him. He knows him personally.
P: He does, eh?
HMJr: Yeah.
P: He -- well, of course, that's often the case; I don't know. But I got, in the meantime, Mr. Morgenthau -- we've gotten in touch with this chap, Jack Keeshin.
HMJr: Yes.
P: Who is the head of the Keeshin Transport Company of Chicago.
HMJr: Yeah.
P: And he has told Mr. J. A. Brown that he would very highly recommend a Mr. Thomas Wilson.
HMJr: Yes.
P: Wilson has -- has been Chairman of the Board of the Transcontinental Western Airways Express. That's an aviation company.
HMJr: Yes.
P: And he says he's a man about 45 years of age and he's had many years experience in the -- trucking experience, in both organization and operation.

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HMJr: Yeah.

P: And Keeshin says that he's prepared to select a few men from his own organization if they are desired, to form a skeleton crew to go along with Wilson, and he -- he very highly recommends him. And we think that probably -- probably this chap Keeshin is the best qualified man to -- to pick out such a man as anyone that we know of in the country. Now I haven't -- we haven't talked with Mr. Wilson, but if you are interested, we can -- we understand that he is to be in New York, I believe, sometime today.

HMJr: Fine!

P: We can locate him through -- through Mr. Keeshin by telephoning Chicago.

HMJr: Fine!

P: So what would you suggest -- shall we.....

HMJr: Well, what I suggest is, that if Wilson is interested, tell him to come on down and see me.

P: Yeah.

HMJr: Is he with T.W.A. now?

P: No, he's just -- my understanding is that he -- he has -- he's resigned from that board just recently, a few months ago; something of that sort.

HMJr: Uh-huh. Well, if he's at all interested, let him come on down tomorrow morning and I -- I'll say tentatively that -- let me see how I'm fixed -- I could see him at ten o'clock tomorrow.

P: Ten o'clock tomorrow morning.

HMJr: Eastern -- we're on eastern standard time here.

P: Yeah.

HMJr: His name is Tom Wilson?

P: Tom Wilson, that's right.

HMJr: And he was with T.W.A.?

P: That's right.

HMJr: Uh-huh.

P: That's right.

HMJr: Well, if he's interested, I'd be delighted to see him.

P: Well, all right, sir, suppose we -- unless you hear from me to the contrary through the -- during the day, I think we can locate him.

HMJr: But.....

P: We -- we'll consider that -- that he'll keep that appointment.

HMJr: Now Keeshin is -- how do you spell Keeshin?

P: K-E-E-S-H-I-N.

HMJr: S-H-I-N -- right. Well then, if I don't hear from you.....

P: He'll be there at ten o'clock.

HMJr: Yes. And if I should decide -- I may want to ask Mr. Keeshin to come down here next week.

P: I see.

HMJr: I could -- I could arrange that through you also.

P: Yes. Yes, we'd be very glad to do that.

HMJr: Fine!

P: All right. In the -- in the meantime, Mr. Morgenthau, why I've -- I've interviewed several other people. I don't think it's necessary to take your -- to take your time on the telephone, and if you so desire I might send -- I might send down letters. I've had them write in letters giving their qualifications.

HMJr: Well, if you would do that, I'd appreciate it.

P: All right, I'll do that.

HMJr: Thank you.

P: But I think that -- I think that probably this -- the Keeshin organization is probably our best bet. That's our feeling.

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HMJr: Well, if -- if you'll send one down, and send this man down, I'd appreciate it very much.

P: All right, sir.

HMJr: Thank you.

P: You bet. Good bye.

June 1, 1939
10:10 a.m.

HMJr: Hello.

Operator: Mr. Campbell.
Bill
Campbell: Hello.

HMJr: Hello, Campbell.

C: Good morning, Mr. Secretary. How are you?

HMJr: Fine.

C: That's good.

HMJr: Campbell, I want to check up on somebody in Chicago.

C: All right.

HMJr: A Mr. Keeshin of the trucking company.

C: Who?

HMJr: Keeshin.

C: How do you spell it?

HMJr: K-E-E-S-H-I-N.

C: Oh, yes. Yes, the trucking people.

HMJr: I tell you why I'm asking. I've been trying to get for the Chinese Government some transportation experts to send over.

C: Yeah.

HMJr: And I've been referred to Mr. Keeshin as the -- as the best man in the United States.

C: As the transportation expert.

HMJr: Yeah. Now, before I took his advice.....

C: Yeah.

HMJr:I wanted to know how he stood in Chicago and whether he was a man of high reputation.

- 2 -

- C: Well, his general reputation I can tell you offhand is very good.
- HMJr: It is?
- C: Yes. As to his knowledge of the transportation business or his ability as a transportation expert, I can't say, but I will find out for you within the next hour or two and call you right back.
- HMJr: Well, I -- I've got that end of it. That I know. I know he knows transportation.
- C: Yes, well, I don't have any knowledge on that, but his general reputation in the community is good.
- HMJr: But I wanted -- for instance, if you had a thing as important as making a recommendation to another government, could -- could you place yourself in Mr. Keeshin's hands -- that's what I want to know.
- C: Yeah. Well, offhand I would say, "Yes", and I would like to just run over the thing with one or two people who I know will be in a position to give me very accurate information on the point and maybe to verify my own opinion and then call you back.
- HMJr: Will you do that, and you can reverse the charges.
- C: Oh, that's perfectly all right. I'll be glad to call you. Will you be there this morning.
- HMJr: Yes. What I want is, I mean, can I just say, "All right, Mr. Keeshin, you take charge and organize this expedition." You see?
- C: I understand.
- HMJr: I mean, -- is he the kind of man that you can do that with.
- C: I'll find that out definitely for you and call you back.
- HMJr: Thank you, so much.
- C: You're welcome, Mr. Morgenthau.
- HMJr: All right.

June 1, 1939
10:13 a.m.

HMJr: Hello.

General
Craig: Good morning, Mr. Secretary.

HMJr: Hello, General.

C: Yes, sir.

HMJr: They said that you called me, I believe.

C: Well, I wanted to call you to tell you that I had gotten that answer from Disque.....

HMJr: Yes.

C:and he had given his address, both day-time and night, and his telephone number, but I wanted to tell you that in looking up I don't find that he's had any experience along that line. He's probably a pretty good business man.

HMJr: Yeah. Well, I saw your Aide.

C: Yes, sir.

HMJr: And I got your letter, and I told him I thought we'd forget about him, and.....

C: Very good, sir.

HMJr: I'm now working with the Keeshin Transportation Company out of Chicago.

C: Yes, sir.

HMJr: And he's willing to organize a group of his own people to go over there.

C: Well, there's some strength in that, Mr. Secretary.

HMJr: And he's been recommended very, very highly.

C: Yes, sir.

HMJr: Do you know of him?

C: No, sir.

HMJr: Well, I think they're the biggest commercial transportation trucking company in America.

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C: Yes, sir.

HMJr: And so I think I'm -- I think it's -- well, they're sending people here tomorrow.

C: Well, there was somebody, I don't know whether it was for or not, had seen Disque last Friday.....

HMJr: Well, that would undoubtedly be it.

C:on this same subject.

HMJr: That's right.

C: So we'll just sit tight and do nothing more about it until you tell me.

HMJr: That's right.

C: I thank you, sir.

HMJr: Thank you.

C: Good bye.

June 1, 1939
12:07 p.m.

HMJr: Hello.

Operator: Senator Pepper.

HMJr: Hello.

O: Go ahead.

Senator
Pepper: Hello.

HMJr: Morgenthau talking.

P: Yes, yes. Hello, Mr. Secretary. How are you?

HMJr: Fine.

P: I wanted to tell you that if you haven't received it already, you will get, probably today, a letter from Adams who is writing you about our St. Augustine restoration coin bill.

HMJr: Oh, yes.

P: Now, he's -- in a way, he looks to me like he's trying to put you on the spot.

HMJr: Uh-huh.

P: And he intimated something to me this morning that he's -- had written you to the effect that he wanted you to be advised that you were the fellow who was letting down the bars to the coin bills that -- that might come rushing through, and I pointed out to him that this -- that your discretion had been exercised purely and distinctly upon the basis of distinctions that existed in this situation from those that existed in other situations.

HMJr: That's right.

P: That coin bills had passed in the -- in the past, but there were reasons why they passed and why some of them were not recommended.

HMJr: Is that.....

P: That you sometimes recommended one bill and sometimes you didn't recommend a bill that might be referred to your Department.

HMJr: Is this Alva Adams?

P: Yes, this is Alva Adams.

HMJr: Oh, I'd love to get a letter from him.

P: Well now, that's the reason -- I just wanted to put you on notice that -- that he's written you such a letter.

HMJr: All right.

P: And he's awaiting your reply before he takes it up with his sub-committee.

HMJr: He'll get it.

P: Yeah, I know. (Laughter)

HMJr: I -- I spoke to Director of the Budget, Smith, myself and got it through there.

P: Well, that was fine. A million thanks to you, and I was pushing Adams, to, "Let's get going on it." Wagner said he was trying to help us, but Adams is Chairman of that sub-committee.

HMJr: Right!

P: And so naturally we wanted -- didn't want this session to get too far advanced without getting it along.

HMJr: Well, I'll give him a prompt answer.

P: Well, fine. I just wanted you to know about that.

HMJr: Thank you.

P: Thank you a lot.

June 1, 1939
12:09 p.m.

HMJr: Hello.

Operator: Senator Wagner.

HMJr: Hello.

Robert

Wagner: Hello, Henry.

HMJr: How are you?

W: Oh, pretty good. How are you?

HMJr: Oh, I'm fine.

W: Good! Well, you're always fine. You're a young, snappy youngster.

HMJr: (Laughter)

W: You called me up, Henry.

HMJr: Yes, I wanted to know if you and that other youngster, Carter Glass, are going to get my bill out.

W: Well, they're meeting tomorrow afternoon at two-thirty. I finally.....

HMJr: Uh-huh.

W:got the old man to come up. I guess he's -- he's a pretty sick man.

HMJr: Uh-huh.

W: There's no doubt about that.

HMJr: But you're going to -- you're going to take a vote tomorrow.

W: On the -- that is, on the sub-committee, you see.

HMJr: Yes, that's what I mean.

W: We've got to get it out of there, and then I'll have a meeting next week on the bill.

HMJr: But you will have a vote of the sub-committee tomorrow?

W: Tomorrow - yes.

HMJr: Swell!

W: Yeah.

HMJr: Swell!

W: Yeah.

HMJr: Now -- well, I guess that's all that I wanted.

W: Say, did -- I didn't speak to Miller myself. Did he say he'd vote -- or what?

HMJr: I don't know what he told the President.

W: I see.

HMJr: I had a very nice talk with the Senator from Michigan.

W: Yeah.

HMJr: And he said he'd be away all this week, and he'd hoped you'd do it this week.

W: Yeah. Well -- yeah.

HMJr: But what the President did with Miller, I don't know.

W: I talked to Radcliffe; he had been against it, and I think he's sort of weakening a little bit.....

HMJr: Uh-huh.

W:in his -- well, all right, Henry.

HMJr: Well, I.....

W: I've had my troubles with the -- my young friend, you know, but you've got to be -- you've got to be very careful in handling him, you know.

HMJr: Righto!

W: He's old and he'd get a good deal of sympathy if.....

HMJr: I know.

W: All right.

HMJr: Thank you.

W: All right, Henry. Good bye.

June 1, 1939
12:12 p.m.

HMJr: Hello.
Jesse
Jones: Hello.

HMJr: Hello, Jesse.

J: Reporting for duty.

HMJr: Atta boy!

J: How are you?

HMJr: Oh, I'm fine. How are you?

J: Just fine. Got in this morning.

HMJr: Did you see that granddaughter graduate?

J: Absolute!

HMJr: Good!

J: That's the best trip I've had.

HMJr: Well, I want to see you when you -- you've gotten caught up on your work.

J: I'm ready now whenever you are.

HMJr: Are you?

J: Have you got anything to eat?

HMJr: Well, I -- always, but.....

J: Not today, huh?

HMJr: No. Well, the first date I've got open is next Tuesday.

J: All right. Put me down for next Tuesday then.

HMJr: All right. We'll have swordfish for you if there is any.

J: All right.

HMJr: Next Tuesday at one o'clock.

J: At one o'clock?

HMJr: Righto.

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- J: In the meantime, if there's anything on your mind, why.....
- HMJr: Well, sometime I'd like to talk to you about this Mead bill.
- J: All right.
- HMJr: As far as -- when are you going to testify?
- J: Tomorrow.
- HMJr: Well, I'll read what you've got to say in the papers, and then I'll talk to you.
- J: Well, I'd like to talk to you before. I was going to see the President this morning, but he -- they cancelled the engagement because I wanted to find out -- I wanted to talk to.....
- HMJr: Well, I don't know an awful lot, I'm studying it, but I don't know how he feels on it.
- J: What are your inclinations about it?
- HMJr: I don't know.
- J: Well, I'll say this, Henry, that we've got all the authority now that's explained in that bill.
- HMJr: Yeah.
- J: Every particle of it. Now, the -- I've got a report here from the Secretary of Commerce. He -- they sent -- they sent a couple, three of their men over here and went through three hundred and thirty of our rejected applications.
- HMJr: Yeah.
- J: I asked them to do it and they think we've been pretty generous in lending money.
- HMJr: Uh-huh.
- J: We've got that report here, and somebody was here from the S.E.C. I don't know who that was, and I.....
- HMJr: Well now, we set up a little committee inside the Treasury with Preston Delano on there.
- J: Yeah.

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HMJr: And -- and to get all the information together.

J: Yeah.

HMJr: So if you've got anything, if you'd shoot it over to him.

J: All right. Is he going to testify?

HMJr: No, but I just wanted to get everything ready that was in town so in case they asked the Treasury for a report I'd have one.

J: I see.

HMJr: I asked Preston to get everything together for me.

J: Uh-huh. So you haven't matured your.....

HMJr: No.

J:notes on it.

HMJr: I'm open for propositions.

J: I see.

HMJr: I expect to see Eccles Saturday, see?

J: You are going to see Eccles Saturday?

HMJr: I think so.

J: Is he going to testify on this?

HMJr: On Monday.

J: On Monday?

HMJr: Yeah.

J: Well, I'm supposed to go tomorrow. I'd rather wait until they're all through.

HMJr: I can be influenced.

J: Can you?

HMJr: Oh, yes.

J: Well -- (Laughter) I'll bear that in mind. Now, if some -- if it was some people, I'd know that a bottle of liquor would do some good.

HMJr: No, not that easy.

J: But you're not that easy.

HMJr: Not that easy. All right, Jesse.

J: You can't -- you can't -- ain't fooled until Tuesday.

HMJr: No.

J: I'll have to consult Mrs. Morgenthau to find out what your price is. Where is your weak spot?

HMJr: Well, you ask her.

J: Huh?

HMJr: You ask her.

J: I'll ask her. Yes.

HMJr: All right.

J: How are you getting along otherwise.

HMJr: Fine!

J: All right then. I don't know what I'm going to say. I told Mead a while ago -- he called me -- that I'd a good deal rather testify last because I'd rather everybody else -- I'd like to hear their criticism of what we're doing.

HMJr: Well, Eccles sounds very persuasive these days. I don't know which way I'm going to jump.

J: I see. All right, I don't know what he's going to testify to, do you?

HMJr: Yes, I've got an inkling, yeah.

J: You have, huh?

HMJr: Yeah.

J: You mean, credit for the bill?

HMJr: Well.....

J: Knocked down, huh?

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HMJr: I think if you waited a day or two you wouldn't be losing anything.

J: All right.

HMJr: Yeah.

J: I'll try to wait.

HMJr: O. K.

J: Good bye.

HMJr: Good bye.

June 1, 1939
12:17 p.m.

Operator: Go ahead.

HMJr: Hello.

Bill

Campbell: Hello, Mr. Morgenthau.

HMJr: Yes, Mr. Campbell.

C: Yes, sir. Now, I've checked carefully into Mr. Keeshin here, both with the Association of Commerce and friends of mine in the business, and he's undoubtedly your man.

HMJr: Good!

C: His reputation is splendid.....

HMJr: Fine!

C:throughout the city.

HMJr: Fine.

C: And he's a very outstanding man, of very good character, splendid references, and everyone thinks highly of him.

HMJr: Fine.

C: They think highly of his ability in the transportation field with particular reference to trucking or motor lorries, or things of that kind. They think that his experience is a little more limited in the field of railroad or air transportation.

HMJr: No. Well I'm -- this is all -- this is motor truck I'm interested in.

C: Well, in that they say he has no equal in the United States. He is undoubtedly the outstanding man in that particular phase of the transportation industry.

HMJr: Well, thank you so much.

C: Not at all, sir. I'm very happy to be of a little service to you.

HMJr: Thank you.

C: All right, Mr. Secretary.

WAR DEPARTMENT
OFFICE OF THE CHIEF OF STAFF
WASHINGTON, D. C.

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June 1, 1939.

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

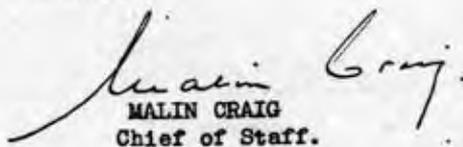
My dear Mr. Secretary:

Enclosed herewith is a letter which has just been received from General Brice P. Disque. He gives the Metropolitan Club, New York City, as the place where he can be located in the day-time, and he gives the 'phone number. He also gives his residence and the 'phone number. He apparently has been gotten in touch with by someone else on the same subject last Friday.

I can find nothing which would indicate that General Disque has had any particular experience in transportation matters. He was formerly a Cavalry officer and during the World War seemed to have been very successful with the Spruce Production Corporation. He is now on the retired list of the Army as colonel.

With kind personal regards,

Sincerely,


MALIN CRAIG
Chief of Staff.

encl.



METROPOLITAN CLUB
FIFTH AVENUE & SIXTIETH STREET
NEW YORK

May 29, 1939.

Dear Colonel W. C. C.:

Your letter of May 29 refers to a matter which a gentleman in this City discussed with me in confidence last Friday.

I will not mention your letter to him.

The project is a most tempting and interesting one

and you may say to
those who are responsible
that I am distinctly interested
and would be glad to go
into details at their convenience.

I am to be located
here during the daytime and
the phone is Regent 4, 8300.

My residence is in
Spuyten Duyvil, New York
City, no street number, and
my phone there (not registered)
is Kingsbridge 6-1612.

Best regards and thanks,

Very Sincerely,

Priscilla Digney



ASK YOUR F



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Colonel E. R. M. McCabe

3225 Edmonds St N.W.

Washington
D.C.

TREASURY DEPARTMENT

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INTER OFFICE COMMUNICATION

DATE June 1, 1939

TO Secretary Morgenthau
FROM W. H. Hadley

5-year Notes

<u>Coupon</u>	<u>Yield</u>	<u>Estimated Market Price</u>	<u>Premium</u>
3/4%	0.49	101.8	1 pt. 8/32
	0.51	101.5	1 pt. 5/32
5/8%	0.49	100.21	21/32
	0.51	100.18	18/32

"Rights"

<u>Market Price Just Before Today's Announcement</u>	<u>Present Market Price</u>	<u>Present Premium</u>
101.29	101.9	1 pt. 9/32

The market has become very steady at present levels so that an interest adjustment, which would amount to but 5/32nds, appears unnecessary. The present price on the "rights" indicates market expectation of a 3/4% coupon on the new note.

GROUP MEETING

June 2, 1939.
9:30 A. M.

PRESENT: Secretary Morgenthau
Mr. Hanes
Mr. Lochhead
Mr. Graves
Mr. Foley
Mr. Duffield
Mr. Gaston
Mr. Haas
Mr. White
Mr. McReynolds
Mr. Bell
Mrs. Klotz

H.M. Jr: A nice press.

Gaston: Yes, except for the pictures.

H.M. Jr: Gaston is complaining about his pictures. "Well,"
I said, "After all that is the guy."

I would like you to take on a contract for me, John.
I want to make life so miserable for Jesse Jones that
we can get him to do this, that is, to get through
a bank organization of a hundred million dollars.

Hanes: A bank --

H.M. Jr: A bank of North and South America, with a hundred
million dollars, but limited to North and South
America. You see, they have reached their limit,
practically of four million dollars -- the same
everything, but new capital, one hundred million
dollars, limited to North and South America.

White: A hundred million dollars?

H.M. Jr: I think that is all they can get this session.

Hanes: Will that be an extension on the amount or extra?

H.M. Jr: No; new.

Foley: A new setup.

H.M. Jr: A new setup.

- 2 -

Hanes: Whatever the management?

H.M.Jr: The same management, the same everything -- just to assist the bank. As a matter of fact, if I am correct, originally there were two banks.

Foley: First and Second.

H.M.Jr: I was talking to Cotton (?) about handling the thing, and then he comes back and reports to me that there is no chance; there is nothing but export and import. That is just what I want to do, to keep after North and South America; keep talking to me about it until I tell you to get the hell out of here. I told him "You get a bank of North and South America and you have earned your salary." Just give us the history on the No. 1 and No. 2 banks.

White: The Export and Import Bank was created especially to make possible loans to Russia.

H.M.Jr: That was the No. 1.

White: That was the first bank.

H.M.Jr: And that died.

White: That died of inanition.

Foley: It never was used, and later was dissolved.

H.M.Jr: I talked to Jones about this about a month ago, and he kind of liked it, but the time was not ripe. Well, I think the time is ripe now, and we need it very badly.

Hanes: Do you have any bill?

H.M.Jr: Have you got a bill?

Foley: I think we have. If not, we will have it today. It is not very hard.

H.M.Jr: What I would like you to do is to get hold of "Uncle Jesse" as we call him, and see if we cannot get it on Monday, and, if necessary, we can go over and see the President about it. But I would really like to put the heat on it. It is silly to talk about doing something for North

- 3 -

and South America when you have only four million dollars lending power left. We talk about doing things for recovery, and every dollar that is spent is spent here. But will you have this contract for me?

Hanes: Yes, sir.

H.M. Jr: What?

Hanes: Yes; I will.

Lochhead: Mr. Morgenthau, I think we ought to suggest the other alternative, and the RFC leans toward it, that in case of the two per cent bank, one hundred million dollars, with the proviso that they use it only for North and South America --

H.M. Jr: Sumner Welles liked the idea. He thought it would be very popular. He is for this, that it will be very popular in South America, if the bank were called the Bank for North and South America. It is just good publicity and another friendly gesture, the good neighbor. Sumner Welles said he would like that very much. We just want to go to the extent of pushing Jesse. We really need it awfully bad.

Hanes: I cannot do this until after the hearing.

H.M. Jr: No.

Hanes: But I can have it in late this afternoon.

H.M. Jr: All right; but just before you go, this is the humor the President is in: I have a new assistant in the Treasury; he gets a memorandum from the President. He no longer writes me, and I do not suppose there is anything I can do about it. You see whom the letter is addressed to. Look at the envelope. (Handing document to Mr. Hanes.)

Hanes: Yes.

H.M. Jr: Read the memorandum.

Hanes: It is addressed to "Dano", care of the Secretary of the Treasury.

H.M. Jr: Read the memorandum.

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- Hanes: "Preparation of reply for my signature".
- H.M.Jr: Yes; addressed to "Dano".
- Mrs. Klotz: It is about dog food or something.
- H.M.Jr: Somebody is complaining about the ruling that they got on dog food. Last night, with Mrs. Roosevelt, we were sitting at supper. Here was Henry Wallace, and here was I (indicating), and the President said, "Henry, I've got something I want you men to answer on dog food." So Henry Wallace said, "Which Henry?", and I said, "Which of us is in the dog house?" (laughter). I think it is a pretty good thing, sick as he is, he can write a letter like that. I am going to answer it.
- Gaston: That is based on that Argentine beef thing. They put up that canned stuff, which is used very largely for human consumption in South America, and labeled "Dog Food".
- H.M.Jr: Well, good luck to that contract on this thing. John, one second please. (The secretary conferred with Mr. Hanes, after which Mr. Hanes left the room.)
- Mac has too many papers with him this morning.
- Gaston?
- Gaston: No; I haven't anything. I thought you asked me something.
- H.M.Jr: No. I wish somebody would write a history, between now and Tuesday, of what I have done on the question of small business loans since I have been here, starting with the Viner study. I think that would be rather interesting. The Viner-Hardy study made back in 1934, wasn't it?
- White: This is the first I knew about it.
- H.M.Jr: Well, what else have I done? I know I asked the investment bankers of America to make a survey for me, which they did, and they made a report on the loans.
- Duffield: Do you want me to do that?

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H.M.Jr: Yes.

Duffield: All right.

H.M.Jr: Well, if anybody has any ideas, chuck them over to Gene.

Haas: I believed they wired from Honolulu about that.

H.M.Jr: Well, just look it up. It will be interesting. The Wall Street Journal has a good article on it today.

Gaston: I notice that the papers, the weeklies are crediting Douglas with authorship of that idea of the intermediate credit banks for industry. Douglas, I think, was a member of the committee that produced that report. They did not give out their report, but Douglas gave it out as a personal idea.

White: In this town there is really but one party to an idea.

Gaston: You do not need the words "in this town", Harry.

White: Well, I mean any place where it germinates.

Gaston: In fact, there is a bill in Congress to that effect. (laughter)

H.M.Jr: Come around and see me later, Harry. (laughter)
Ed?

Foley: Here is the reply to Wagner. You might not want to sign it until after you have shown the other letter to the President; but, you see, there you are in favor of the extension of the function of the USHA.

H.M.Jr: Bell is seeing it through the Budget office for me.

Bell: It is in the Budget, and they said they would give it prompt attention, because Straus already had a letter from the Budget, saying that there is no objection to it.

H.M.Jr: When you get clearance from the Budget, you bring it back to me and I will sign it.

Bell: O.K.

H.M.Jr: How is that?

Bell: O.K. I think I can get it today.

Foley: And here is one on the Mead bill, on the hearing of yesterday, as to the method of financing.

Duffield: Bill Campbell called yesterday and said that he was going to present the Annenberg case to the Grand Jury starting on Monday, and he thought he was in pretty good shape.

H.M.Jr: Did you give him the other half of that lawyer?

Duffield: Yes; he got it, and he said he would be down to see us on the first free day after he started, which might be in a week or ten days, or whenever the Grand Jury took a recess for a day.

H.M.Jr: The move is from him.

Duffield: He will be down, and, in the meantime, he is going to ask some lawyer to come in, whom he may want to recommend later on as counsel in the case. I told him I would have him see the people here. I do not know who he was talking about; so if he wanted to recommend him afterwards --

H.M.Jr: That is all right. I am a little bit pressed for time.

Duffield: I have Tietjen outside, if you want to see him.

H.M.Jr: Not just now.

Duffield: All right.

H.M.Jr: Did you send Miss Lonigan to Boston?

Haas: She is leaving tonight. She will have a written report for you.

H.M.Jr: All right.

White: John Hanes said that every power that is in the Mead bill,^{a9} he understands it, is in the RFC now. I thought maybe you could check up on that.

Foley: I do not think they have insurance power.

Bell: They have loan power.

Foley: They have loan power, but not insurance power.

White: He said every power, including insurance power, but he could check up on it.

H.M.Jr: There is a criticism in the Wall Street Journal to be answered. I would like to answer it. They say that all the bad loans will get three and a half and four per cent rate under the insurance plan, and the good loans will have to pay six per cent.

White: There is a special provision to prevent that, but it will depend on who operates.

H.M.Jr: I am raising the point as to who should answer that criticism.

White: You were speaking of Latin America and if anything further was done with respect to getting the thing lined up. I spoke to one of the men up from Brazil, and he just mentioned that there was a terrific possibility of getting together.

H.M.Jr: If you and Archie can map out a course, clear it through Mac, and Herbert, to me.

White: All right.

H.M.Jr: Archie, I wish you would call up Mr. Duganne and tell him I am still waiting to hear from them. I mean as to Venezuela -- or is it Venezuela?

White: Those people said they were waiting for Fox.

H.M.Jr: Just let him know that the Secretary of the Treasury is still waiting -- not impatiently, but waiting.

Harold, I hear you are raising hell over there in the Internal Revenue Bureau.

Graves: I don't think we are.

H.M.Jr: I hear you and Mac are having a grand time putting things in order.

Graves: Well, we are trying.

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H.M. Jr: My informant was Mac. (laughter) Why are you selfish; why don't you let Bell in on this.

McReynolds: I have not talked to Dan about it.

H.M. Jr: I suppose you have noticed that the Attorney General got back.

Foley: The night before last.

H.M. Jr: Yesterday morning. He had six or seven very important movie magnates on the carpet.

Foley: Bill Morris called Wenchel yesterday, and wanted to know whether he could impose upon him for a lawyer to work on the case, his people are scattered all over the country, and he has not anybody to work on it.

H.M. Jr: Really!

Foley: Yes.

McReynolds: He never has.

Foley: That is right.

H.M. Jr: I thought I might have gotten a "Thank you" or something on it.

Bell: I have nothing.

McReynolds: You will probably remember that Henry Wallace asked you about a fellow that is not wanted to get back into this country.

H.M. Jr: Yes.

McReynolds: That is the latest memorandum on it. (handing document to the Secretary)

H.M. Jr: Well, show that to Wallace, let Wallace see it.

McReynolds: All right.

H.M. Jr: Give him a copy of it.

McReynolds: Yes. Here is a memorandum that you were going to sign for the President, about that Indiana collector.

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- H.M.Jr: Mac, write the memorandum to the President, saying "This is the way; I guess I won't change the Collector of Revenue in Indiana any more than I did the one in Florida for you" -- just like that. I told him to leave off the Florida one, and not to remind the President. Mac thought it was a good suggestion.
- McReynolds: That has not been cleared with the Senators yet. That is that Sullivan case, and I will see that it is cleared. (handing another document to the Secretary.)
- H.M.Jr: My friend Pepper called me up yesterday to tell me that there was a letter on the way down from Adams to protest against this medal business. I told him not to worry, that I was still going to pin a medal on Pepper.
- McReynolds: I had a letter yesterday from Adams, saying they would have a thousand other bills if they followed your recommendation on the Florida case, and I sent it down to Larry Bernard to prepare the argument. It came in yesterday afternoon.
- H.M.Jr: He has forgotten his college manners.
- Bell: He saw Adams yesterday on the Rivers and Harbors and Flood Control Bill.
- H.M.Jr: Yes; but the boys did a good job on Dr. Townsend.
- Bell: Very good.
- H.M.Jr: That is something to be thankful for.
- O.K.
- (Conference concluded at 9:55 o'clock A. M.)

AFG

TREASURY DEPARTMENT

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INTER OFFICE COMMUNICATION

File

DATE June 1, 1939

TO Secretary Morgenthau
FROM Mr. Foley

With further reference to Senator Norris' amendment to our bill to amend the Second Liberty Bond Act (H.R. 5748) which the Senate adopted this afternoon when it passed our bill by a vote of 44 to 23 -

Under existing law the TVA is authorized to issue, for general TVA purposes, 100 million dollars in bonds, one-half of which are authorized to be issued "on the credit of the United States", while the other half are "fully and unconditionally guaranteed both as to interest and principal by the United States". The TVA law also provides that any bonds issued under it shall have all the rights and privileges accorded to Panama Canal bonds, which means that they are fully tax exempt and have the circulation privilege.

Norris' amendment would combine the two authorizations into one authorization to issue bonds not to exceed in the aggregate 100 million dollars; would eliminate the provision of the TVA Act which accords to its bonds the rights and privileges accorded to Panama Canal bonds; and would eliminate the expression "on the credit of the United States", by providing that all bonds issued under the TVA Act would be fully and unconditionally guaranteed both as to interest and principal by the United States.

On May 23, 1939 we submitted a favorable report on the fiscal aspects of S. 1796 (which is identical with the Norris Amendment) to the Chairman of the House Committee on Military Affairs; however, we called attention to the fact that such bill would require approval by the Federal Power Commission of the purpose for which the funds derived from the sale of bonds could be used prior to their issuance, and suggested that it might be better to substitute for such provision one which would permit issuance of the bonds without such approval but restrict the use of the proceeds to purposes approved by the Federal Power Commission. A copy of S. 1796 is attached.

S. 1796

76TH CONGRESS
1ST SESSION

S. 1796

IN THE HOUSE OF REPRESENTATIVES

APRIL 17, 1939

Referred to the Committee on Military Affairs

AN ACT

To amend the Tennessee Valley Authority Act of 1933.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*
3 That the Tennessee Valley Authority Act of 1933, as
4 amended, be, and the same is hereby, amended by striking
5 out sections 15 and 15a of said Act and inserting in lieu
6 thereof the following:

7 "SEC. 15. With the approval of the Secretary of the
8 Treasury the Corporation is authorized to issue bonds not
9 to exceed in the aggregate \$100,000,000 outstanding at any
10 one time, which bonds may be sold by the Corporation to
11 obtain funds for the construction or acquisition of dams with
12 appurtenant facilities, generating plants, transmission lines,

1 rural distribution lines, and other electric utility properties
2 as authorized by this Act, including the purchase of the
3 electric utility properties of the Tennessee Electric Power
4 Company, and for the purpose of carrying out the provisions
5 of section 12a of this Act. Such bonds shall be in such
6 forms and denominations, shall mature within such periods
7 not more than fifty years from the date of their issue, may
8 be redeemable at the option of the Corporation before ma-
9 turity in such manner as may be stipulated therein, shall
10 bear such rates of interest not exceeding $3\frac{1}{2}$ per centum per
11 annum, shall be subject to such terms and conditions, shall
12 be issued in such manner and amount, and sold at such prices,
13 as may be prescribed by the Corporation with the approval
14 of the Secretary of the Treasury: *Provided*, That such
15 bonds shall not be sold at such prices or on such terms as to
16 afford an investment yield to the holders in excess of $3\frac{1}{2}$
17 per centum per annum. Such bonds shall be fully and un-
18 conditionally guaranteed both as to interest and principal by
19 the United States, and such guaranty shall be expressed on
20 the face thereof, and such bonds shall be lawful investments,
21 and may be accepted as security, for all fiduciary, trust, and
22 public funds, the investment or deposit of which shall be
23 under the authority or control of the United States or any
24 officer or officers thereof. In the event that the Corporation
25 should not pay upon demand when due, the principal of, or

1 interest on, such bonds, the Secretary of the Treasury shall
2 pay to the holder the amount thereof, which is hereby
3 authorized to be appropriated out of any moneys in the
4 Treasury not otherwise appropriated, and thereupon to the
5 extent of the amount so paid the Secretary of the Treasury
6 shall succeed to all the rights of the holders of such bonds.
7 The Secretary of the Treasury, in his discretion, is authorized
8 to purchase any bonds issued hereunder, and for such purpose
9 the Secretary of the Treasury is authorized to use as a
10 public-debt transaction the proceeds from the sale of any
11 securities hereafter issued under the Second Liberty Bond
12 Act, as amended, and the purposes for which securities
13 may be issued under such Act, as amended, are extended to
14 include any purchases of the Corporation's bonds hereunder.
15 The Secretary of the Treasury may, at any time, sell any
16 of the bonds of the Corporation acquired by him under this
17 section. All redemptions, purchases, and sales by the
18 Secretary of the Treasury of the bonds of the Corporation
19 shall be treated as public-debt transactions of the United
20 States. With the approval of the Secretary of the Treasury,
21 the Corporation shall have power to purchase such bonds in
22 the open market at any time and at any price. No bonds
23 shall be issued hereunder to provide funds or bonds necessary
24 for the performance of any proposed contract negotiated by
25 the Corporation under the authority of section 12a of this

1 Act until the proposed contract shall have been submitted
2 to and approved by the Federal Power Commission. When
3 any such proposed contract shall have been submitted to
4 the said Commission, the matter shall be given precedence
5 and shall be in every way expedited and the Commission's
6 determination of the matter shall be final. The authority
7 of the Corporation to issue bonds hereunder shall expire
8 January 1, 1941, except that such bonds may be issued at
9 any time after the expiration of said period for refunding
10 purposes or to provide bonds or funds found necessary for
11 the performance of any contract entered into by the Corpora-
12 tion, prior to the expiration of said period, under the
13 authority of section 12a of this Act."

Passed the Senate April 13, 1939.

Attest:

EDWIN A. HALSEY,

Secretary.

70TH CONGRESS
1st Session

S. 1796

AN ACT

To amend the Tennessee Valley Authority Act
of 1933.

APRIL 17, 1939

Referred to the Committee on Military Affairs

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

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DATE June 1, 1939

TO Secretary Morgenthau

FROM Mr. White

Subject: The Proposals of Mr. Berle to the Temporary National Economic Committee

The proposals made by Berle are not definite as to detail or method of administration but are quite specific with respect to principle.

The proposals in essence are:

1. Setting up of a public works finance corporation (similar, for example, to the R.F.C.) to finance self-liquidating projects of the United States Government and of local governments. The rate of interest on loans to be no higher than is necessary to get the needed public works constructed. The interest rate would vary from time to time depending upon the level of business activity -- low rates when business activity is low and high rates when business activity is high. Rates would be low for public works which cannot afford to pay interest. Judging from his comments, rates almost down to zero are possible if necessary to get the particular public works, such as hospitals.

The funds would be financed either by the extension of the Federal reserve credit through rediscounting the bonds accepted for the loan or through sale of debentures to the public (though Mr. Berle apparently prefers the former).

Though no recommendation is made on this point, presumably the Federal Reserve Board would dictate the rate of rediscount.

The principles involved in the first proposal are (1) flexibility in the rate of interest charges which would provide for selectivity as to type of project with rates as low as zero, and alteration in the rates according to time for purposes of preventing inflation, and (2) that the funds required for the public works projects should be obtained from the central bank through the process of rediscounting (presumably at a rediscount rate which is also selected in accordance with the rate charged to the borrower.) This proposal is a stop-gap to be used until the Capital Credit Banks proposed under (3) are set up.

Secretary Morgenthau - 2

2. The second proposal is full support of insurance of loans to small business men, presumably the Mead Bill.

3. The third proposal is the establishment of a system of capital credit banks. The difference between such banks (which may even be grafted on present private commercial banks) and present credit facilities is that (1) loans shall be made for long term, (2) the rate of interest shall vary according to the level of business activity and should be selective as to type of project in order to insure full use of our capital resources.

Obligations accepted from public bodies are to be rediscountable at the Federal reserve banks at a rate of interest presumably also selective and variable.

Loans made to private industry, however, are to be financed through the sale of the banks own debentures to the public or through the acceptance of banking deposits.

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Questions raised by Mr. Berle's proposal that need to be discussed:

1. Is there danger of inflation resulting from the use of Central Bank credit at low rates of interest for public works?
2. Who is going to make the decision as to the criterion of variation in rates charged for different projects?
3. Who is to decide what criterion shall be applied to determine the rate of rediscount to be charged by the Federal Reserve banks?
4. Who is going to pay the losses that would arise from extension from later defaults?
5. What advantage does this method have over the present r.f.c. method of financing public works?
6. What is the difference between this method of financing and the financing of public works ~~public~~ projects through printing of fiat currency?

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E. J. ...

TREASURY DEPARTMENT
INTER OFFICE COMMUNICATION

DATE June 1, 1939

TO Secretary Morgenthau
FROM Mr. White
Subject: The Mead Bill, S.2343

Summary of the Bill

1. The R.F.C. to insure bank loans up to 90 percent of the loan when the loans are made to business under the following conditions:
 - a. Maximum amount of insurance to any single borrower not to be in excess of \$1 million.
 - b. Loans to be made for a period of 1 to 10 years.
 - c. The interest rate on loans to be no more than 4 percent of the unpaid balance of the loan plus a service charge of no more than an amount equal to 1/4th of 1 percent(per annum, or total - not clear).
2. The insurance provision is exceptionally liberal in that the R.F.C. is permitted to insure loans even though such loans are subordinated to short-term indebtedness which may be incurred in the ordinary course of business by the borrower.
3. The only safeguard against granting loans of doubtful security is the judgment of the banks which have a 10 percent stake in the loan. The corporation may require from the banks reports as to the condition of the loan.
4. Any loan insured under this Act is eligible for rediscount by the Federal Reserve Bank.
5. There is apparently nothing in the Act that would prevent banks from insuring loans which have already been extended and which may be of doubtful security. However, the corporation can refuse to insure loans of those banks which follow the policy of insuring only their bad risks.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE

June 1, 1939.

TO Secretary Morgenthau
FROM E. H. Foley, Jr.

For your information

Further hearings were held this morning by the Subcommittee of the Senate Committee on Banking and Currency on the Mead bill.

Congressman Schwert of New York and Congressman Voorhis of California testified in favor of the bill and emphasized the need of additional credit facilities for small business enterprises. Congressman Schwert suggested that provision be made in the bill for the insurance of character loans with an upper limit of \$2,500 or \$3,000.

Jerome Frank of the Securities and Exchange Commission and Jesse Jones of the Reconstruction Finance Corporation are scheduled to testify tomorrow. Chairman Eccles of the Board of Governors of the Federal Reserve System is scheduled to testify sometime the early part of next week.

E. H. F. L.

RE: THE MEAD BILL - HOUSING.

June 1, 1939.
11:00 A. M.

PRESENT: Secretary Morgenthau
Mr. Hanes
Mr. Foley
Mr. White
Mr. Gaston
Mr. Haas
Mr. Duffield
Mr. O'Connell
Mr. Kades
Mr. Tietjen

H.M.Jr: Who is going to be teacher? Let us start on the Mead bill.

Foley: Here is a memorandum on the bill. (Handing a document to the Secretary)

H.M.Jr: Suppose you read it outaloud.

Foley: All right. I think everybody has a copy of this memorandum. (reading:-

"Senator Mead of New York on May 8, 1939 introduced Senate No. 2343 which was referred to the Committee on Banking and Currency and, if enacted into law, will be known as the "Insured Business Loans Act of 1939."

"The bill authorizes the Reconstruction Finance Corporation to insure business loans of banks, whose deposits are insured by the Federal Deposit Insurance Corporation, to the full extent of losses incurred in excess of 10% of the principal amount of any loan for a business purpose.

"Premiums charged for such insurance may be at the rate of not less than 1/4 of 1% and not more than 1% per annum, depending upon the nature of the loan and the character of the risk involved.

"The bill permits the Corporation to charge a higher premium or to refuse to grant insurance altogether on loans of any bank which pursues the policy of insuring only its more doubtful loans.

"To be eligible for insurance, a loan to any one firm must not (1) exceed \$1,000,000, (2) be made for a period less than one year or more than ten years, (3) bear interest, (exclusive of premium and a moderate service charge) in excess of 4% per annum, and (4) be made to any firm of which an officer, director, or security holder owning more than 10% of stock is also a director of the bank making the loan."

Mr. [unclear]: Read that again, will you.

Foley: " (4) be made to any firm of which an officer, director, or security-holder owning more than 10% of stock is also a director of the bank making the loan."

In other words, if somebody is an officer, director or owner of ten per cent of the profit of a corporation --

Upham: Of the stock of the bank.

Foley: Yes; of the stock of the bank -- he cannot get an insured loan from that bank. (reading further)

"Insured loans are made eligible for rediscount with the Federal Reserve banks for the full amount of the insurance, that is, 90% of the face value of the loan. In addition every Federal Reserve bank is authorized to buy and sell obligations evidencing loans insured under the bill in accordance with rules and regulations which the Federal Reserve Board shall prescribe.

"Putting the risk of loss -- the risk of all losses up to 10% of the principal amount of the loan on the lending bank -- would appear to have several advantages:

- " (1) It constitutes a safeguard against improvident lending and as an automatic check on the abuse of the insurance privilege;
- (2) It eliminates the expense and annoyance involved in the adjustment of relatively small losses;
- (3) It should operate so as to relieve a bank from the fear that even a fair business risk may be a greater risk than a commercial bank can afford to assume, but at the same time deter a bank from assuming other than a fair business risk.

"A distinct advantage of the Mead bill is that it meets the credit problem of small enterprise without creating a new system of banking institutions, without creating a new Federal agency, and without disturbing the traditional method of financing capital expenditures by small enterprises."

Here is a copy of the bill. (Handing a document to the Secretary.)

H.M. Jr: Yes. Thank you. Mr. Delano, have you people studied this matter?

Delano: We have done it in a very preliminary way. We have read the bill, and have had a copy of it, certainly.

H.M. Jr: Tell Mr. Bell, if he is not busy, he ought to stop in on this meeting.

Delano: There are several considerations that appear manifest in the bill to me and to the Comptroller's office. In the first place, we doubt if it would produce any large increase in the amount of bank loans to small industries.

H.M. Jr: Yes.

Delano: That is just a forecast, but that seems to be a pretty general impression. Secondly, it would seem to cover somewhat the same field as already covered by the exchange to the RFC. Thirdly, it is, of course, taking a step towards what you might call socialization credit. It does not go all the way, but it is a step in that direction. It has that implication. Now, as to the advisability of it, I do not think we are in a position to give you a recommendation or commitment.

H.M. Jr: Have you been asked?

Delano: We have not.

H.M. Jr: Well, I will ask you to make a recommendation.

Delano: Well, we will do that.

H.M. Jr: To me.

Delano: I will be glad to do that.

H.M. Jr: Do you think you can get me something by Monday?

Delano: Yes, sir.

H.M.Jr: Is there anybody who wants to talk either for or against the Mead bill?

Hanes: I do not want to talk against it. I am against it, but I do not know that I want to be on record as being opposed to it. I will say this for it, that it is the best of all the plans that I have seen so far. It follows pretty closely the general pattern of the plan that I brought back --

H.M.Jr: From Minneapolis.

Hanes: From Minneapolis, but I think it is just another step in the direction of the Government's entrance into the banking field. For that reason, I am opposed to it.

H.M.Jr: I do not understand, I thought the banks would do this business just the way they do the FHA, but we are assuming a Federal risk.

Hanes: Ten per cent of the risk.

H.M.Jr: I thought the plan that you brought back on that was the plan --

Hanes: I say it is patterned closely after that plan. There are several minor differences.

Duffield: Yes; there are some minor differences.

Hanes: Six per cent. This calls for a ten per cent guarantee.

Duffield: The guarantee works a different way.

Hanes: Yes.

Duffield: The guarantee was eighty per cent on all loans under Title 1 of the FHA, whereas this is under Title 2.

Hanes: This is much better.

Foley: This is much better; yes.

Delano: It takes the first twenty per cent of the risk under Title 1. That insures the first loss. This insures the last end of the loss.

H.M.Jr: In other words, the bank in each particular case takes the first part of the loss.

Foley: That is right, and that is why it is a check on the insurance feature.

Delano: That is the reason I am forecasting that it might be generally used to reduce the flow of credit that they are after.

H.M.Jr: This does go through the RFC, does it not?

Delano: Yes.

Foley: Yes. It does not create any new agency, but it takes care of small industries through the RFC and the principle which has been established by the FHA.

H.M.Jr: Is Jones for this?

Foley: I think he is.

Hanes: He is going to testify today.

Foley: Tomorrow.

H.M.Jr: What about the American Bankers?

Delano: They are opposed to it.

H.M.Jr: Have they a memorandum?

Delano: They have no memorandum, but I am quoting from Benson's speech, and the comment of various bankers.

H.M.Jr: Could you ask them what their position is?

Delano: I will do that.

H.M.Jr: And if they have a committee on it, maybe they would like to come in and tell me why.

Hanes: From an examination or investigation which they made over a period of twelve months, I think there is --

Delano: We have nothing here.

Hanes: I think we can get it.

H.M.Jr: Could you get them, Preston?

Delano: Yes.

H.M.Jr: Ask them, and tell them I would like to know.

Delano: Did you happen to see Benson's speech?

H.M.Jr: No, I did not.

Delano: That is what I am quoting from. I imagine he checked that pretty carefully.

H.M.Jr: I have an open mind. I am trying to get all the facts.

Delano: I feel very sensibly on what is trying to be done here. I thoroughly understand that and sympathize with the comments, but there are some grave questions involved.

H.M.Jr: Well, if we can get them to work all together --

Delano: We will have something for you by Monday. I will get the papers.

Hanes: The one million dollar limit is extremely high for little businesses. The maximum of fifty thousand dollars for a little business is why I am in much more sympathy with the bill. A one million dollar loan to little business --

White: The first bill calls for \$200,000 maximum. Do you know why that was arrived at in the second bill?

Hanes: No, I have not any idea why it was arrived at in the second bill.

Duffield: I do not know why this bill was changed, but I think Johnny will remember that we discussed that when Mr. Taylor was here a year ago. He said there was a gap in the underwriting facilities, and that gap was sometimes from three million dollars down to \$50,000, and sometimes from one million dollars, depending upon the regional practice. This insurance thing ought to take care of that, and we suggested it at that time. It does not ordinarily move through underwriting channels. The limit is somewhat debatable, but the question is whether if a fellow wants to raise this money,

a million dollars, say, he could go to an underwriter for it, or whether he is dependent upon bank credit for that sort of money.

- White: I think that is explained. You will remember a year ago, when they were discussing the inadequacy of the credit disability, it was too expensive for them to use the current channels, particularly since the last change was made in the question of underwriting those facilities by banks. This is also designed to take care of an entirely different type; namely, those individuals who cannot borrow because the bankers are reluctant to extend credit because they feel the risk is a little too great; but under this plan they would obviously be risking only ten per cent of the capital, which they would get back in two years, plus the fact that this is from a one to a ten year loan, whereas commercial banks presumably want to have short term loans.
- H.M. Jr: Do they get back their ten per cent first?
- Duffield: Their interest would cover within three years under the ten year loan.
- Hanes: They paid the RFC one quarter for it.
- H.M. Jr: For example, if a fellow wants a hundred thousand dollars, does he go to the RFC office first?
- Foley: No; he goes to the bank.
- H.M. Jr: If the bank approves it, they clear it through the RFC.
- Foley: Yes; that is right; except for insurance.
- H.M. Jr: Well, they have to examine each loan.
- White: They will have to insure it.
- H.M. Jr: They have a right to reject it.
- Foley: Oh yes, absolutely. They have a right to reject, and they have a right to charge a higher premium than --
- H.M. Jr: On all above four per cent?

Foley: No; it is a quarter to a full one per cent.

H.M.Jr: Does it mean that everyone of these loans will come to the Washington office of the RFC?

Foley: I think they would handle it through their agency in the field. They have offices in Chicago and New York.

H.M.Jr: If it all goes across one man's desk --

Duffield: I do not believe that all the FHA loans come down here.

Foley: No, they do not.

White: But many loans of the bankers would have to be cleared by somebody in authority.

H.M.Jr: I understood that the Federal Reserve, a few weeks ago, were to take the position that these should clear through the Federal Reserve and not the RFC.

Foley: I think the RFC is in a much better position to administer a program of this kind. They have had more experience and they are equipped to do it, I think, better than the Fed. banks.

White: The Federal Reserve banks have agencies; they have regional banks. They have conducted a banking business, that is presumably no different than the others. The only difference would be that the Federal Banks have hitherto looked on the thing, probably, as too much of a business risk, whereas the RFC has regarded it, presumably, although, actually, the opinion might be quite different, but presumably have regarded it from the point of view of the public interest.

Foley: That is right.

White: And that would be the difference, but presumably it does mean that whoever has the right to insure the loan has a lot of power, because there is a lot of power that will be concentrated in each of the banks. I think the RFC could accomplish it, so far as the loans are concerned, much better, and I think the administration has much more policy control over the RFC than over the Federal Reserve banks.

H.M.Jr: Is there any limit on the amount of insurance?

Hanes: One billion dollars.

White: There is nothing in the bill.

Hanes: I understood it was one billion dollars.

Foley: It is a million dollars to each firm.

Hanes: No; it is one billion dollars total.

Upham: A billion has been suggested or talked about.

Hanes: That is my understanding, and the suggestion was that there should be some top limit that they could put out for this purpose.

H.M.Jr: I heard of several cases in New York and Chicago, where the banks make a seven, eight or ten year loan. They keep the five and sell the six, seven and eight year to the insurance companies. Have you heard about that?

Delano: Yes.

White: There is a provision in here --

H.M.Jr: They sell the six, seven and eight years to an insurance company, and the insurance companies are hungry for that business.

Delano: That is rather interesting, Mr. Secretary. I made an inquiry into the situation several weeks ago, when this question first came up, as to how much in the way of small investments there was in the Federal banks. Our Federal banks have got out about \$330,000,000 of long term small industrial loans. Now, the RFC has got out a little over four hundred million. The Fed has practically none. Of course the Fed had a different law under which they operated. The thing I am wondering about is why one would think this setup would produce more active lending by the banks than has already been covered by the RFC direct authority. I cannot see why. Here is the RFC with a pretty broad general authority to loan. Of course, they are subject to the statement that the institution to which they loan must be solvent, and that it must be a credit transaction, not a capital

transaction; but where you have credit and where you have capital, they merge very readily in discussing loans of this character, because a lot of this money is risk capital and not just a plain straight bank loan. The thing I cannot get clear on is why the original ten per cent loss has to be taken by the bank, as differentiated from the FHA, which takes the original twenty per cent loss, with all the complications that set in, with the RFC sitting in the banks, going over the records and locking into each transaction -- why that would create a larger flow of capital than simply by the RFC sitting down, with its broad authority to loan. Then, why not use the RFC agency and let them make that loan? Broaden it that way.

Foley: It seems to me that what you are saying is that it may not create all the advantages that its sponsors hoped they would provide.

Delano: I think that is right.

Foley: But if it does not, I do not see why any harm has been done in providing this sort of mechanism, because if the banks do not want to make the loan, there is nothing that the RFC could do.

Delano: That is very true.

Foley: And I think it is better for the banks to make this loan than have the RFC make it, because I think it is their business to make it. I think they will be making these loans, and if this is going to encourage them to do it in any degree at all, then I think it is a desirable thing to do.

Delano: Well, there is that aspect of it.

Foley: As far as the banks are concerned, it seems to me that the FHA program has been a very desirable thing. While they are in favor of it, they were not all in favor of it at first. I do not see why the operation by them should be any different than the operation by the FHA, and the FHA has not been sitting down on the banks.

Delano: They work on a different theory, it seems to me.

Duffield: That is only Title 1.

Delano: Yes.

Duffield: Title 2 is each loan in itself.

Delano: Yes; but I am just using this as an example, but I think you must have in mind this different relationship. The first loss was taken by the FHA. In this it does not.

Foley: I agree with John on all of these things that have been suggested so far. It seems to me that this is the most innocuous. It leaves the lending function where it belongs -- in the banks. It does not transfer it to the Government. It really provides for a method and encouragement to the banks to make this sort of loans. The fact that they have to take the first ten per cent risk is a deterrent upon the improvident use of this insurance scheme. It seems to me that it cannot do very much harm. It may do an awful lot of good.

H.M. Jr: May I interrupt you to ask this question? You used the phrase "This is the most innocuous scheme that has been presented." I would like somebody to present to me first the need. What I would like to have first are the basic facts from somebody from the economic section first, the need, if there is the need, and if there is no need, why should I take the position that this is the most innocuous? I want to know first the need; I would like to have that information first. Then, if there is no need, let us all jump in and say, "To hell with it". If there is no need, then it is not necessary. Does that make sense, John?

Hanes: I think it does.

H.M. Jr: I think somebody -- Foley, White and the rest of them should ask Dr. Hardy. What is it, George?

Haas: This is a part of the Berle thing; so he would probably come in on it.

H.M. Jr: Before I go any further with somebody's pet scheme, I would like to have the basic information. I mean, first, the need for this -- how badly is the need for it. I would like to start with that.

White: There is a difference of opinion, and it is impossible to illustrate the difference. Some

business men are unable to borrow from the banks, because the bankers do not want to take the risk, but this is reducing the risk by ninety per cent; instead of one hundred, they risk only ten per cent. Unquestionably, there will be some loans which they will make which they would not make if they were not insured up to ninety per cent.

H.M. Jr: We are talking now about a matter of opinion.

White: Yes; and there is no way to restrict that thing. When you initiated the investigation four years ago --

H.M. Jr: Which Hardy made.

White: Yes. The results were inconclusive, and they went into very great detail in attempting to run down the fact as to whether or not a small business man had any difficulty in getting a loan, even if his credit was good.

H.M. Jr: You seem surprised, Cy, at that statement.

Upham: I did not think that that was inconclusive.

H.M. Jr: What is your recollection of the Hardy report?

Upham: That they felt that there was a very small number of businesses which, without good credit reasons, could not get banking accommodations. I would say the reason it was inconclusive was because we could not participate in an examination of each loan, and we had absolutely no way of telling whether it was available to us. We did not want to go any further with it because we felt it was impossible to determine from the papers whether a bank was justified or not in turning down a loan on various imponderables.

H.M. Jr: I would like first to have whatever stuff there is. Let us get that first. In that connection, we had FHA with authority to make loans up to \$50,000 to plants for equipment. Is that still in force?

White: No; that is in. --

H.M. Jr: In what -- one or two years? You have the experience of the Fed. Let us find out their experience. You have the whole

experience. You have the experience of the RFC, and if we are going into this thing, I want at least to be courageous and honest about it, about the whole question of deposits and the rest of this thing. Are we just going to do something because there is pressure on us, or are we really going to do something about the banks which handle checking accounts that they have to keep liquid?

Delano: Of course, this all comes back, Mr. Secretary, to those schools of thought, and I think there is a tremendous difference in schools of thought as to what is reasonable.

H. M. Jr: I am as dispassionate as anybody can be. I do not know that I am even going to be asked, but if we are asked I would like the information which is available, and this is the best way to make it available now. Of course, we ought to get hold of this man that Bill Myers had here. Bill Myers had a man here from Europe, who was the outstanding authority on long term credits for banks in Europe. What was his name?

Gaston: Was that Curt Victorius?

H. M. Jr: I think so.

Gaston: Secretary to the German Bankers Association.

H. M. Jr: Yes. There is a very fine bank in France that makes long term loans. That, of course, is just a bank put up for that purpose. I am just wondering if the Mead bill is the answer to a maiden's prayer, or doesn't the maiden need any help? Cy thinks the maiden is not virtuous. He never used to be like that when he was in the Treasury Department. But I am not satisfied that I have the information, and I wish I could get it.

Haas: May I comment on what you may expect?

H. M. Jr: Yes.

Haas: I don't think -- well, in fact, I am quite positive that we cannot assemble any information, quantitative information, that will be conclusive. I think you can demonstrate without much difficulty that the credit in this field, the small business field,

is a weak spot in our credit structure. I think we can demonstrate that. It has been a problem in this country and in Europe and elsewhere, whether or not this is the best solution of the problem, which I do not believe can be measured quantitatively, in view of any statistics that I have knowledge of, and whether or not this is the best solution of that problem is a matter of opinion. But I think the Mead bill is the best plan I have seen, particularly as to this first ten per cent, because I think that is the outstanding characteristic of the whole thing. As I view it, the local banker should know, because of his familiarity with the community, the credit risks, if he knows anything. This tends to put that burden on him and make him responsible there to the extent of ten per cent. If that ten per cent was not in the bill, I do not think it would be a very --

H.M.Jr: The first ten?

Haas: The first ten, and that applies, Mr. Secretary, not to the total, but to each loan, and that is very important, too.

Duffield: Mr. Secretary, may I recall one thing? There was this subcommittee a year or so ago, consisting of, I think --

H.K.Jr: Szymczak.

Duffield: Yes; Szymczak, Mr. Taylor and Mr. Fahey or Mr. Douglas -- I have forgotten.

H.M.Jr: Yes.

Duffield: They at that time came out in favor of increasing the RFC authority, with the additional request on the RFC that they keep files on all applications, both approved and rejected. It seems to me that in those files there ought to be a distillation of the experience that they have had with the type of borrower or type of prospective borrower who comes to them. I have talked to some of the younger men in the RFC who have handled cases, and if spot judgment is any good on this thing, there is some doubt whether, with insurance or anything else, these people are a good credit risk. They say the amount of their borrowings are less than ten per cent, with nothing but their life

insurance policy as collateral; but it seems to me that since there was that understanding with the RFC, they ought to keep some records and know what the problem was at the end of a year or so, and we ought to ask them for what they have.

H.H. Jr: Well, you ask them.

Doffield: I think John has already talked to Jesse Jones about it. Haven't you?

H.H. Jr: No; I have not talked to Jesse Jones about it.

H.H. Jr: I have had two experiences with these loans. I remember the husband of the housekeeper at the White House stopped me one afternoon. He had a cousin in the whaling business, with two hundred or two hundred and fifty men, and equipment. All they needed was twenty-five thousand dollars or a fifty thousand dollar loan to put them in a position to shove off for the whaling season, but they could not raise that amount of cash, whatever it was. They were in San Francisco, and I telegraphed out to San Francisco to the Fed and asked them to look into it, and within twenty-four hours they got that loan; they sailed and they paid every dollar back -- and I got a whale's tooth out of it. (Laughter)

But this fellow just could not get it.

Another case was one of these small business men down here, a fellow who did repair work on Diesel engines. He had a written contract with the Atlantic and Pacific to furnish them with the red tail, secondhand, used lanterns for motor-boats going up in the salmon country in Alaska. He signed a contract for those engines, ten thousand dollars, they could not borrow enough money in order to get the materials, although here was a contract and the fellow was an expert; he knew his business, and very few people know how to repair these Diesel engines. We got him the money. He did his business. We had to pay a terrific interest. How much did this fellow have to pay -- twelve or fourteen per cent?

H.H. Jr: Something like that.

H.M.Jr: Twelve or fourteen per cent.

Haas: And he was glad to pay it.

H.M.Jr: But the bank would not give it to him. He had to go to one of these loan sharks -- I had to go to the loan shark for him. We could not get it from the bank. He rebuilt the engines, delivered them, and made his profit.

Those are a couple of cases that I handled personally. There are a lot of cases like that, where the fellow cannot get the money. So there is something wrong somewhere.

Delano: Personally, I have seen them make them loans when they started.

H.M.Jr: But they do not --

Delano: The Fed.

H.M.Jr: But they do not.

Delano: No.

White: I think there was only \$20,000,000 loaned. It was some trifling sum that they loaned out of the \$143,000,000.

H.M.Jr: I do not know how much experience other people have had, but the thing that bothers me is whether this should be in the National banks at all.

Delano: That is one of the pertinent questions.

H.M.Jr: I do not know whether it should be in the National banks at all, or whether it should be in the banking industry, carefully regulated and carefully supervised.

Delano: That is what Berle holds, very roughly.

H.M.Jr: That is something else again. O'Connell, can you just sketch Berle's plan for us.

O'Connell: Berle's suggestions for the immediate future were the enactment of a bill substantially along the lines of the Mead bill and the creation of a Public Works Finance Corporation to finance

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projects of self-liquidating Federal agencies and projects of states and municipalities. The Mead bill is, to his mind, merely a stop-gap pending the formulation of his broader and more revolutionary idea for a permanent cure of the capital stagnation problem. His long range proposal involves the creation of a system of capital credit banks to meet the capital needs of our economy, operating on an entirely different basis from anything we now have. He feels that the profit motive should be incidental to the need to be served and advocates flexible interest rates, the rates being fixed at whatever rates a particular socially desirable project could stand. For example, he would think that such a project as a hospital should be financed at a purely nominal rate of interest, that the interest which a low housing project or slow clearance project should bear would also be little more than nominal and that the interest rates should grade upward toward the more usual commercial rate in what he calls the more strictly commercial projects. In general, he feels that the interest rate should be fixed low enough to permit the work to be done, rather than to have a comparatively inflexible rate which, to his mind, prevents much needed work being undertaken. His long range plan is obviously quite revolutionary.

- W.H. Jr: Let us get back to my old theory that we have to decide whether we are going to have a capitalistic system based on profit or state socialism. They are two systems which are used as an example.
- Delano: That is where this discussion leads.
- O'Connell: There was a substantial amount of testimony before the Temporary National Economic Committee last week by a number of small business people and representatives of the SEC relative to the needs of small business for credit and inability to obtain it. The testimony included the results of surveys made by SEC representatives in several different localities, which surveys reinforced the testimony of the individual small business people as to their inability to obtain needed credit. The witnesses included the head of the Chamber of Commerce of Scranton, Pennsylvania, and a business man from Seattle, Washington, as well as small business people from Chicago, Detroit and other sections. Generally speaking,

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the witnesses told straightforward stories of their difficulties and were, to my mind, reasonably persuasive. Many of them were ultimately able to obtain some credit from commercial credit banks, supply houses and the like, at an interest cost which ran from twelve to fifteen per cent, and in many cases higher. The witnesses were unanimous in believing that the Government should do something to help them, and a number of them spoke in favor of the Lead bill. Incidentally, several of them were quite definite in opposing the RFC as the insuring agency, taking the position that the RFC had not been able to do anything for them in the past, and that the FHA or some other more sympathetic agency would be preferable.

- White: I think your statement with respect to the issue is a little less than fair. I do think, if it is believed that private business can or will take up the slack, then obviously, there is no need, no room and no justification for any proposal such as Berle recommends. I think that is the issue. If you feel that they are not going to take up borrowing because the Government deters them or the opportunity is not there, then I think some alternative must be sought to put idle capital to work.
- H.M.Jr: Do you think this interest rate should be determined by the social need.
- White: He skips over that issue because it is extremely troublesome.
- H.M.Jr: No; but you?
- White: I would not state it that way. That is one of those "When did you stop beating your wife?" questions.
- H.M.Jr: What is there unfair about the statement?
- White: Wait a minute.
- H.M.Jr: Wait a minute. I am asking you.
- White: Yes.
- H.M.Jr: You say it is not fair, that when a man suggests that the interest rate be determined by the social

need, that is state socialism. What is the matter with that statement?

White: I do not know whether you and I mean the same thing by "socialism". I think you would understand me better if I were to state it in these terms, but I do feel that if the thesis is accepted that there is going to be an enormous amount of idle resources -- not being used for one reason or another -- that is justified by the Government promoting the use of those idle resources through, if necessary, lowering the rate of interest even down to zero.

Gaston: What the traffic will bear.

White: To what the traffic will bear. The assumption is that you will make it no higher than is absolutely necessary to take care of worthy projects and have worthy loans made; but I think it just rests on the preliminary assumption --

H.M.Jr: I cannot go along with you. I helped to organize the Farm Credit and we certainly have the best record of any agency in the matter of interest rates. I do not have to apologize for those interest rates. They have the same interest rate whether it is fifty or twenty-five hundred miles from New York. The idea in the Farm Credit was to make it attractive for the man that had a farm, and to help him put his place in such shape that he could run his farm profitably. We did not say to this fellow "Just because you have a business that does not pay, we are going to lend you money." Mr. Lenke wanted them to raise the money. We have been all through this thing of lowering interest rates, and helping him out through lowering the interest rates, and this present capitalistic system just won't stand up. Now, Mr. Lenke --

White: We are talking about two different things.

H.M.Jr: No, no.

White: I think so.

H.M.Jr: Keep lowering the interest rate.

White: We were talking about public bodies -- municipalities.

H.M.Jr: Lenke thinks about it a little differently than Mr. Berle -- to lend the money on

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mortgages and not charge any interest rates for rediscounting the mortgages, and everybody got excited about it because it was Mr. Lemke. Now that it is Mr. Berle, everybody thinks it is wonderful.

White: I think you are doing a little less than justice to the idea.

H.M.Jr: No. I have been sitting at a desk here and over there for six years, and maybe I see it a little more clearly than some people want me to see it.

Gaston: I think it would be interesting to look at the report of that committee that Gene Duffield talks about, the subcommittee of which Bill Myers was Chairman. It seems to me they came to the conclusion that we should go along with the present authority in the RFC, but if something more were ultimately found to be needed --

(Telephone conversation with the Secretary at 11:45 A. M. but it was not recorded)

- Gaston: What I was going to say was that committee proposed as their line of approach that they preferred at the time a cooperative industrial credit system on the pattern of the intermediate credit banks.
- H.M. Jr: Well, that makes sense.
- Gaston: That is what they proposed.
- H.M. Jr: That makes sense.
- Gaston: If they tried anything, they thought at the time that that would be the best line of approach.
- H.M. Jr: Preston, why don't you do this for me? Today is Thursday. Why don't you call a meeting and try to have something for us to begin to look at on Monday or Tuesday. Do you think that is a good idea, John?
- Banes: Yes.
- H.M. Jr: We have not the time to make surveys, but let us find out every suggestion that has been made as to what is needed, what is the ideal plan. I want this group to get it straight. From the little experience I have had, I do not think that the present bank setup -- I mean that the rules and regulations are deterrents to a bank in making a ten year loan, and I think they should be. I don't think banks should be in that business, as long as they have to keep so much of their assets liquid. I know from my own personal experience -- and I am talking about small needs -- it is very difficult. I had hoped that I should be able to take a position one way or the other -- not necessarily that nothing could be done, but to try it out on a section again, or try it out on the whole country, although I do not suppose that is feasible.
- Delano: How broad do you want this to be? Do you want us to go into the fundamental question?
- H.M. Jr: I want you to go into this thing with Viner and Hardy and this whole group that made a study of that whole section over in the Cleveland area -- wasn't it?
- Haas: And Chicago.
- H.M. Jr: There is a bank in Providence, Rhode Island, an

industrial bank -- you could find the name of it -- with five million dollars capital. That banker is a high class man, and his only business is making long term loans to industry. I do not know how successful he has been.

White: Maybe it would be possible to try this out in certain areas. There is no fundamental reason why you could not adopt that approach. You could select certain key places, confining it to people who were domiciled in that area, and take samples there. Of course, you could not try it out long enough to see whether the loans would be good.

H.M.Jr: Well, we have two agencies to do it, now, if we wanted to; but, as I say, I am interested in this thing. From my little experience, I know that there are cases. On the other hand, I know that people are also very unreasonable and not entitled to --

Delano: In lots of cases, it is a question of judgment.

H.M.Jr: We have not begun to do for the small industrialist what we have done for agriculture.

Delano: No; we have not begun to.

H.M.Jr: We have the basic principles set up for the credit, and still functioning successfully on a perfectly healthy basis, but we have not begun to do for industry what we have done for agriculture.

Delano: Yes.

H.M.Jr: The trouble is that at the RFC that is one of the many things that they have to do.

Delano: We would like to draw on the experience of the RFC.

H.M.Jr: You draw on whatever you can.

Delano: Certainly.

H.M.Jr: And come in on Monday or Tuesday again. I imagine this thing will go over. Why don't we set a time, even if we do not have the thing in final shape? Be here on Monday or Tuesday.

Delano: Yes; we will be here.

H.M.Jr: On this matter.

Delano: Yes.

H.M.Jr: Say Tuesday at eleven o'clock.

Delano: Yes. All right.

H.M.Jr: On bank loans.

Do you want to say something?

Hanes: I gave you a copy of the bill. I think Taylor handed me this copy.

Duffield: He turned his file over to me when he left. I do not have any extra copies, but if you want him to have a copy of it, I will see that he gets one.

H.M.Jr: I would like to say one other thing: On this Berle thing, if I understand it -- maybe I don't understand it; that is possible, but unless somebody connected with the Administration is bold enough to answer it, there is no reason to believe that he is not talking for the Administration. I do not like it any better than the Federal Reserve theory that we should examine banks in good times one way and in hard times another way. I do not think you can do it.

White: That is not comparable. That is not a fair analogy.

H.M.Jr: All right.

Upham: You think that is an unfair theory.

White: Yes; on this point.

H.M.Jr: I will let you have your holiday.

White: And I will wake up tomorrow with a sore head.

Upham: You have one now.

H.M.Jr: I am enjoying your criticism.

Gaston: Anyway, we want to put some whale's teeth in the Mead Act.

H.M.Jr: Harry expects to hear me say compare Berle and Lenke, except that Lenke is doing it in the farm

mortgage field and Berle in the industrial field.

White: I would like to divorce Berle and Lemke.

H.M. Jr: He is one of the most brilliant people in the country. He is a brilliant person. Look up Lemke's ideas on how to handle the farm mortgage situation.

White: I do not think it is any question of persons.

Delano: We will try to give you something, Mr. Secretary.

H.M. Jr: O.K., and be sure to let Harry sit in.

Delano: All right.

H.M. Jr: O.K.

Foley: Do you want to take up housing?

H.M. Jr: All right.

Delano: What is this?

Foley: Housing.

Delano: I thought we settled that.

H.M. Jr: Sit tight and be a good boy. (Mr. Foley handed a document to the Secretary.)

What is this?

Foley: This is the report on the Straus amendments to the United States Housing Authority Act. We have a letter -- the report originally was initialed in the Department and made available to Wagner, at his request, before it went up on the Hill, and Wagner has replied to the letter as it was originally written. The principal thing that he suggests now is a substitution of the provision in the bill as it was reported out by the Senate Committee insofar as underwriting the issues of the local housing authorities is concerned. This is what he suggests in lieu of the provision in the bill that just wipes out the ten per cent and permits national banks to underwrite the entire issue.

"The limitations and restrictions herein contained as to dealing in, underwriting and purchasing for its own account investment securities shall not apply to such obligations of any public housing agency (as defined in Section 2 (11) of the United States Housing Act of 1937, as amended) as are secured by a pledge of payments under an annual contributions contract between such agency and the United States Housing Authority!" --

And this is the new language.

"Provided that the Comptroller of the Currency may by regulation prescribe prohibitions limitations and restrictions as to such dealing in, underwriting and purchasing of such obligations."

Then he goes on to say:

"You will note that this provision would make it entirely discretionary with the Comptroller of the Currency by regulation to prohibit, limit, or restrict dealings in, underwriting and purchasing of local authority obligations. As a matter of fact, under this proposal the Comptroller could prohibit any underwriting of local authority obligations or he could allow underwriting subject to such limitations as he saw fit. I have every confidence in the administration of this provision by the Comptroller of the Currency and would be entirely satisfied to have the matter rest within his sole discretion."

Delano: Who says that?

Foley: Senator Wagner.

"What I am anxious to avoid is the inflexibility which proceeds from the existing language of Section 5136 and the time that would necessarily be consumed in obtaining amendments to it authorizing the purchase and underwriting of public housing agencies' bonds to the extent that such action may appear proper from time to time. This proposed substitute provision would provide the necessary flexibility to meet varying conditions as they arise."

Then he goes on and says further:

"I would like to know how you feel about the suggestion I am making in order to avoid any disagreement between us about a matter which I feel is so vitally important to the housing program and business recovery."

He also said that while this bill has been reported out, he thinks he could effect this change, as Chairman of the Committee, before it is put on the Floor.

I think that is even worse than the other one, because it puts the pressure right on you.

Delano: Yes; it puts us into a field we are not competent to be in. I would say that very definitely, but I am giving you a horseback opinion.

H.M. Jr: All right. When is that dated?

Foley: The 25th of May.

H.M. Jr: We ought to answer that, not later than tomorrow.

Delano: I never heard of it.

H.M. Jr: Can you get me up an answer by noon tomorrow?

Foley: Surely.

H.M. Jr: With the help of the Comptroller.

Foley: This group?

H.M. Jr: This group. Get me the answer by noon, after we get these things straightened out. It is nothing about whether the bill should or should not be passed?

Foley: That is right.

H.M. Jr: I would like to get the record, I would like to see the bill itself.

Delano: Mr. Secretary, expressing a more dispassionate opinion, it seems to me that this would put us in a very unfortunate position.

H.M. Jr: I may not have or I may have, but I would like to see the United States Housing get an extension of their authority. I would like to see them get an

extension of their authority.

Delano: I am not expressing an opinion on that. I have expressed my opinion about it.

H.M.Jr: I would like your help and advice.

Foley: Here is the letter, Mr. Secretary, which has been initialed by everybody, and here are the changes that we made yesterday. At your suggestion we added this paragraph.

H.M.Jr: Let the Comptroller see it.

Foley: Everybody has seen it.

Delano: I guess I will have to ask Mr. Upham. Is that what you were talking with me about?

Upham: Yes.

Delano: I did not understand it.

Foley: I did not know anything about it until Dan Bell showed it to me this morning when I came into the nine-thirty meeting. I do not think that has anything to do with this. If we are still opposed to the suggestion there, then I think we can report on the Wagner bill, and we can independently indicate to Wagner our feeling with respect to the first suggestion so I do not think this letter has to be changed by virtue of this letter. This was added, Mr. Secretary: "Although the Treasury is sympathetic" etc.

We also recognized, with the exception of Section 4, which is this underwriting provision, that it had to be enacted.

H.M.Jr: I will write this and send it over. You can rewrite it and get it to me.

Foley: It is all ready. I will just erase these things that I wrote on there to show you what I added.

H.M.Jr: Give it to Mrs. Klotz, will you?

Foley: Yes.

H.M.Jr: All right. Is everybody happy now?

Delano: You not only want a report on the Mead bill, but you want something from us on the whole problem?

H.M.Jr: The problem of the man who needs additional working capital. Can he get it under the present system, as it is set up? I mean, is it available, and can he get it? If not, why not, and what can we do about it? I feel there is a great big gap in our industrial system, as far as getting the money to these fellows is concerned. I repeat -- I do not believe the job has been done in the industrial field as it has been on the farm. If the farmer wants it, he can get it through the Farm Credit or through his bank, and he can get it at reasonable rates -- all kinds of credit.

Delano: Yes.

H.M.Jr: Thank you very much.

Foley: Here is one more thing, Mr. Secretary. Maybe you do not want to take it up now.

H.M.Jr: I never should have promoted it.

Foley: In regard to this whole discussion. This pertains to the bill that the President asked you to discuss with him. Now, it has been here for some time, and I have a memorandum here --

H.M.Jr: Has that anything to do with banking?

Foley: Well, I think it has. It involves financing, and it is, in substance, one of Berle's proposals before the Wagner committee. We are against it.

H.M.Jr: Well, let Mr. Delano and his group take a look at it.

Foley: O.K.

H.M.Jr: That gives me leeway.

Delano: I will be here on Tuesday morning.

H.M.Jr: Yes. Thank you very much. You do not mind, do you?

Delano: No; I will be very glad to, Mr. Secretary.

(Conference concluded at 12:05 o'clock P. M.)

June 1, 1939

Secretary Morgenthau

Mr. Foley

With further reference to Senator Norris' amendment to our bill to amend the Second Liberty Bond Act (H.R. 5748) which the Senate adopted this afternoon when it passed our bill by a vote of 44 to 23 -

Under existing law the TVA is authorized to issue, for general TVA purposes, 100 million dollars in bonds, one-half of which are authorized to be issued "on the credit of the United States", while the other half are "fully and unconditionally guaranteed both as to interest and principal by the United States". The TVA law also provides that any bonds issued under it shall have all the rights and privileges accorded to Panama Canal bonds, which means that they are fully tax exempt and have the circulation privilege.

Norris' amendment would combine the two authorizations into one authorization to issue bonds not to exceed in the aggregate 100 million dollars; would eliminate the provision of the TVA Act which accords to its bonds the rights and privileges accorded to Panama Canal bonds; and would eliminate the expression "on the credit of the United States", by providing that all bonds issued under the TVA Act would be fully and unconditionally guaranteed both as to interest and principal by the United States.

On May 23, 1939 we submitted a favorable report on the fiscal aspects of S. 1796 (which is identical with the Norris Amendment) to the Chairman of the House Committee on Military Affairs; however, we called attention to the fact that such bill would require approval by the Federal Power Commission of the purpose for which the funds derived from the sale of bonds could be used prior to their issuance, and suggested that it might be better to substitute for such provision one which would permit issuance of the bonds without such approval but restrict the use of the proceeds to purposes approved by the Federal Power Commission. A copy of S. 1796 is attached.

(Initialed) E. H. P., Jr.

LJB:ip

TREASURY DEPARTMENT

118

INTER OFFICE COMMUNICATION

DATE June 1, 1939

TO Mrs. Klots

FROM Mr. Blough

RB

This is the Secretary's original which he took to the White House on May 25th. The marks and comments include those made by the Secretary at that time, with the following exceptions:

- 5/24 draft*
- (1) Suggestions that Mr. Hanes made by blue brackets on pages 9, 11 and 16.
 - (2) Deletions made by the Secretary on pages 5, 6 and 8 at the conference with Congressional leaders, Friday afternoon, May 26.
 - (3) Revisions in preparing the next draft: the word "that" inserted on page 6. The word "elsewhere" deleted on page 9. The words "one of the objectives" substituted for the words "the end" on page 11. The words "enacted in 1933" deleted on page 12. The word "an" substituted for the word "another" on page 13. The words "of the tax burden between broad groups of taxpayers and especially should" inserted on page 14. The next word "nor" changed to "not" on page 14.

This material is submitted as requested by the Secretary.

May 24, 1939

I appreciate this opportunity to appear before your Committee to discuss with you certain broad fiscal problems and certain specific tax questions.

Tax proposals cannot be discussed comprehensively except in relationship to our whole 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 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

- 2 -

and of national income, that the change promotes and does not retard business recovery, and that the change makes easier and not more difficult progress toward the 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 military expenditures, 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 these developments present the danger that they may involve us in increased cost for national defense here and that they may result in monetary instability abroad and disruption of our commerce, 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.

- 3 -

No proper solution of any major problem facing this government today can be achieved without full consideration of the impact on our country of the present international crisis. The unmistakable implication of the international situation is that we should give serious attention 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 in each specific year any more than in 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 assume 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 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 state 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 both to what the nation needs and to what the nation can afford.

In my opinion the fundamental fiscal question raised by the pending Department of Agriculture appropriation bill is precisely the type of question with which this joint committee should concern itself. This bill proposes to increase budgeted expenditures for farm parity payments by \$372,000,000 but no provision has been made for a compensating increase in revenue although we already face a deficit of \$3,426,000,000 in the coming fiscal year. The bill, upon the merits of which I am not commenting, is

- 6 -

typical of scores of others which seem to me to present questions appropriate for consideration by a joint committee which looks at each proposed expenditure and each proposed revenue measure as a part of an integrated budget policy.

This committee should 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 in this work to the full extent that the Committee desired.

Thus far I have dealt with the financial problems of the Federal Government alone. We must remember, however, ^{that} with the best conceivable Federal fiscal plan in operation, 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.

In the last five years we have given serious study to the problems created by Federal-State tax conflicts. The same problems had been recognized by our predecessors. It is my belief that we should take steps without delay to make these studies effective. I suggest that Congress create a small temporary national commission to report to Congress as soon as

- 7 -

feasible on the various aspects of intergovernmental fiscal policy and propose a plan for the solution of the problems involved. Such a commission should be made up of men of ability who command the highest possible public confidence, who are familiar with fiscal problems, but who will represent the public at large rather than particular governmental units.

Overlapping and competing 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 this fiscal situation are increasingly unsatisfactory to both state and municipal governments and to the Federal Government, and more and more burdensome to taxpayers. The recommendations 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 fiscal matters of great importance. Let me turn now to more specific questions of Federal taxation.

I desire first to reiterate two tax recommendations which the President has already made and various suggestions which the Treasury has previously presented:

- 8 -

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 in June and July, and 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 interest on all 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. During hearings before this Committee in 1937 and 1938 representatives of the Treasury Department brought to your attention several changes in the tax laws upon which Congress has not yet acted. Of these the principal ones are (a) curtailment of excessive deductions now allowed for depletion of oil and gas wells and certain mines, (b) elimination of the preferred

income tax status enjoyed by residents of the eight community property states and (c) integration of the estate and gift taxes.

Even though a comprehensive revision of the tax structure probably will not be feasible at this time that fact, in my opinion, should not restrain your Committee from giving serious attention at this time to removing from the tax laws any manifest inequities or other defects.

Before specifying the tax provisions which I believe deserve your special attention at this time I wish to emphasize the importance of maintaining the present revenue in any tax revisions which may be made. 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 be offset by tax increases, ~~elimination~~~~ If tax revision were confined to tax reductions the resulting uncertainty as to our future fiscal position would injure and not help business. We should take no step which the public may interpret as moving away from the objective of a balanced budget.

In discussing the elements or features of the tax system which you may wish to reexamine, I should like to classify them roughly into three groups.

The first group includes features which have been characterized as likely to hinder business expansion and investment.

One such feature is the absence of provision in our income tax laws for carrying over net business losses to be deducted from business profits of future years. The profits or losses of each year are considered without reference to those of any other year. In consequence a business with alternating profit and loss now pays higher taxes over a period of years than does a business with stable profits although the average income of the two firms may be equal. New enterprises and the capital goods industries are especially subject to wide fluctuations in earnings.

Average
Year
61.6
Loss

As a second example, I should also like to mention the questions of tax-exempt securities and surtax rates in the higher brackets. These two questions should be considered together. Tax exemption of securities is highly inequitable and tends to nullify our progressive surtax rates. Most persons subject to the high surtaxes have sizable holdings of governmental securities which yield them an income free from Federal income taxation, while other persons entirely escape the high surtaxes in this manner. Tax exemption also operates as a magnet which

Ultimately
179 to
337
Gain
Added
Federal
Interest
Cost
19 to 50

pulls persons subject to high income taxes away from investments in private business. We should by all means pass legislation to make it impossible in the future to issue any more tax-exempt securities.

This having been accomplished first, it would then be fair and logical to reexamine the question of whether the present surtax rates on very large incomes may not be so high that they discourage the limited number of individuals subject to them from taking normal business risks.

Lowering to 60%
11.5
Loss
Immediate

In a second group are features of our tax system which have been referred to as "tax irritants". As an example I would mention the undistributed profits tax. In its present form, this tax is unimportant and does not accomplish the objectives of the original proposal. The tax produces little revenue and has little effect on business. It has acquired prominence as a psychological irritant, [largely because of the widespread and emotional criticism which has been directed against it.] ^{one of the objectives} ~~The end~~ which the law sought to attain was to prevent the retention and accumulation of earnings by corporations from being used to avoid the personal income tax. This is still an important, and to my mind, a sound objective. The law in its present form does not attain it. Since the income tax

1939
Basis
17.5
Loss

on corporations, of which the undistributed profits tax is a minor segment, expires by its own terms at the end of this year, your Committee should deal with this problem. The Treasury, of course, stands ready to work with you on it.

Another example is found in the capital stock tax and the related excess profits tax, enacted in 1938. 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. Their major defect 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. 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.

1939	
Basis	
<u>123.4</u>	
Loss	
<hr/>	
Average	
Year	
Basis	
<u>147.7</u>	
Loss	
<hr/>	

There is a third category of tax problems now being widely discussed which raises questions of tax equity. The Treasury has already worked on those problems and, if your Committee desires, our staff could continue these studies in collaboration with the Committee, possibly with a view to action at a later session.

out
out
An example is the double taxation of corporate dividends paid to individuals. Under the present law corporations pay the normal corporate tax on their earnings. When these earnings are distributed to the individual stockholder they are subject to both the individual normal tax and to the surtax.

Dividend
Exemption

1939
Basis
90.2
Loss
Average
Year
98.9
Loss

an
Another example is the limitation now placed on the deduction of corporation capital losses. 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.

1939 Basis
65.2
Loss
Average
Year
71.4
Loss

In the consideration of many of the possible tax changes just mentioned, it is essential to bear in mind that their adoption would result in a reduction in the revenue-producing capacity of the tax system. I have already emphasized the importance of not permitting the revenue-producing power of the tax system to be reduced at this time. Accordingly, with

Passed
added
by RB

of the tax burden
to taxers
broad groups
of taxpayers
and equitably
should

They should not
change the relative
132
distributions
not place
additional
burden
upon
consumers

the adoption of any of the above measures involving loss of revenue there should be associated revenue-producing revisions. Although this problem is difficult, it is one that must be faced. The taxes resorted to for replacing any lost revenues 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, with due allowance for corporations with small incomes.

2. A second possible source of additional revenue is the individual income tax. There is merit to the suggestion that the rates on incomes between the \$7500 and \$75,000 levels could be increased without inequity or material deterrent effects. Furthermore, to promote wholesome tax consciousness and good citizenship, the personal and family exemptions might well be decreased. At the present time only about 3,000,000 persons pay income taxes. If the exemption for individuals were decreased from \$1,000 to \$800 and the exemption for married couples decreased from \$2,500 to \$2,000, it is estimated that an additional 1,500,000 persons would be subject to the income tax. The rates imposed on small

56.4
Gain

- 15 -

incomes could be low with perhaps a small minimum tax. Even though the tax imposed on small incomes were of little importance from the revenue point of view, the tax would constitute a valuable instrument for making a larger group of our citizens directly aware of the Federal tax problem.

3. Estate and gift taxes could be increased. Although high rates are applied to extremely large estates the great majority of the estates pay little or no tax. The exemption and the insurance allowance could be reduced and rates in the lower and middle brackets could be increased. Furthermore, as previously suggested consideration might well be given to the possibility of combining the estate and gift taxes into one consolidated tax. At the present time a person with a large volume of property who is in position to give much of it away during life can reduce his total tax far below that which must be paid on the estate of a person who is not in position to give away his property during life.

In connection with all of the matters I have mentioned the Treasury is prepared as usual to furnish further information and will be happy to work with you to the extent that you desire.

Coordination
with one
\$40,000
exemption
23.7 to 70.2
Gain
Eventual

The subjects I have discussed are for the most part confined to a limited segment of the tax system. I do not consider them as constituting an adequate program of tax revision. Such a program can be developed only through long continued study and it cannot be static but must be adapted to changing conditions. But the general lines along which Federal taxation should develop in the future appear to be quite clear. We ought to increase the part played by direct taxes that can be made to take account of differences in the abilities of individuals to support Government. This means that we should endeavor eventually to minimize the use of manufacturers' excises and other commodity taxes which tend to be shifted directly to consumers, [transferring the burden as far as practical to the individual income tax and the estate and gift taxes.] Such revisions would facilitate coordination of Federal with State and local taxation. //

In conclusion, permit me to say that one of the major tasks we have before us is to do everything we can to promote lasting business recovery. With this still uppermost in my mind I would like to repeat now with the same deep conviction what I said in

November, 1937: "The basic need today is to foster the full application of the driving force of private capital. We want to see capital go into the productive channels of private industry. We want to see private business expand."

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Berlin, Germany

DATE: June 1, 1939, 11 a.m.

NO.: 429

CONFIDENTIAL.



It appears that the German Government had assurances from the British Government several weeks ago that no objection would be raised to withdrawal by the Bank for International Settlements of six million pounds which it had on deposit in London for the account of the Czech National Bank and turning it over to the control of the Reichsbank. [Reference is made to telegram No. 378 of April 24, 11 a.m., from the Embassy.]

A fortnight ago a German commission went to London to try to negotiate the release of the Czech balances which Great Britain has blocked, and this commission has returned to Berlin. The commission did not reach an agreement, but arrangements were made that a delegation will return to London later. It seems clearly understood that before the end of June an agreement will be reached.

The British informed the German delegation that British claims had to be met within a fortnight or so or Great Britain would use the impounded balances and unilaterally pay these claims. A delay was requested by the German delegation until the thirtieth of June, and in return for the delay they agreed that the May (installment?) of the 7-1/2 percent Prague sterling loan would be remitted

in

in full.

It is our understanding that the British Government still has blocked some 14-1/4 million pounds of Czech gold and balances, which is more than enough to meet present claims of the British. The British do not expect to have any difficulty in getting the Germans to agree with the British Treasury to pay back to itself the six million pounds which it loaned to the Czech Government after the Conference at Munich since the funds are held by the British. Nor do they expect difficulty in getting permission to pay out to refugees from Czechoslovakia some 3,250,000 pounds which had been remitted to England for safe-keeping. It is figured that at the present time the cash claims of British creditors amount to only 3 1/2 million pounds, whereas after repayment of the credit to the Czechoslovak Government and the "refugee funds" about 5,000,000 pounds will still be blocked. It is the German desire that the balance of 1 1/2 million pounds be returned to the Czechoslovak, that is, the German exchange control. However, the British expect successfully to insist that the balance be used to buy up and retire part of the Czech sterling long term bonds which are outstanding. It is understood

- 3 -

understood also that the British will insist on full transfer of the interest on long term Czech obligations which are held in England, the dividends on British-held shares of Czech business enterprises, and the earnings on British direct investments in the protectorate.

It is requested that this telegram be repeated to the Treasury as Heath's No. 32.

KIRK.

EA:LWW

REB

GRAY

London

Dated June 1, 1939

Rec'd 1:55 p. m.

Secretary of State,
Washington.

761, June 1, 6 p. m.

FOR TREASURY FROM BUTTERWORTH.

Due to the accumulation of funds for today's war loan dividend payment and the continued excess of Treasury bill payments over maturities this week's Bank of England return shows another switch from bankers' deposits which decreased by pound 12.9 million into public deposits which increased by pounds 12.8 million. Note circulation at pounds 499.8 million showed an increase on the week of pounds 5.2 million due largely to month end requirements while holiday currency has not yet returned from circulation.

The hitch in the Russian negotiations seems to have checked the slightly increased activity in the foreign exchange market of yesterday and there was little business today, the British fund dealing in neither the spot nor forward dollars. 117 bars of gold were sold at fixing, 27 of which were married, the Bank of England giving a few. Samuel Montagu was again the sole buyer.

The

REB

2-#761, From London, June 1, 6p.m.

The guilder was offered today the rate going from 8.71 to 74-1/2 on a reaction from the completion of the purchase of guilders in Paris for the repayment of the Mandelsohn loan. The Bank of France bought a few dollars today at 37.73-7/8.

KENNEDY

HPD

RECEIVED

JUN 2 1938

TREASURY DEPARTMENT
Office of the Secretary
Federal Reserve Bank of New York

MA

GRAY

Paris

Dated June 1, 1939

Rec'd 2 p.m.

Secretary of State

Washington

1047, June 1, 4 p. m. (SECTION ONE)
FOR THE TREASURY.

Trading on the exchange market was on a restricted scale and without special features except that the florin was offered on rumors of a cabinet crisis in Holland. The security market was depressed and showed moderate losses all around.

The Bank of France statement dated May 25 published today reveals an increase of 600 million francs in the commercial portfolio. Note circulation down 741 millions. Deposits up 419 millions. The ratio of gold cover is 64.28 compared with 64.14.

(End Section One)

BULLITT

KLP:DDM

JR

GRAY

Paris

Dated June 1, 1939

Rec'd 1:15 p.m.

Secretary of State,
Washington.

1047, June 1, 4 p.m. (SECTION TWO).

AGENCE ECONOMIC editorially reviews recent developments relating to the Czech gold in London. In its view the Bank of England could not have refused delivery under the circumstances but vigorously questions and blames the action taken by the B.I.S. It ridicules the statements made to its Basel correspondent by Beyen (see my telegram No. 1038 of May 31st) and observes that the position taken by the B.I.S. that it was not called upon to consider the question of the annexation of Czechoslovakia by Germany does not hold water pointing out in this respect that in the last report of the Basel institution it is recorded that the attribution of the voting rights attached to the shares of the B.I.S. issued in Czechoslovakia had not yet been settled. AGENCE ECONOMIC therefore expresses astonishment that a decision could be taken as concerns the gold.

BULLITT

RR:DDM

REB

GRAY

Paris

Dated June 1, 1939

Rec'd 1:45 p. m.

Secretary of State,
Washington.

1047, June 1, 4 p. m. (SECTION THREE)

That the B. I. S. was organized principally to serve as trustee in the settlement of international payments, and notably as concerns the payment of the reparation annuities, the editorial concludes that the B. I. S. has outlived its usefulness.

Pertinax expresses similar views in a lengthy article published in L' ORDRE. This writer invites attention to the investments of the B. I. S. in Germany and the advantages which Germany has drawn from the bank.

Generally speaking apart from the comment of AGENCE ECONOMIQUE and Pertinax the French press has confined itself to reproducing the statements which have appeared in the London newspapers regarding the Czech gold question and has refrained from taking a position for or against the B. I. S.

(END MESSAGE)

KLP
DDM

RECEIVED

BULLITT

JUN 3 1939

TREASURY DEPARTMENT
Office of the Secretary
General Account of the Secretary

PARTIAL PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Rome, Italy

DATE: June 1, 1939, noon

NO.: 211

Reference is made to telegram No. 42 of May 24 from the Department.

On May 26 I communicated the substance of your telegram to Ciano, who did not appear to be interested in the least. He admitted frankly that he knew nothing about the matter. Then I had the Commercial Attaché make arrangements to see the Minister of Foreign Trade and Exchange and to hand him a copy of the aide memoire which I had given to Ciano. Yesterday Livengood did so, and I give below the following report of his conversation with Minister Guarnieri:

"Professor Guarnieri after reading the paper carefully asked me to thank the Ambassador for his courtesy which he much appreciated. He characterized as 'very useful' the exposition which showed that in connection with the question of possible countervailing duties no policy of singling out Italy was involved. He added that a telegram was being sent the Italian Embassy in Washington. Italy would have no objections to investigations

-2- #211, June 1, noon, from Rome.

investigations being made by the United States Treasury Department regarding Italy's aids to exportation.

Referring to silk he said that while Italy paid a guaranteed price on cocoons in order to sustain the industry, the Italian exporters sold abroad at world market prices not at dumping prices. He said that knowing thoroughly as he did Italy's export practices he could declare from the depths of his own conscience that Italy was not exporting anything to the United States at dumping prices.

He said that he regretted that at a time when conditions were as difficult as they are at present new complications might be presented by the United States, a country which he remarked was understood to be either contemplating or practicing a policy of giving what amounted to export bounties on wheat and cotton.

Before any action is taken by the United States in the matter of imposing countervailing duties he said Italy's situation and result which would have to follow should be thoughtfully considered. He continued in substantially the following words: 'if it is made impossible for us to export to the United States I must say with all frankness that we shall not be able to admit American merchandise and

our

-3- #211, June 1, noon, from Rome.

our position will be such that we shall not be able to continue to pay credits due to the United States--credits which up to now we have been scrupulously paying, whatever the sacrifices involved'.

'Italy values very highly its trade relations with the United States' he said. He was the only person he added who knew the full extent of the sacrifices which had been made to meet Italy's obligations to that country. It had been hoped that an accord for improving trade relations between the two countries would become possible.

Continuing, he said that if the American officials would put themselves in his position they would see that he could not import from the United States unless he had means for payment, and this he could not have without exporting--exporting at world prices; for, he repeated 'Italy is not exporting at dumping prices'.

At the close of the conversation he said again that he was glad that the aide memoire had been furnished, that it was very useful and that there would be no objection to investigations of the Treasury Department".

PHILLIPS

CSB

JR

GRAY

London

Dated June 2, 1939

Rec'd 1:10 p.m.

Secretary of State,
Washington.

768, June 2, 6 p.m.

FOR TREASURY FROM BUTTERWORTH.

One. The attitude of the American brokers, as set forth in my No. 720 of May 20, 1 p.m., has been put before the Bank of England. When it was argued by the representatives of the American brokerage houses that switches, which in essence are designed to improve the quantity of British holdings of foreign securities, were wholly desirable from the British Government's point of view the Bank of England did not interpose any objection to such transactions. But the Bank of England would not accept the definition of the prohibition as applying only to transactions resulting in the transfer of funds across the exchanges and therefore it did not give its approval to the investment in American securities of dollar balances already in New York. The Bank of England also insisted that circulars be drastically modified and a committee of the American brokerage houses in London is now attempting to effect a working arrangement.

The

-2- #768, June 2, 6 p.m., from London.

The representatives of the American brokerage houses who have carried on these discussions with the Bank of England are left with the impression which is no doubt correct that the British monetary authorities (a) are anxious to prevent the flow of sterling funds into American securities and (b) are furthermore desirous of taking back some (repeat some) British capital repatriation.

Two. The foreign exchange market was again quiet today with the dollar slightly more offered and the British fund gaining a few dollars at 468-3/8. 104 bars of gold were sold, three of which were married and 30 supplied by the British fund. Samuel Montagu took most of the gold.

KENNEDY

CSB

RECEIVED
JUN 3 1939
TREASURY DEPARTMENT
Office of the Secretary
Treasury Building at the Department

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris

DATE: June 2, 5 p.m., 1939

NO.: 1056

FOR THE TREASURY DEPARTMENT

Official announcement was made last evening that the proceeds of the five percent loan issued May 15 and closed May 25 totalled 10,646 million francs in nominal capital. Of this amount 4,612 millions represented conversions and 6,034 millions represented cash subscriptions. (Reference my No. 1025 of May 27).

Business was dull and almost devoid of interest on the exchange market. Again the florin lost ground. It seems that offers of this currency are due in part to the continuation of reports of disagreement in the Dutch Cabinet and to the recall by the Paris market of some funds from Amsterdam which have been released by the amortization of French Treasury Bonds which have come to maturity.

EA:DJW

RECEIVED

JUN 2 1939

THE TREASURY DEPARTMENT
 RECEIVED JUN 2 1939
 TELETYPE UNIT

Handwritten: Rome



DEPARTMENT OF STATE
WASHINGTON

June 2, 1939.

My dear Mr. Secretary:

I enclose for your confidential information one copy of a telegram sent to the American Embassy, Rome, on May 24, and a copy of the Embassy's telegram of June 1, replying thereto, with regard to the application of countervailing duties to certain Italian products.

Sincerely yours,

Handwritten: Herbert Feis

Herbert Feis,
Adviser on International
Economic Affairs.

Enclosures:

No. 42 of May 24 to
Rome.

No. 211 of June 1 from
Rome (partial paraphrase).

The Honorable

Henry Morgenthau, Jr.,

Secretary of the Treasury.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE June 2, 1939

TO Secretary Morgenthau
FROM Mr. Foley

For your information.

Further hearings were held today by the Subcommittee of the Senate Committee on Banking and Currency which is considering the Mead bill.

Jerome Frank of the Securities and Exchange Commission, speaking as an individual and not as a representative of the Commission, testified in favor of the bill. He stated that there is a distinct need for supplying small business enterprises with a means of obtaining capital. While making it clear that he was in no way criticizing either investment or commercial bankers, he stated that it is impossible for investment bankers to underwrite issues of less than \$1,000,000 except at rates which are prohibitive to the borrowers and that for very good reasons, it is not now the practice of the commercial banking community to make capital loans. He also stated that the proposed bill is an important step in meeting the capital needs of small business enterprises, and that although the eventual establishment of a system of regional industrial banks which would supply capital to business enterprises is desirable, the enactment of the necessary legislation would involve considerable preliminary study by the Congress, and therefore the Mead bill should be enacted at this session.

Ernest G. Draper, a member of the Board of Governors of the Federal Reserve System, stated his personal views concerning the proposed

- 2 -

legislation. He expressed general approval of the Mead bill, but suggested that it be revised in certain respects. It is his belief that banks should be insured against all loss resulting from loans made for business purposes rather than only for the loss in excess of 10% of the amount of the loan as is provided by the bill as now drafted because insurance limited to 90% of the loan might not afford sufficient protection to encourage banks to make loans. He further suggested that a separate title be added to the bill which would liberalize the provisions of section 13b of the Federal Reserve Act which concerns the granting of loans for industrial or commercial purposes by the Federal Reserve banks - the proposed addition not to be a substitute for the Mead bill, but a supplement to it.

Further hearings will be held Monday, June 5th, at which time Chairman Eccles of the Board of Governors of the Federal Reserve System is scheduled to testify. Jesse Jones of the Reconstruction Finance Corporation, who was scheduled to testify this morning, but did not appear, is also scheduled to testify Monday.

E. W. F. H.

JUN 2 1939

MEMORANDUM FOR THE PRESIDENT:

I am returning herewith the letter addressed to you by Senators Van Nuys and Minton recommending the appointment of Mr. Pleas E. Greenlee of Shelbyville, Indiana, as Collector of Internal Revenue for the State of Indiana to succeed the present Collector, Mr. Will H. Smith.

Collector Smith was appointed during your Administration and has made an outstanding record in the performance of the duties of his office. The Commissioner of Internal Revenue urgently requests that Collector Smith be permitted to retain his present position, and has stated that to replace him would have a demoralizing effect on that Service. I agree with Commissioner Helvering.

Faithfully yours,

(Signed) H. Morgenthau, Jr.

File
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June 2, 1939

COMMENTS ON THE BERLE PROPOSALS

Berle's objective is to find means of stimulating the volume of both private and public investment, since he believes that under existing conditions a sufficient volume of private investment to insure full and continuous employment will not be forthcoming. There is no quarrel with this analysis or with this objective.

Specifically he proposes (a) that a Public Works Finance Corporation be set up for the purpose of financing Federal self-liquidating projects and non-Federal public works at a nominal rate of interest, the funds to be obtained through rediscounting with the Federal Reserve; (b) that loans to small businesses be insured; and (c) that new types of capital credit banks be established to provide capital for enterprises both private and public. Capital funds for private enterprises might be obtained through the sale of debentures; funds for public enterprises "through the creation of reserve credit".

Evidence is steadily accumulating in support of Berle's contention that under conditions prevailing since 1929 and in the foreseeable future there is need for a substantial continuing volume of public investment, and that such volume, so far as non-Federal public bodies are concerned, will probably not be forthcoming without special inducements. There are various ways of providing such inducements: they could take the form of (1) virtually interest free loans, as Berle proposes, or (2) of a grant of principal, as is done in effect at present, or (3) of an annual subsidy by the Government to assist in servicing new municipal borrowings, as is done

in the U.S.H.A.

While interest free loans through a Public Works Finance Corporation have the merit of insuring a continuing program financed outside the Federal budget, they entail very unequal subsidies and commitments, depending on the varying maturities of loans. It would appear preferable to provide the subsidy by contributing a percentage of the interest and amortization charges.

The major defect of Berle's proposal, however, is that he proposes to reduce or abolish interest rates for the necessary stimulation of investment by directing the Federal Reserve banks to create money for the purpose. That is an indirect money-printing scheme. It would enormously intensify the problem of excess reserves without increasing the system's ability to handle the problem, and would constitute a precedent for borrowing from the Federal Reserve for all sorts of purposes. It would result in a collapse of the system. This method of raising funds is not really essential to Berle's proposal, and could be replaced by the issue of short-term guaranteed obligations and an annual contribution by the Federal Government.

The proposal to insure capital loans to small businesses needs is desirable and is under consideration in pending legislation.

Berle's other proposal is to establish a system of capital credit banks. He states that this suggestion merits study and does not work out the details. Since (1) pending proposals for the insurance of loans and for the establishment of industrial credit banks would meet the requirements of small businesses, (2) the public investment needs would be taken care of by Berle's first proposal if it were properly modified, and (3) large-scale

private business has little difficulty in obtaining all the capital it is willing to solicit, it would seem that the proposed new capital credit banks would be superfluous.

Incidentally Berle makes some rather startling statements to the effect that commercial banks do not need nor are entitled to make a profit. In this connection he was apparently under the impression that the "creation of money" is costless. Elsewhere, however, he concedes the necessity of covering expenses, and he does not propose that existing banks should make loans at other than "commercial rates of interest". While, therefore, some of his statements are, to say the least, injudicious, actually he is not proposing to decrease bank earnings.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE JUN 2 1939

File
157

TO Secretary Morgenthau
FROM Mr. Foley

With reference to legislation dealing with Export-Import Bank loans to Latin-America alternative drafts have been prepared and are attached hereto as follows:

- (1) A bill which would simply increase the amount of funds which may be loaned by the Export-Import Bank of Washington for the purpose of aiding in the financing and facilitating of exports and imports and the exchange of commodities between the United States and Latin-American countries.
- (2) A bill which would set up a separate Latin-American Export-Import Bank to make Latin-American loans. The provisions of this legislation have been modelled on the RFC Act.

F. H. F.

A BILL

Relating to the lending operations of
the Export-Import Bank of Washington.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 9 of the Act approved January 31, 1935 (49 Stat. 4), as amended, is hereby further amended by changing the proviso at the end thereof to read as follows: "Provided further, That the Export-Import Bank of Washington shall not have outstanding at any one time loans or other obligations to it in excess of \$ (not more than \$ of which shall consist of loans or obligations made or incurred primarily for purposes other than the purpose of aiding in the financing and facilitating of exports and imports and the exchange of commodities between the United States and any of its territories and insular possessions and the countries of Latin America or agencies or nationals thereof), the capital for which the Reconstruction Finance Corporation, when requested by the Secretary of the Treasury with the approval of the President, may continue to supply from time to time through loans or by subscription to preferred stock".

A BILL

To create the Latin-American Export-Import Bank.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That there is hereby created a body corporate with the name "Latin-American Export-Import Bank" (hereinafter called "the bank") the administration of which shall be subject to the supervision of the Federal Loan Administrator. The principal office of the bank shall be located in the District of Columbia, but there may be established agencies or branch offices under rules and regulations prescribed by the board of directors. This Act may be cited as the "Latin-American Export-Import Bank Act".

SEC. 2. The bank shall have a capital stock of \$ _____, subscribed by the United States of America, payment for which shall be subject to call in whole or in part by the board of directors of the bank. There is hereby authorized to be appropriated, out of any money in the Treasury not otherwise appropriated, the sum of \$ _____ for the purpose of making payments upon such subscription when called. Receipts for payments by the United States of America for or on account of such stock shall be issued by the corporation to the Secretary of the Treasury and shall be evidence of stock ownership of the United States of America.

SEC. 3. The management of the bank shall be vested in a board of directors consisting of five persons appointed by the President of the United States. Before entering upon his duties each of the directors so appointed and each officer of the bank shall take an oath faithfully to discharge the duties of his office. Nothing contained in this or in any

other Act shall be construed to prevent the appointment and compensation as an employee of the bank of any officer or employee of the United States in any board, commission, independent establishment, or executive department thereof. The terms of the directors appointed by the President of the United States shall be two years and run from the date of the enactment hereof and until their successors are appointed and qualified. Whenever a vacancy shall occur among the directors so appointed, the person appointed to fill such vacancy shall hold office for the unexpired portion of the term of the director whose place he is selected to fill. The directors of the bank appointed as hereinbefore provided shall receive salaries at the rate of \$ per annum each. No director, officer, attorney, agent, or employee of the bank shall in any manner, directly or indirectly, participate in the deliberation upon or the determination of any question affecting his personal interests, or the interests of any corporation, partnership, or association in which he is directly or indirectly interested.

SEC. 4. The bank shall have succession for a period of ten years from the date of the enactment hereof, unless it is sooner dissolved by an Act of Congress. It shall have power to adopt, alter, and use a corporate seal, which shall be judicially noticed; to make contracts; to lease such real estate as may be necessary for the transaction of its business; to sue and be sued, to complain and to defend, in any court of competent jurisdiction, State or Federal; to select, employ, and fix the compensation

of such officers, employees, attorneys, and agents as shall be necessary for the transaction of the business of the bank, without regard to the provisions of other laws applicable to the employment and compensation of officers or employees of the United States; to define their authority and duties, require bonds of them and fix the penalties thereof, and to dismiss at pleasure such officers, employees, attorneys, and agents; and to prescribe, amend, and repeal, by its board of directors, by-laws, rules, and regulations governing the manner in which its general business may be conducted and the powers granted to it by law may be exercised and enjoyed, including the selection of its chairman and vice chairman, together with provision for such committees and the functions thereof as the board of directors may deem necessary for facilitating its business under this Act. The board of directors of the bank shall determine and prescribe the manner in which its obligations shall be incurred and its expenses allowed and paid. The bank shall be entitled to the free use of the United States mails in the same manner as the executive departments of the Government. The bank, with the consent of any board, commission, independent establishment, or executive department of the Government, including any field service thereof, may avail itself of the use of information, services, facilities, officers, and employees thereof in carrying out the provisions of this Act.

SEC. 5. The object and purpose for which the bank is created is to aid in encouraging and facilitating exports and imports and the exchange of commodities between the United States and any of its territories and insular possessions, including the Philippine Islands, and the countries of

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Latin America or agencies or nationals thereof, and in connection therewith and in furtherance thereof the bank is authorized to do a general banking business; to receive deposits; to purchase, sell, discount, and negotiate with or without its endorsement, or guarantee, notes, drafts, checks, bills of exchange, acceptances, including bankers' acceptances, cable transfers, and other evidences of indebtedness; to purchase and sell securities, including obligations of the United States or of any state thereof; to accept bills or drafts drawn upon it; to issue letters of credit; to purchase and sell coin, bullion, and exchange; to lend money; and, with the approval of the Secretary of the Treasury, to borrow money and rediscount notes, drafts, bills of exchange, and other evidences of indebtedness; provided, however, that the bank shall not have outstanding at any one time loans or other obligations to it in excess of \$ _____, the capital for which the Reconstruction Finance Corporation, when requested by the Secretary of the Treasury, with the approval of the President, shall supply from time to time.

SEC. 6. Upon the expiration of _____ years from the date hereof, or upon the earlier dissolution of the bank by Act of Congress, the board of directors of the bank shall proceed to liquidate its assets and wind up its affairs. During the course of liquidation the bank may at any time pay to the Treasurer of the United States as miscellaneous receipts any money belonging to the bank or from time to time received by it in excess of reasonable amounts reserved to meet its requirements. Upon such deposit

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being made, such amount of the capital stock of the bank as may be specified by the bank with the approval of the Secretary of the Treasury, but not exceeding in par value the amount so paid to the Treasury, shall be canceled and retired. Any balance remaining after the liquidation of all the bank's assets and after provision has been made for payment of all legal obligations of any kind and character shall be paid into the Treasury of the United States as miscellaneous receipts. Thereupon the bank shall be dissolved and the residus, if any, of its capital stock shall be canceled and retired.

SEC. 7. If at the expiration of the ten years for which the bank has succession hereunder its board of directors shall not have completed the liquidation of its assets and the winding up of its affairs, the duty of completing such liquidation and winding up of its affairs shall be transferred to the Secretary of the Treasury, who for such purpose shall succeed to all powers and duties of the board of directors of the bank under this Act. In such event he may assign to any officer or officers of the United States in the Treasury Department the exercise and performance, under his general supervision and direction, of any such powers and duties; and nothing herein shall be construed to affect any right or privilege accrued, any penalty or liability incurred, any criminal or civil proceeding commenced, or any authority conferred hereunder, except as herein provided in connection with the liquidation of the remaining assets and the winding up of the affairs of the bank, until the Secretary of the Treasury shall find that such liquidation will no longer be advantageous to the United States and that all of its legal obligations have been provided for, whereupon he shall retire any

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capital stock then outstanding, pay into the Treasury as miscellaneous receipts the unused balance of the moneys belonging to the bank, and make the final report of the bank to the Congress. Thereupon the bank shall be deemed to be dissolved.

SEC. 8. The bank shall make and publish a report annually of its operations to the Congress.

SEC. 9- (a) Whoever makes any statement knowing it to be false, or whoever willfully overvalues any security, for the purpose of obtaining for himself or for any applicant any loan, or extension thereof by renewal, deferment of action, or otherwise, or the acceptance, release, or substitution of security therefor, or for the purpose of influencing in any way the action of the bank, or for the purpose of obtaining money, property, or anything of value, under this Act, shall be punished by a fine of not more than \$5,000 or by imprisonment for not more than two years, or both.

(b) Whoever, being connected in any capacity with the bank (1) embezzles, abstracts, purloins, or willfully misapplies any moneys, funds, securities, or other things of value, whether belonging to it or pledged or otherwise entrusted to it, or (2) with intent to defraud the bank or any other body politic or corporate, or any individual, or to deceive any officer, auditor, or examiner of the bank, makes any false entry in any book, report, or statement of or to the bank, or, without being duly

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authorized, draws any order or issues, puts forth or assigns any note, draft, check, bill of exchange, acceptance, or other evidence of indebtedness, or mortgage, judgment, or decree thereof, or (3) with intent to defraud participates, shares, receives directly or indirectly any money, profit, property or benefit through any transaction, loan, commission, contract, or any other act of the bank, or (4) gives any unauthorized information concerning any future action or plan of the bank which might affect the value of securities, or, having such knowledge, invests or speculates, directly or indirectly, in the securities or property of any company, bank, or corporation receiving loans or other assistance from the corporation, shall be punished by a fine of not more than \$10,000 or by imprisonment for not more than five years, or both.

(c) No individual, association, partnership, or corporation shall use the words "Latin-American-Export-Import Bank" or a combination of these five words, as the name or a part thereof under which he or it shall do business. Every individual, partnership, association, or corporation violating this prohibition shall be guilty of a misdemeanor and shall be punished by a fine of not exceeding \$1,000 or imprisonment not exceeding one year, or both.

(d) The provisions of sections 112, 113, 114, 115, 116, and 117 of the Criminal Code of the United States (U. S. C., title 18, ch. 5, secs. 202 to 207, inclusive) in so far as applicable, are extended to apply to contracts or agreements with the bank under this Act, which for the purposes hereof shall be held to include loans, advances, discounts, and

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rediscounts; extensions and renewals thereof; and acceptances, releases, and substitutions of security therefor.

SEC. 10. The right to alter, amend, or repeal this Act is hereby expressly reserved. If any clause, sentence, paragraph, or part of this Act shall for any reason be adjudged by any court of competent jurisdiction to be invalid, such judgment shall not affect, impair, or invalidate the remainder of this Act, but shall be confined in its operation to the clause, sentence, paragraph, or part thereof directly involved in the controversy in which such judgment shall have been rendered.

BK 193

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June 2, 1939.

My dear Mr. Secretary:

At your request I have undertaken a survey to determine what steps have or have not been taken to place ourselves in a position to immediately function in the event of an outbreak of war. I understood your interest to lie chiefly in the transportation and ocean shipping problem and I have directed my enquiries along this line, especially concentrating on matters pertaining to shipping.

At the outset I was somewhat at a loss as to how to proceed and so I began with the Treasury Department (Customs and Coast Guard). I have talked with many persons in this Department and have asked innumerable questions. I next approached the Maritime Commission, and then the Navy and Army Departments.

After I had proceeded some distance I learned of the "Industrial Mobilization Plan of 1936" which plan I am informed is being revised as of 1939. Under this plan the Assistant Secretary of War is charged by existing legislation with the responsibility for assurance of adequate provision for the mobilization of materiel and industrial organization essential to wartime needs. Inasmuch as the Navy Department is as vitally interested in this problem as is the War Department, by joint legislative action the necessary coordination has been provided

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for by the establishment of the Army and Navy Munitions Board (Liaison Division).

This board consists of the Assistant Secretary of War and the Assistant Secretary of the Navy assisted by an executive committee composed of three active Army and Navy officers. An Ocean Shipping Section has been established and contributes the views of the Maritime Commission.

(At this point it would seem to me that on the Advisory Defense Council, which is the parent company as it were, consideration should be given to the appointment to this board of the Secretary of State, the Secretary of the Treasury and the Chairman of the Maritime Commission.)

The one thread that runs through the Army, Navy, Treasury and Maritime Commission in war time is ocean shipping. Fortunately the World War is not too far behind us not to be able to profit by the mistakes we made and to utilize the lessons we learned. After much confusion and floundering about in 1917/1918 a Shipping Control Committee was set up: it comprised a committee of three -- actually one man (P. A. S. Franklin) ran it virtually single handed; from then on to the end of the war great efficiency was gained and the committee functioned smoothly.

Admiral Land of the Maritime Commission has been most cooperative and assigned to me his assistant, Mr. Huntington T. Morse. I feel that Mr. Morse has a broad grasp of the whole question

at issue and should be encouraged to continue his efforts. From time to time he has submitted to his Superior reports which show a thorough understanding of the question. After many conferences and much ground covering Mr. Morse has been encouraged to bring his reports up to date with the result that there is attached as exhibit "M" a final report dated May 15, 1939. With this final report I am in full concurrence and feel, Mr. Secretary, that it gives you the full answers to the question you asked me to investigate.

One point was very evident in my many talks and that was that everyone was keenly alive to the seriousness of the situation and that a great deal of exploratory work had been done by each Department. I did find however that some coordination was needed to bridge over the intangible barrier where Department met Department and it seems to me there is great need of a "Devil's Advocate", who will continually ask questions, many of them doubtless quite foolish, but by so doing the subject will be thoroughly explored. One danger I have foreseen is that some problems are so simple and trivial that they are apt to be passed by or left to some one else to handle whereas it is the very trivial matters which might in an emergency be the monkey wrench that would slow up the big machine.

In conclusion I would respectfully point out to you that the successful working out of the problem at issue will depend largely on the caliber of man selected to head the

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Shipping Control Committee in the event of war, and to my mind it must be headed by a civilian for obvious reasons. Would it not be well to quietly select some outstanding man in the shipping industry who would be made an ex-officio member of the Liaison Division of the Army and Navy Munitions Board to meet with them twice or more a year in order that he might be conversant with their efforts as they may pertain to shipping, and so that he may bring to them an outside viewpoint of the shipping industry. Then in the event of sudden hostilities you would have at hand a man well trained and qualified to step into the breach who would already have the advantage not only of knowing the various Departments of Government, but would have, or should have, gained the confidence and respect of his fellow workers. It should not be overlooked that if the present policy of this Administration is followed the merchant fleet of this country will be augmented by over 500 comparatively new vessels in the next ten years and in the event of war the handling of such a vast fleet plus the vast fleet of older ships then existent would require a well trained executive conversant with the many phases of this vast problem.

Respectfully submitted,

Basil Harris.

FEDERAL RESERVE BANK
OF NEW YORK

June 2, 1939.

Dear Mr. Secretary:

There is no new corporate security financing to be reported this week. The nearest thing to a corporate issue was an \$18,000,000 bank loan obtained by E. F. Goodrich Company. This loan, at 3 per cent interest and maturing in 1945, will be used to refund 6 per cent debentures of 1945. Banks are becoming increasingly active in what may be called the private purchase of obligations in the form of loans. Maturities rarely, if ever, exceed ten years.

Municipal bond awards this week amounted to about \$20,200,000. In an intermediate category, so far as maturity is concerned, was a \$100,000,000 issue of Commonwealth of Pennsylvania notes, due in two years. The issue was awarded to dealers at an interest cost of about 0.45 per cent and reoffered to the public to yield about 0.437 per cent. The dealers' mark-up was about 0.03 of a point. Over 80 per cent of the issue has been placed in the 24 hours since the award, including approximately \$17,000,000 taken by a State fund.

More than a dozen corporate issues are now in line for marketing during the next month or two, reaching a total of several hundred million dollars. They will not, however, mean much increased business except among security underwriters, because about 99 per cent of the entire sum is for refunding. The market appears to be more than ready for new offerings whether for refunding or for new capital. Competition among buyers is more intense than ever, and institutions probably are easing the standards which they have hitherto maintained in selecting investments.

This situation (competition of buyers rather than easing of standards, perhaps) also finds expression in the government security market, as you know, and particularly in the long-term section of the market.

Yours faithfully,



Alan Sproul,
First Vice President.

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

1939

June 5, 1939.

Dear Mr. Spraul:

For the Secretary I am acknowledging your weekly letter dated June 2, 1939. As you know, Mr. Hargenthan is always most interested in your comments upon current security financing.

Sincerely yours,

(Signed) H. S. Klotz

H. S. Klotz,
Private Secretary.

Mr. Allan Spraul,
First Vice President,
Federal Reserve Bank of New York,
New York, New York.

GHP/dbs

cc to H.S.

MEETING OF FISCAL AND MONETARY
ADVISORY BOARDJune 2, 1939.
10:30 A. M.

Present: Mr. Eccles
Mr. Delano
Mr. Smith
Mr. Bell
Mr. White
Mr. Haas
Mr. Currie
Mrs. Klotz
Mr. Duffield

H.M.Jr: I don't know whether it's the weather or what it is, but I feel pretty good.

Are you (Delano) going to be teacher?

Delano: Huh?

H.M.Jr: You going to be teacher?

Delano: I have nothing to say today. I'll have to listen.

H.M.Jr: Mr. Smith, you want to be teacher?

Smith: No, I - I haven't got the ball. Let's find out who has the ball.

H.M.Jr: Yes, who's got the ball?

White: Well, we've got the old ball.

H.M.Jr: Well, it isn't worn out, is it?

White: No, we repolished it a bit. It's much the same as the corrected one. This is so much the same - oh no, it isn't. I guess not. We changed it since then, although I think everybody got a copy of the changes that were made and this is merely a - we polished it up this morning.

Would you like to have it read?

H.M.Jr: Yes, please.

- 2 -

- White: "1. It is almost the unanimous opinion among Administration officials and technicians in Washington who are on or are cooperating with the Fiscal and Monetary Advisory Board that there is little if any prospect for marked recovery during the next two years.
- "2. They also recognize....
- H.M.Jr: Do you mind if I work with you people as we go along on this, because I think it's better.
- White: I think it's better if you work along at this stage of it.
- H.M.Jr: Well, if you don't mind, if this is going as an introductory first paragraph to the President, I think it's terrible. I mean he immediately - I mean he'd start to make fun on that. "It is almost the unanimous opinion...."
- White: Well, we can make it....
- H.M.Jr: And if I might make another suggestion. Mr. Eccles brought to my attention the one we sent him in December and I think if we're going to do this - my thought was, if we're going to send him over something, we'd say, "Following up the suggestion which we made to you last December, we'd like to do so and so and so and so."
- Eccles: The statement that we made in December - we referred to certain things that should be done and said that we would continue to study and make a later report; so it would be perfectly logical here to say that "Supplementary to, or following up the report of December, why, your Committee has been studying the future prospects" and then raise these questions.
- White: I think that would be more desirable.
- H.M.Jr: Yes. So if it's agreeable, could it take that form?
- White: Yes.

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- H.M.Jr: Go ahead, Harry.
- Eccles: Might work this ~~thought~~ into it some place. But I agree with you that it's pretty abrupt starting here.
- H.M.Jr: Yes.
- White: Now, this phrase which will be woven in still remains - "It is almost the unanimous opinion...."
- Delano: I think you could say "It is the general opinion." Wouldn't have to be unanimous.
- Eccles: That's better.
- Bell: Might say - I don't remember how you opened that other one, but you might say "We still are of the opinion...." I think you said that then.
- White: Yes, except that that referred only to the Fiscal and Monetary Advisory Board and this, to give it a little more strength, spoke of officials and technicians who are on or cooperating with. Maybe you'd like to make this "still," but it would give it a little more strength to have it this way.
- Delano: I think that this thing - the merit of it is this, that there is no effort to paint a rosy picture or anything like that. We're trying to be honest and realistic. Let's not bet on what may not happen. But of course, we're not thinking of this as a kind of thing that would be made public or published, or anything like that. But we've got to tell the President what we think. And then he says, "So what?" and so we give him a final page on what we think of it today.
- H.M.Jr: All right.
- Haas: I think - may I say - the question of the general - I mean general opinion as to the prospects.... I don't agree that the - in fact, I have a feeling and I think there is some support for the position that we will have some recovery between now and the end of two years. And then it's a question of

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what you mean by "marked." If you mean 80 billion dollar national income, there's a serious question-mark on that. But this may lead the President to think that we are - that this present upward movement that started last year is now at an end and we're going into another downward trend of the business cycle. I think that would be misleading. It would be from my point of view.

White: Would you suggest another adjective?

H.M.Jr: May I - I think I can make a suggestion which would answer it possibly this way. If you could put it in terms of national income - that during the next two years it is the opinion of most of the people that the national income will not rise above X millions of dollars - wouldn't that satisfy you?

White: That would be better, if we could get agreement.

H.M.Jr: Well....

White: We'd have to get it right now.

H.M.Jr: Well, you could over the week-end.

Eccles: Why couldn't you with safety put in there 68 billion? We talked last year of a possibility - of an outside possibility, you remember, in December, of getting a national income up to a maximum of 68 billion this year. Well now....

Currie: Average for the year.

Eccles: That was right, an average for the year of 68 billion. Now we know that that isn't - that we're not going to get even close to 68 billion for the year, at least it doesn't look like it, and it's got to be....

Delano: What year are you talking about?

Eccles: This year.

Delano: Fiscal year?

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- Eccles: We're talking calendar year. In our report before we were talking calendar year '38 - I mean '39. Why couldn't we with - it seems to me that we could put in there that prospects for marked recovery during the next two years, rising above 68 billion for the year - I wouldn't say 68 billion for a month; I don't think that means very much anyway - but certainly during the entire year '39 and the entire year '40 it is not likely, under present prospects, to rise above 68 billion dollars.
- White: You could relate that back to your previous statement in which you said you did not anticipate more, and say that as things look now you feel it will be substantially less for 1939 and for 1940. I don't know what you want to say for 1940, but....
- H.M.Jr: If you do it that way, just....
- White: Except that I'd like to hear a figure for 1940 that you'd want in there.
- Haas: Why not say the figure we have talked, Marriner?
- Eccles: That isn't consistent with the next sentence, though, because you say there that they recognize the possibility of a downturn in business activity before the end of 1940.
- White: The way it will be phrased will be "not more than...."
- Eccles: That may be all right.
- Haas: You'd have to take 68. Why don't you take the figure which was the goal set - 80 - and say it will not reach that?
- Eccles: Well, nobody expected to even approach that.
- White: The answer to that is, if it reached 75 it would be so good that we would not be justified in doing anything. Even if it reached 72 - a four billion increase would be very substantial.
- H.M.Jr: Could I say something on 1 and 2. I think anybody that's going to tell the President - put himself

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on record that we look for a downturn at the end of '40, is getting - well, he's getting out in the range of crystal-gazing.

Haas: Nobody knows.

H.M.Jr: What I would suggest for 1 and 2 - you might think of combining them, and say that "In December we said that national income in this calendar year 1939 would not exceed 68; it now looks as though we won't approach that; and looking into the year 1940, for the year, it is the best opinion that the national income for the calendar year will not exceed X billion." And don't get it down to whether it's going to turn down or turn up within the year. Now, we could be fairly safe on that and most likely get an agreement. Don't you think so?

Eccles: It depends entirely on the amount you put in.

Currie: There is one little difficulty there, Mr. Secretary. The Department of Commerce may make our estimate come out for this year. They have been revising their figures and they have raised last year by two billion dollars. Last year was 64 billion dollars. So we only need to get a four billion increase this year to get our sixty-eight, on the basis of the new figures. We were going on the old figures.

H.M.Jr: I think whatever the basis we were going on, we better stay on that basis.

White: Then make it in terms of the increase rather than absolute amount, so as to save ourselves that difficulty.

H.M.Jr: Let's say for argument - I don't care - let's say that nobody can see that the national income, figuring on the old basis, will be above 70 billion. I'm not saying that. Then you use your argument that in order to increase that by five billion dollars - so forth and so on. Huh? I mean I'm just offering that as a suggestion.

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- White: Yes, if there is agreement that we can set it at a top for 1940 of not more than 70 billion and probably less. But if we can use that figure 70 billion in that way....
- Delano: I think "possibly less" and not "probably less."
- White: "...and possibly less."
- H.M.Jr: "...possibly less."
- White: And you want to delete this statement that they recognize the possibility of a downturn.
- H.M.Jr: When somebody tells me there's going to be a downturn at the end of 1940, why, I think he's just crystal-gazing.
- Haaa: Possibility on the other side, too.
- Eccles: Of course, if we don't, I don't see why we want to make any report at all. I mean I see no point in even taking any interest in a study or an approach of this thing if it's a question of admitting that we can't - that it's all crystal-gazing, that it's purely guess-work. Then why should we even be interested in trying to forecast anything?
- White: Well, the strength of the position is this - the strength of understatement, that even here we are being conservative; we say that it might reach 70 billion, though we think that it probably won't, may be something less than that. And your whole case is built on the point that even if it does reach 70 billion, you still have a sufficient problem to justify action now.
- Delano: I think that phrase of understatement is a good phrase to use, because that's what we're going to do. We're going to deliberately not fool ourselves or fool the President by making an overstatement. We want to err on the side of understatement.
- White: That's right. If your case rests on the assumption that if you get a 70 billion national income nothing should be done, and if you get 67 or 66 something

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should be done, I think that one might be justified in taking the gamble that we might get 70. If on the other hand, you are taking the position that you don't see any reasonable likelihood of getting more than 70 and that even at 70 a program is called for, it seems to me you've made your position stronger.

Eccles: Yes, if you keep your figure down to a low enough point. But as I understood the point that George was making - that we just couldn't attempt to forecast or look through to 1940, that it's too far off.

H.M.Jr: No.

Eccles: That anything can happen. Well, it seems to me that if we have any job at all, it is planning or trying to forecast at least that far ahead, because if you're going to get action to meet a situation that might exist in '40, certainly you've got to get action at this session of Congress, if it calls for legislative action. Therefore, if we're going to perform any function at all, we've got to forecast for at least two years from now.

Haas: I didn't mean that, because we have to do that in the question of revenue estimates, we have to go out.

What I meant was that to describe the pattern, that it's going to turn down at the end, and so on, is really something that's, as the Secretary says, crystal-gazing, I think.

White: It says "Before the end." That means anytime within the next eighteen months. However, we can delete that and still make a good statement.

H.M.Jr: Well, I've got another - I mean, Eccles - I mean you wouldn't - and I'll go along with you that we estimate what the national income will be for the calendar year 1940; but the only question that I was raising was on saying that in a particular quarter it will go up or down.

Eccles: Oh no, I wouldn't think that - I don't think that anybody can time these things within six months, anyway.

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- H.M.Jr: Well, that's all - well, you and I are in agreement.
- Eccles: I think all we can do is to look at the thing from more or less of a long-range approach, because psychologically you can get an upturn or a downturn against economic conditions that would call for something else. But the permanent long-range trend, the fundamental economic conditions are the thing that determine. But as to the question of timing, I just don't think that you can - hell, you might even miss it as much as a year. I think that's even possible.
- H.M.Jr: There's no disagreement. And the other thing - I'm sure that neither White nor Currie could have possibly had this in mind, but they might be accused of it - they're talking about the end of '40, and it sounds kind of political.
- White: That was bare coincidence.
- H.M.Jr: I just thought we might get a rise on that.
How do you spell "bare"?
- Delano: You said it.
- H.M.Jr: All right; gentlemen?
- White: All right, we'll delete that and we'll send the paragraph around to make sure, since that's a key paragraph, that everybody agrees.
- Smith: I was wondering - may I inject here a moment - I was wondering if before we go further it might not be wise to agree upon the general form. I would suggest that this start out with a general statement setting forth the relation of this statement to the December statement, without joining 1 and 2 to that general statement, because it seems to me that if you join 1 and 2, when you get down to 3 and 4 and 5 you are in much the same sort of difficulty. And I was wondering if we wouldn't make more progress by perhaps agreeing

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that we'd have a general introductory paragraph and then any revisions we have relating to these specific things, as you have them here now. I was following through on the thought that you might put 1 and 2, I believe the Secretary suggested, into a general paragraph, but then it seems to me that that gets us into trouble with 3 and 4 down the line; they're also quite general.

White: We can do that, make it a separate paragraph.

Smith: Yes.

White: Shall I go on with the third?

H.M.Jr: Yes, please.

White: "Even with a moderate improvement in business the unemployment situation will not be substantially different from what it is now. With no improvement in business, the number of unemployed will increase because of the annual accretion to the labor supply of more than half a million a year and because of continued technological change."

I'll go on unless you indicate....

H.M.Jr: All right, or anybody else?

Delano: I'd be inclined to say "cannot" instead of "will not."

White: In the second line?

Delano: Yes.

White: "The unemployment situation cannot be substantially...."

Delano: If you think that....

White: Well, that would follow with a moderate improvement.

Bell: Does that tie in with that national income figure you're going to put in the first paragraph - 70 billion?

White: Well, you get an increase of a million two hundred thousand in two years, so that in order to get a

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million two hundred thousand increase in employment - if you got a three billion - it would take almost a three billion increase, I think, to get that.

- Eccles: Even to hold where you are in your unemployment situation.
- White: In the unemployment - not in the employment, but in the unemployment, to remain where you are, it would take several billions increase.
- Bell: You're going to jump from 64 to 70, as a possibility. Now, that certainly takes care of more than the accretion to your labor market in the next two years.
- Eccles: You've got substantially....
- Currie: You're dealing with ten million, so eight or nine million....
- Eccles: Substantially you'd improve five hundred thousand. Even a million - if you dropped the unemployment from ten to nine, you wouldn't have made very much - you've still got a terrific problem.
- White: What would you want to make that, Dan? Would you want some other phrase there?
- Bell: I think there would be moderate improvement.
- White: "...greatly different"?
- Bell: Something like that, or say that even with this improvement that you've just talked about, the unemployment situation would not be....
- White:be more than X number different.
- Currie: Or "will remain acute."
- Bell: Yes, something like that. The "moderate improvement" didn't seem to me to tie in with the six billion dollar possible increase in your income. That's more than moderate.

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White: Well, we'll try to harmonize those two statements.

Bell: "Even with this improvement...."

White: All right, we'll harmonize those and I'll check with you after we get it.

Eccles: Aren't we going to be a lot better off if we approach this problem in a pessimistic way? In other words, I'd like to see us hope for the best and prepare for the worst. Instead of assuming now that we can get 70 billion or 72, let's assume that we are - say we're going to get 68 at the end of next year, and assume the unemployment situation certainly isn't going to improve; it's really going to be worse. Those are the safe assumptions to make. If you were conducting a business of your own, if you were successful, that's the way you'd approach your problems.

White: In other words, conservatism should not mean understatement, but overstatement.

Eccles: Of the difficulties.

White: Of the difficulties.

Eccles: That's my view of it. Now, if you approach it that way and then call for a program, any program you're going to get, that there's any prospect of getting.... It seems to me that if you're going to get 70 without a program, or 72 without a program, and if you had a program in addition and you got 75 or 78, you're just that much better off. It isn't as though you were close to the top. In other words, if you were in a position of 80 billion and were at this time trying to make it 90 billion, and had the danger of bottlenecks and inflationary developments, that would be another thing. But it seems to me we're perfectly safe in approaching this problem from the standpoint that at best you can't hope for more than 70 or 72 and there is every prospect that it may not be more than 65 to 68; therefore, let's prepare for the worst.

White: Let's not gamble.

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- Eccles: Then if the best happens, you're just that much better off. That's the way I'd like to....
- H.M.Jr: What's that you said, Harry?
- White: I said, let's not gamble.
- Eccles: That's the way I think we ought to do it. If we're going to advise the President on this, I think that's the way.
- H.M.Jr: No disagreement between you and me on this approach.
- White: I'm wondering whether - I spoke of understatement - I wonder whether conservatism in this case doesn't demand overstatement rather than understatement. When a general goes into battle, he estimates the number of reserves he will need not on the basis of the fewest he might lose, but he estimates on the basis that he might run into difficulties. It is true, however, the statement becomes a little more effective if there is a feeling on the part of the reader that you're not attempting to exaggerate.
- Delano: I think that's very important. History is full of military leaders who always underestimated their own strength and overestimated the enemy's strength, and they just didn't get anywhere.
- White: Neither does an analogy.
- Well, would this be a way out, Mr. Secretary: to have another paragraph or a couple of statements embodying the ideas which Mr. Eccles just stated and which you said you agreed with, which would make it possible for us to understate the case and yet indicate the importance of action, even though our understatement proved correct.
- Eccles: Admit certainly that we might miss it within a few billion dollars. But, even assuming that there's the prospect of 72 billion, can he gamble and take the chance that it's only going to be 68 or - 65 or 68? He's got to assume that it may be 65 or 68 and that the most he can hope for is 70 to 72. And if he doesn't get that, gets nothing, he's caught with 65 or 68.

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White: And, as you know, the President is against gambling.

H.M.Jr: I'm in complete sympathy with what you say. In other words, we'll figure it at the worst and anything we get above that is just velvet.

Eccles: That's right.

H.M.Jr: You can't fight with me on that.

White: Then we might work another couple sentences in.

H.M.Jr: Please, yes.

White: In which case it will be very easy to make provision for George's and Danny's comments.

"4. The inability of our economy to reach and maintain even the modest objective of an 80 billion dollar national income is due to the existence of certain fundamental maladjustments which have been developing. It is more and more apparent that a profound change in our economy has taken place since the twenties."

Now, one of the changes that I have made since the last time was to move (a), the question "We have for the first sustained period in our history a volume of savings which at a high level of national income is considerably in excess of the profitable outlet for such savings" - moved that down as one of the factors rather than where it appeared before, that everything was a consequence of that one; putting it first and then giving (b), (c), (d), (e), (f), and so forth, further expansion on that idea so that it gets sufficient emphasis, doesn't rest exclusively
....

H.M.Jr: I hadn't noticed that.

Duffield: I don't much like the tone of paragraphs 4 and 5, taken together, especially the last sentence, that "It is more and more apparent that a profound change in our economy has taken place since the twenties," if 5 is to spell out that sentence, because the tone seems to me to be one of saying that these

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things are here to stay, and there are a lot of things in the list which I would certainly not like to see admitted to be permanent new features of our economy.

Nor do I think the Secretary, in line with what he said at the first meeting, would like to say, for instance, that railroads and agriculture are permanently no longer sufficient outlets for capital.

White: Then you think the idea of permanence is implied.

Duffield: Certainly seems to me so.

Currie: From our point of view, five years is our problem. We're not saying that in 1960 we won't have a great boom in building. But for the foreseeable future
....

Duffield: What you are now saying isn't in this statement.

White: How would you want to phrase it?

Duffield: Leave out the second sentence of paragraph 4 and say in the first sentence "is due to the existence, of unpredictable duration, of certain maladjustments
...."

White: Well, they are predictable to the extent that you know they're going to exist for the next two or three years.

Duffield: Well, all right, say it that way, then. But as I understand, the Secretary's first criticism of what you came in with was that we don't attempt to solve the hard problems, the fundamental things which would make the first suggestion fruitful. Now, you've listed here, it seems to me, under 5 a great many of the hard problems and haven't said anything about the necessity of trying to solve them. You have accepted them, it seems to me, as inevitable.

White: Would this help to correct that, to say "It is more and more apparent that a profound change in our

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economy has taken place since the twenties, which gives every indication of lasting at least several years"?

Duffield: That goes part way. It doesn't meet the question - maybe you don't want to - of whether we ought to do anything about these fundamental changes....

White: Oh yes, very definitely.

Duffield:other than to offset them by channelizing savings into certain directions.

Currie: We can't do much about the line of population growth.

Duffield: That's true of some of them, not true of some of the others.

White: Doing something about the railroads should be a part of any proposed changes that will be made. I take it that it would be an essential part of your program to do something about agriculture, if we can suggest anything to be done. That ought to be an essential part. To do something about changing the tax structure is an essential part of the program of corrections. So that it appears to me that any program that would be devised on the basis of this would aim to correct some of the maladjustments which have taken place.

Duffield: Then I think you ought to spell that out either here or under 7.

White: Well, it is spelled out on - it is spelled out before you get to the end. That's your conclusion.

Duffield: Well now, for instance, take this "Certain large industries experienced the...." - this is (b) under 5 - "...major part of their expansion during the twenties." The question of whether there are - whether the great invention wasn't the invention of inventions, and you're going on in some other field now which is unpredictable - that point of view is entirely absent from this.

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- White: No, we say that the development - under 7 we say "As a consequence of these basic changes we are faced with the inevitability of a low national income unless either or both of the following happen: the development or appearance of sufficient investment outlets...." Now, unquestionably, something may appear, but we could hardly warrant Government policy affecting the lives of 130 million people on the hope that something will appear.
- Duffield: Well, you would meet most of my criticism if you would just make it not appear that these things listed under 5 are inevitable and permanent.
- White: We certainly ought to do that. We don't mean to - we'll try to work out a sentence that will do that.
- Bell: You're trying to cover the next two years, aren't you, Harry?
- White: Not only....
- Bell: You say 1939 and 1940. That's what you're trying.... First two paragraphs.
- Eccles: You've got some permanent changes in the economy.
- Duffield: Let's separate them out from the others.
- Eccles: For instance, we are a creditor nation on a very important scale today.
- White: You're not going to change that in two years.
- Eccles: As far as we're concerned, we can talk as if that were more or less permanent. It's true something could happen in the unforeseeable future so that we might become a great debtor nation; I can't imagine it. I think, after all, we're perfectly safe in talking about what the situation is and is likely to continue to be, so far as we can see now. That doesn't necessarily mean that a world war or some other unforeseeable thing in five or ten years from now might not develop, and it certainly does not make us look ridiculous to state

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pretty definitely that there are certain profound changes as compared with the twenties. And in a few years from now, we'll see profound changes then as compared with now. So that the change of population growth and the change of creditor status are two very fundamental factors, and I think we should prepare to deal with them as permanent until something happens to cause us to change.

- Duffield: Would you want to rank with those as permanent and inevitable such portions under 5 as this statement that State and local bodies which once provided an important outlet no longer do? You certainly wouldn't regard that as permanent or inevitable, nor the fact that the Federal, State and local governments now take more in taxes from consumption than they did in the twenties. There are a lot of things mixed up here which are both permanent and which are not.
- Currie: The sense of it is that those changes in the economy, both those which are permanent and those which are not, which have hindered business activity during the thirties are as follows.
- Duffield: But it comes right after a sentence which says that "It is more and more apparent that a profound change in our economy has taken place since the twenties," and it seems to say, in my mind, that here it is and what we've got to do is to meet these things, whereas I go back again to say that what we ought to do is try to change some of them.
- Currie: We certainly don't mean to rule that out.
- Duffield: Let's say so then.
- Bell: Why don't you say "will certainly be with us the next two or three years"?
- White: I could add that these changes which have taken place will certainly be with us for the next two or three years.

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Currie: Spell that out. "Certain of these maladjustments are subject to correction; others are not, and must be met in other ways."

Duffield: That statement you just made goes to the heart of the Secretary's first criticism: some of these maladjustments are subject to correction; let's, for heaven's sake, correct them.

H.M.Jr: May I interrupt at this time. This is what is running through my head, in order to make this thing effective. If we could get off a letter, say, tomorrow, to the President along these lines: the introductory just the way we said, and then refer back to our December thing and simply say something like this: "Now, Mr. President, we've been working on this thing for the past month in regard to some of the basic changes which are responsible for the lower level of business, and we would like to have an opportunity to meet with you and present some of the answers...." - or something like that - "...to these things."

In other words, what I'm trying to do - I'm trying in the first place to do it in a courteous manner, simply saying to him, "We are here, we have something, we'd like to have ample time to talk with you." Then we'd go over and if he'd give us a couple of hours, then we could sit down and you people could talk with him. And not just have another memorandum which goes into that wicker basket and doesn't do anything.

Eccles: Don't you think, though, as a basis of talk, that

H.M.Jr: See? And not give him so much of this. This might frighten him. And simply say - well, go back to December, say the introductory thing and then say, "We feel it's going to be 67 or 68 this year, and next year it looks like the best you can hope for would be the same."

White: Would both be appropriate? Could you get the letter that you speak of, and would it be appropriate and effective then to say "There is appended a memorandum...."?

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- H.M.Jr: No. I've been sitting here, if you don't mind, and - no, I wouldn't give him that, because if he reads that we may never see him. And if, on the other hand, we gave him a sort of a letter - "Well, what have these boys got on their mind? I'd better see them." And then come over and see him for a couple of hours. That's really what I think we need, and not just another memorandum.
- What would you think of that, Mr. Delano?
- Delano: Very good.
- H.M.Jr: And it's a courteous way to do it.
- Delano: I think that's a very good idea.
- Duffield: Could you take the memorandum and read it?
- H.M.Jr: Oh, then take the memorandum to the meeting and present it, one by one, and have a discussion just the way we're having here. And then he could cross-examine - "What do you mean by this, and what do you mean by that?" And he'd get something out of it. That's what we want.
- Delano: I think that's very true.
- H.M.Jr: And not send a lot of this stuff over which - oh, he'd say, "Well, that's nothing new," so forth and so on.
- White: Your point is that if the letter doesn't get him, the memorandum certainly wouldn't, whereas the letter might get him where the memorandum wouldn't; so you have nothing to lose and something to gain by a letter, not a memorandum.
- H.M.Jr: I'm thinking of time. He's talking of going away on the 15th. If we can get such a letter, get it written, get it signed tomorrow, get it over to him - then he makes up his schedule for next week, and in this letter we say we'd like to have a couple of hours, see?

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Delano: Very good.

H.M.Jr: And he'd have that tomorrow. Then he'd say, "Well now, I think maybe I'd better set aside a couple of hours for these men," and then we'd go over there and have a face-to-face discussion. And in it I'd say, "We'll be delighted if you would invite any other members of your Administration that you'd like to have participate." You see, Mr. Delano? Then it's up to him. If he wants Hopkins or if he wants Leon Henderson or if he wants this man or that man, he can ask whoever he wants. What would you think of that?

Delano: Very good, I think.

H.M.Jr: And then - what do you think, Marriner - to bring it to a head?

Eccles: Well, I'm - I don't see any point in us going over and discussing a program with him unless we get together ourselves on a program.

White: He wasn't speaking of the program, he was speaking of an explanation of the letter.

Eccles: Well, that's all right. That's just a question of approach. I see no objection to writing the President the letter and not sending the memorandum. I agree with you that he may not read the memorandum or he might lose interest and forget it. But if we have a memorandum that we've gone over and we've gotten together on, or at least as near as we can, at the time we go over, so that we give him the memorandum and then discuss it with him....

H.M.Jr: We can get agreement. But I'm just trying to save time. If he's going on the 15th, he's got - beginning with Monday, he's got 10 days. And I'm trying to - I want to get it over to him so that he won't....

Delano: About two or three of those are taken up by that royalty.

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- H.M.Jr: Right. Yes, the 8th, 9th, 10th and 11th are taken up by royalty - 8th, 9th, 10th and 11th. So I'm trying to get the thing to him tomorrow and then we could continue working to get our memorandum and try to get an agreement. But I'm sincere about this. I could just sit back and say, "Oh well, we'll send this...."
- Eccles: What you want to do is get a letter over to him before it's too late, and be working at the memorandum in the meantime.
- H.M.Jr: Right.
- Eccles: That's all right. I didn't....
- Delano: I think that's a very good program.
- White: That has the further advantage that if there's a chance that the letter doesn't bring results, you always can follow that whenever you think it's appropriate with a memorandum; so you're not losing anything.
- H.M.Jr: If he has me for lunch Monday, I'll press him for an appointment.
- Delano: I think that's a good idea.
- I was reading this fourth paragraph. I think one of the things he might say on reading that - "What does this - how come that you prognosticated 80 billion dollars some months ago and now you say it's impossible?" Well, of course, we could defend that in conversation.
- Eccles: We didn't, though. We didn't say anything about A....
- Delano: I know, but it got around that it was wishful hoping and all that sort of thing.
- Eccles: No, it seems to me, Mr. Delano, that all we said was that it would take an 80 billion dollar income to balance the present outgo on the basis of the present tax structure.

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- Delano: I think we went a little further than that. I got the impression from Ruml that he didn't regard it at all as an impossibility.
- Eccles: Next year, in '40? Gosh, I certainly didn't get that impression.
- Delano: Of course, it's predicated on a good many "ifs." He may have been talking about fiscal year '40 and not the calendar year of '40.
- H.M.Jr: Well, I would like to continue, as I say, working on the memorandum. And if you people could draft the letter, maybe today circulate it around, and then get it over to him tomorrow morning....
- Currie: Was it your thought, Mr. Secretary, that in the letter we follow up - that we tie back to the December statement, say, "We are convinced there is a grave situation and that there are fundamental maladjustments that should be corrected; we do think they can be corrected. We'd like to have the opportunity...."
- H.M.Jr: And send him a copy of the December memorandum. I think that's very important. I think that that's very important, to send him a copy of the December memorandum.
- Delano: Refresh his memory.
- White: Rather than to make certain that we are in agreement as to the program of action, it is immediately more important to agree upon what the problems are. So rather than to ask for a conference to find ways of correcting the situation - that's the second phase - I'd rather ask for a conference to explain why you feel this way.
- Smith: Set forth the problem.
- White: Set forth the problem, not come prepared with a solution. Then we can attempt to agree on the solution, which we haven't yet.

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H.M.Jr: That's right. Is that all right with you, Mr. Smith?

Smith: Yes, yes.

H.M.Jr: For instance, on this thing.... Were you going to say something?

Smith: I was going to say, I think if we agree on the approach here, that then we can get at the memorandum, which seems to me to be the important thing.

H.M.Jr: Well, I'm available Monday morning to work on this further.

White: Then we'd like to adjourn, if it's all right with everybody else, to begin working on the letter right away, because that might be a difficult....

H.M.Jr: But there's one thing I'd like to get over which I don't think is here, for you people to think about.

I'll be available 10:30 Monday morning, if that's convenient.

Eccles: Of course, I don't - I'm likely to have to be up on the Hill on that Mead bill.

H.M.Jr: All morning? All day?

Eccles: Well, it's either Monday or Tuesday.

H.M.Jr: Well....

Eccles: I'm not sure which.

H.M.Jr: Well, if you'll let Gene know, I'll adjust myself; I'll make it either Monday or Tuesday.

Eccles: Other than that - if I don't have to go up on that, why, I can....

H.M.Jr: Now if you men - I'd like to get one thing over. I don't know whether you'll agree. I'd like to get something into this memorandum about consumption of food and surplus cotton, as opposed to constriction, see?

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Eccles: As opposed to what?

H.M.Jr: Constriction.

White: I wonder if we couldn't - that is partly taken care of in the proposal of suggested changes, but it could be worked in here by saying that one of the manifestations of that basic maladjustment is the pursuit of a policy of constriction rather than....

H.M.Jr: I feel very, very strongly on it. I don't know whether you people agree with me in the room here. But I mean you can take Arkansas or Texas, any one of those States, and the reduction in the cotton acreage and the throwing people out of work and the falling off of the cork business and the steamship and the railroads - it just multiplies and multiplies; and a third of the population is affected by the price of cotton. And what we know now, I think, is correct, that the farmer gets just as much money from a small crop as he does from a big crop. And I don't - I mean we're not facing this cotton problem. It costs us what, 50 million dollars a year to carry it?

Bell: Forty-five to carry just the cotton alone.

H.M.Jr: And I feel that on that front, of eating our surpluses and wearing our surpluses, we could get somewhere very fast, and it's just a question of changing the mental attitude. We've tried this constriction now for, what is it, six or seven years, and haven't gotten anywhere.

Eccles: Of course, I agree with you fully that a policy of restriction of the production of wealth is a defeatist policy. It may be all right as a temporary emergency to meet some situation; but to adopt it as more or less of a permanent thing - it just doesn't make sense. And when we have a lot of unemployed people, of course, that's a corollary; they work together. One creates the other. It's difficult to say to what extent one affects the other, but we know certainly that a lot of unemployed people is a question of a restriction in the production of wealth. When you've got a lot of unemployed people, you just fail to consume and produce wealth. And

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if we could approach the problem from a standpoint primarily of getting buying power to people, see, the question of the consumption of cotton and the citrus fruit products and innumerable food products, such as butter - just think of the amount of butter that's piled up and the number of people in this country that just eat oleomargarine; there's a typical case. And if we think of it from a standpoint of purely people and having buying power, of their ability to consume, it seems to me that then our cotton problem would certainly diminish, just as a good many of our other problems would.

Haas: It would help the savings problem too.

Eccles: Well, it would tend certainly to - there would be a bigger outlet for savings in expansion of productive facilities, if people could buy what is produced by existing facilities.

H.M.Jr: Well, if I could supplement it - I mean it seems to me that the aim of this Administration is to raise the national income to 80 billion dollars, on the one hand; and then we spend, I think, Mr. Smith, some 800 million dollars to pay the farmers to grow less and to tighten everything up. The two things just don't make sense. And what I'd like to have the President do is to face that issue. I mean this idea that a 17 million bale cotton crop is a curse and that a 10 million bale crop is a blessing - the two things seem to me to just clash. And in the agricultural field the food and the clothing and the cotton and the things that we grow - I'd like to see all restriction taken off and let nature take its course.

And the only time we have been successful was the two years - I think I'm right, George - the two years we had a drouth. And we sit here....

Bell: Nature did take its course.

H.M.Jr: Right. We sit here, try to plan this thing, and we've got this - I don't know what proportion of

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the wealth of the country is agriculture, or comes from agriculture....

White: Proportion of national income rather than wealth.

H.M.Jr: Well, it's a very large proportion. And it's the same thing - that they still have no plan - and I think I'm right - of how much land Mr. Ickes will put under irrigation and how much land Mr. Wallace will take out of production. They're not dovetailed still, are they? Am I right on that?

Delano: Yes.

H.M.Jr: I was amazed to hear - somebody thought he had a bright new idea the other day at Cabinet when they were talking about taking the land of North Dakota out of production, putting it into grazing land - trying to decide whether Interior or Agriculture should do what they wanted.

White: If it belonged to Interior, they wanted to irrigate it so it produced more; if it belonged to Agriculture, they wanted to take it out of production so it would produce less.

H.M.Jr: If we could get something on this problem of production and agriculture, not just say that that's something that belongs to another world....

White: I think you've put your finger on the nub of that problem. I'm wondering whether it belongs here or rather in the next memorandum that follows, as to what suggestions you have for taking care of this situation. We might weave it into this....

H.M.Jr: Oh, not in tomorrow's letter.

White: Or in the memorandum upon which the letter is based.

Eccles: The difficulty I see with that - that's only one side of it. I mean if you're going to touch cotton, then you get into the question of tariffs. A good part of the ability to sell cotton depends upon

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our willingness to sell it to all the countries of the world that need it and to take their goods in payment. That gets into a tariff problem, gets into an exchange problem. Then you get into the question of labor. That raises the question of the wages and hours and labor relations. They're both of a restrictive type. When you say a man can't work more than forty hours a week, that's a restrictive - just the same kind of restrictive policy as the cotton policy. And then he's got to get a certain wage as a minimum. The whole thing is involved in the question of a managed economy; and we've managed a part of it without any relationship to the part that we don't manage. And we haven't got the power in our political system to manage any of it, as a matter of fact.

H.M.Jr: Well, if you fellows could just take a bite on agriculture....

Ecclcs: That's a pretty big bite.

White: It's a big apple.

Smith: Well, couldn't it be stated here as one of the problems under 5, maybe?

White: We've got agriculture as merely one of the basic problems under (c), but we could spell it out and make it a separate one. It certainly is entitled to that.

Currie: You have it under (k) too.

White: But we could speak of the pursuit of the policy of restriction and its essential paradox, which has been pointed out here - a ridiculous paradox.

H.M.Jr: Well, again following - I don't want to talk too much - take the question of the dairymen and their surplus milk. The policy is to buy the butter and store it. I'm trying to get Mr. Wallace to say fluid milk is a surplus and take it and put it in the stomachs of the undernourished. I think people - I think it's a question of getting away

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from the policy of restricting it and not consuming it as against the policy of eating it and wearing it.

Eccles: Of course, the reason most people don't eat it and wear it is that they haven't got the money to buy it.

H.M.Jr: Well, in Boston, on the fluid milk thing, they worked out something that looks awfully good.

Haas: Increased consumption 8 to 10 percent.

H.M.Jr: By reducing the distribution cost to two and three-quarters cents a quart.

Eccles: If they reduced the cost - that's one of our consumption problems in every line of activity, the holding up of high wages and high prices. It's a price policy, too.

Don't you think we know that all these problems are problems that we are confronted with and one is - the whole thing is extremely complex - that about all we can deal with here, without getting into the whole realm of the economic difficulties - that primarily we are interested now in meeting the short-range situation, because the other is a long-range thing that....

H.M.Jr: I want to do both, Marriner.

White: They are not mutually exclusive. In fact, they supplement each other.

Eccles: They supplement each other, but what can you do with the labor problem, with the agricultural problem?

White: Well, there are some things that can be done.

Eccles: And the tariff problem. We know this next year is an election year; these problems are terribly political.

White: You wouldn't take the position that because these problems are difficult and complex that we can't

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do something - we shouldn't do something about them?

Eccles:

We ought to point them out, but I think the only kind of a program you can get now is a program that is politically feasible. That's a question of what are the practical things that you can do without saying that that meets the entire problem, because I realize and I agree fully that we have all of these other problems. They're innumerable, and let's recognize them. But certainly you can't start at this stage - if it had been six years ago and we had recognized them then, I'd say let's start on the whole thing; but at this stage, with Congress about to adjourn, with next year a Presidential election year, I think we can point them out all right and let the President talk about them if he wants to, but I think that if we're going to prevent the downturn next year and it's going to depend somewhat on political, on Congressional action, then we've got to think about what action is politically feasible, because to talk about something that isn't politically feasible is just wasting our time.

H.M.Jr:

Well, I'd like to get this over to him so that he has something like this in case he gives another talk, with the hope that he'd have a good document like this rather than some of the things he expressed in his Retail speech. I think it's up to us to give him the best we can.

Smith:

Well, Mr. Secretary, isn't the problem something like this? I mean we can discuss these economic aspects of these various problems here at length, but first we are to prepare a letter for you which will introduce the problem.

H.M.Jr:

Which the four of us sign.

Smith:

Yes.

Secondly, we are to dress up this memorandum as a basis perhaps of discussion and handing it to him....

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

Smith:at the same time. And then later, after that, if the President says, "I'd like to have you tell me now what a program of action might be," then we can come into all of the practical aspects of the problem from the standpoint of politics and so on.

H.M.Jr: Is that all right, Mr. Delano?

Delano: Yes.

H.M.Jr: Well, can you gentlemen get us something that the four of us could sign tomorrow, maybe?

White: I think so.

Eccles: That's a letter to the President.

H.M.Jr: Yes.

Smith: Just a letter.

Delano: I have engaged myself to go away at an early hour tomorrow morning.

H.M.Jr: Well, maybe they can get it to you today. Let them get it to you tonight.

Eccles: I don't think that we should attempt to get a meeting next week with him because we won't be ready with a memorandum.

White: I'm wondering whether it's clear what the program is, Marriner; that the letter is only to get, as I understand it, an opportunity to present the memorandum and a discussion of the aspects, but not to say anything about....

Eccles: I understand that, but what I mean - what I'm pointing out is that in this letter to him - what if he should say, "Well, come over Tuesday" or "Come over...."

White: Aren't you ready to discuss these things Tuesday? You're not going to say anything about what you're going to recommend. If the President says, "What

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are you going to do about it?" we can say, "That's what we'd like to go to work on right away."

Eccles: In other words, all we expect to do - this is the memorandum.

White: That's my understanding of what you wanted to do.

Eccles: All right. If we've agreed, then, that this is the memorandum, that's all right.

White: With some further minor changes.

Delano: I think it would have to be done next week or not at all.

Eccles: I didn't assume that we had agreed upon the memorandum as a basis for discussion, but if we have practically, why, then....

H.M.Jr: For discussion, without - I think there are certain things in there which I wouldn't agree to personally, but I'm willing to go over and see him and have an oral discussion with him. And I thought that's another way to short-circuit this thing - I mean to find a short-cut - that's what I mean. What? Give us a short-cut, huh?

Delano: Be very helpful.

H.M.Jr: O. K. And, Marriner, you're to let us know whether you're available Monday or Tuesday.

Eccles: Yes.

1. It is almost the unanimous opinion among Administration officials and technicians in Washington who are on, or are cooperating with the Fiscal and Monetary Advisory Board, that there is little if any prospect for marked recovery during the next two years.

2. They also recognize the possibility of a downturn in business activity before the end of 1940.

3. Even with a moderate improvement in business the unemployment situation will not be substantially different from what it is now. With no improvement in business the number of unemployed will increase because of the annual accretion to the labor supply of more than half million a year, and because of continued technological change.

4. The inability of our economy to reach and maintain even the modest objective of an \$80 billion national income is due to the existence of certain fundamental maladjustments which have been developing. It is more and more apparent that a profound change in our economy has taken place since the 20's.

5. Some of the basic changes which are partly responsible for the lower level of business activity during the 30's are as follows:

(a) We have for the first sustained period in our history a volume of savings which at a high level of national income is considerably in excess of the profitable outlets for such savings.

(b) Certain large industries experienced the major portion of their expansion during the 20's. These have now reached a degree of maturity which eliminates them as potential outlets for large amounts of new savings. Though we expect a continued growth of most of these industries the rate of expansion and the absolute volume of new savings they will absorb will be much less than it was in the 20's.

(c) Basic difficulties in certain important industries which for special reasons do not provide nearly so important an outlet for capital as they did in prior decades, e.g., railroads, agriculture.

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(d) The rate of population increase has been out in half as compared with the 20's.

(e) The virtual cessation of foreign investment which in the 20's accounted for about one-half billion a year.

(f) State and local bodies which in the 20's provided an outlet for savings of nearly a billion dollars a year have in recent years actually added a little to the current volume of savings through a net reduction in their outstanding debt.

(g) Sharply curtailed expenditure on non-profit private building, i.e., churches, clubs, universities, etc. In the 20's these accounted for a half billion to a billion dollars a year and they now are less than 200 million.

(h) The slack created by the over-production of commercial buildings in the late 20's will not be taken up for several years at least.

(i) The trend of technological change over much of industry has been in the direction of a reduced amount of capital consumption per unit of output.

(j) The Federal, State and local government tax structures now derive a greater proportion of total revenue from taxes that curtail consumption than was true in the 20's.

(k) The serious reduction of certain foreign markets for important export crops, e.g., cotton, wheat, tobacco and hog products, and the failure of foreign trade generally to revive to the level of the 20's. The curtailment of these markets is not due to temporary factors.

(l) The situation is aggravated by the fact that those who have or control the nation's savings are definitely more timid in undertaking business risk ventures. The increasing uncertainty, both economic, political and social, which has characterized the past decade has made people more conservative in both expenditure on consumer goods.

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and in the investment of their savings. In addition, the tax burden has increased as compared with the 20's, thus reducing the net profits left to the investor or business entrepreneur and thereby in some instances reducing the incentive to undertake risks.

6. The United States is not unique with regard to the changed nature of the economy. The advanced European countries have experienced the same contraction of outlets for their savings. Some of them have temporarily solved their problems by a new industry greater than all the new industries of the past period combined, i.e., armaments and complimentary industries. In some of them the problem has been rendered less acute by the fact that their tax program has resulted in a diversion of a larger portion of potential savings back into consumption.

7. As a consequence of these basic changes we are faced with inevitability of a low national income unless either or both of the following happen:

(a) The development or appearance of sufficient investment outlets to absorb the savings of a high national income.

(b) An increased proportion of the national income is spent on consumers goods, thereby reducing the volume of idle funds and increasing the profitable outlets for savings.

8. Turning to the immediate situation there are numerous indications that the prospects for substantially increased national income in 1939 and 1940 are not good.

There are two elements in the picture which are bullish:

(a) Inventory reduction has been proceeding for some months and a cessation or reversal of this trend would be a stimulus to production.

(b) Expenditure on consumers goods has been maintained despite the decline in business activity.

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On the other side of the picture are the following:

(a) The upturn which began in 1938 reached its peak in December and since that time the level of business activity has been downward.

(b) No significant increase in the net contribution to buying power by the Federal Government under the existing program will occur this year and a reduction is anticipated in the fourth quarter.

(c) There is little basis for the expectation that our exports in 1939 and 1940 will exceed the 1938 level despite the increased armament programs abroad.

(d) Housing activities appear to have reached a plateau and there does not seem to be any prospect of a further marked increase of home construction.

(e) No substantial increase in railroad equipment buying can be anticipated in the balance of the year.

(f) There is little prospect of an expansion in public utilities. The present capacity of the industry is adequate to meet the needs of the country even with a moderate increase in the level of business activity.

(g) Despite the increase in orders for armaments both domestic and from abroad, the heavy industries are still depressed.

(h) There is nothing in the prospects of the agricultural situation to justify the expectation that it will supply a stimulating influence on business activity.

(i) There is a further political factor, namely, there will probably develop a strong tendency on the part of certain groups to forego the prospects of immediate profits by postponing any investments or plant expansion until after the election.

9. Even if there is a moderate increase in business activity next year the unemployment situation will be substantially the same in 1940 as it is now.

In 1937, 35 million persons were employed in non-agricultural pursuits. Today less than 35 million are so employed. During 1940 we shall be doing well if we again reach the volume of employment of 1937, whereas the non-agricultural working population in 1940 will be about 2 million greater than in 1937.

In addition to this unemployment situation in non-agricultural lines, there is known to be a surplus labor supply on farms perhaps as large as 1.5 million working persons that need to shift from farming into industrial opportunities.

In view of the fact that there is no expectation for more than a moderate rise in national income for the next fifteen months, and in view of the further fact that a decline in business activity some time during the next fifteen months is a possibility, and, most important, in view of the conviction that sustained full recovery is impossible unless action is taken to correct basic maladjustments:

There is general agreement among the persons referred to above that a comprehensive program of action should be initiated at once, such action to be designed to accomplish two things:

1. Make some important contribution toward the elimination of the basic maladjustments which stand in the way of a sustained full recovery. Though the full effects of this program will not be felt for several years, it is vitally important that such a program be initiated at once for two reasons:

(a) It will take a long time before such a program could be worked out and put into effect.

(b) It is important to make clear to the public that this Administration recognizes the existence of basic maladjustments and will take steps to correct them, that it will push toward a further extension of New Deal principles and will adopt measures designed to insure long-term and sustained prosperity.

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2. A program of immediate action designed to insure a substantially increased national income in 1940 and to protect us against the possibility of a sharp downturn in business during the next fifteen months.

Some of the measures which can be undertaken to correct basic maladjustments can be initiated with sufficient rapidity to raise the national income in 1940.

If to the increase in national income that would result from measures undertaken to correct basic maladjustments there be added the further increases to the national income which would result from measures specifically designed to increase in 1940 investment and expenditures, then an increase in the national income of \$5 billion or so can be assured for next year.

There appears to be general agreement in the group mentioned above that Congress should not adjourn until an adequate program has been inaugurated. Or, if Congress is to adjourn, it should do so only with the distinct understanding that it would reconvene after a short vacation prepared to deal with these major problems, some of which have been before us for a long time.