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TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE January 9, 1940

TO Secretary Morgenthau

FROM Mr. White

Subject: Highlights of plan for Pan American Bank.

1. Capital: Authorized \$100,000,000. -- Initial subscriptions to be paid 50 percent of par at time of subscription, remainder on calls. -- Minimum subscription for participation is arranged according to population groups and ranges from \$1 million for countries with under 2,000,000 population to \$5 million for countries over 10,000,000 population. -- Shares can be paid for only in gold and dollars. -- Countries may buy more than minimum amount of shares, but no country can have over 35 percent of voting power.

There is general agreement within the Treasury on the capital structure. There is some question whether the minima are too high for some of the weakest countries, but the answer to such a question waits on comment from the countries involved. There is also a question as to whether payment for shares might be allowed in "good values within the country" i.e., mortgages, rather than only gold and dollars.

2. There is a difference of opinion on who shall be the stockholders, the central banks or the Treasuries. -- Cochran and Cotton, and Gardner of Federal Reserve believe that the ownership of the stock shall not necessarily be confined to governments. The rest of us, however, feel it desirable to confine the participants to governments, each government would then determine what agency shall represent it.

3. How is American control assured? -- Important decisions require four-fifths vote of the Board. By holding 21 percent of voting power, U. S. can block action. -- The same is true of any government holding more than 20 percent of the stock. -- On Board of Directors is a director and an alternate from each country. No long-term credits can be extended without the approval of this Board. -- The Board names a President (probably an American) and two Vice Presidents who run the Bank in its day-to-day operations.

Cotton believes it desirable to have a small executive committee, elected by the Board, to function as the actual management.

4. Functions: The Bank's powers will include:

1. Long-term operations. -- Loans and credits may be made to governments, local governments, governmental entities and nationals providing that their government guarantees the loan. -- The Bank can lend out of capital, can guarantee the obligations of governments and agencies above mentioned, or it can sell debentures in order to get capital for making loans.

2. Short-term operations. -- Discounting and rediscounting government bills and other eligible paper, dealing in gold and silver, taking a position in local currencies, acting as a clearing house, providing expert advice, assistance in stabilizing currencies. -- The Bank may accept government deposits but not private deposits.

There was some question as to whether private deposits should be excluded. Although it is recognized that funds now going to Europe and the United States might be attracted for use in Latin America by deposit in such a Bank, the major objection is that local banks might be drained of deposits or feel that the Bank is acting as competitor.

5. Views of the five governments that have already answered the questionnaire.

NICARAGUA. Definitely favors a Bank. Reports that it has paper suitable for rediscount, sees the Bank as useful for clearing operations, needs aid for financing seasonal demands. But it emphasizes desire for long-term developmental assistance. It would want \$1 million for currency stabilization in addition to current Export-Import Bank credit provided the term is long and interest not over 2 or 2½ percent.

SALVADOR. Does not feel a need for a Bank, apparently. Its central Bank provides ample rediscounting facilities, it wants no funds for currency stabilization, sees no obstacles to trade within Latin America that the Bank could remove, its seasonal demands are well met by existing institutions. It does mention that the Bank would aid in perfecting the clearing process.

Division of Monetary
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HONDURAS. Does not need the Bank for seasonal demands for financing or to increase trade within Latin America. Does not have Treasury bills market locally. Would welcome foreign capital for development and is always ready to afford it proper protection. Might use long-term loan for currency stabilization, but would need make special study before knowing such requirements.

GUATEMALA. Is satisfied with existing institutions for handling seasonal peaks, does not see that interest rates be much lowered by Bank guaranteeing commercial paper, nor would Bank remove obstacles to Latin American trade, does not want loan for currency stabilization.

HAITI. Reply is unofficial, but it stresses adequacy of existing institutions for seasonal demands and Latin American trade; indicates that little Haitian money goes abroad. Is concerned with capital for long-run development and admits that if coffee sag of war is not offset by gains in cacao and in trade with U. S., a serious situation requiring outside aid might arise.

January 9, 1940.
3:00 p.m.

Present: Mr. Bernstein
Mr. Gaston
Mr. Foley
Mr. White
Mr. Hansen
Mr. Cotton
Mr. Cochran

H.M.Jr: All right, Doctor.

White: You have before you two memoranda. One is a digest, a brief digest of the other. The long memorandum represents the detailed plan for the bank drafted by the legal department chiefly in collaboration with our division. We had several meetings on this matter at which were - most of the people were here and Gardner and Goldenweiser were invited. Gardner came to all of them, I think, and Mr. Lincoln, we asked Mr. Lincoln of the S.E.C. to come to the last one merely in an advisory capacity in case there were any comments he had to make. If you would like to follow the memorandum called Highlights of the Plan, they raised the important matters. Then the details, if you want to go into them, or if you have time, will be in the accompanying one, which is below that.

H.M.Jr: You read them.

White: All right.

"Highlights of the Plan. The capital authorized one hundred million dollars."

.Do you want to stop at any point to raise questions?

H.M.Jr: I will.

White: "Initial subscriptions to be paid fifty percent of par at time of subscription, remainder on calls."

I think I have one more copy.

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"Minimum subscription for participation is arranged according to population groups and ranges from \$1 million for countries with under two million population to \$5 million for countries over ten million population. Shares can be paid for only in gold and dollars. Countries may buy more than minimum amount of shares, but no country can have over thirty-five percent of voting power."

They may buy more than thirty-five percent of the shares if they wish to, but they can't have more than thirty-five percent of the voting power, so if it is a hundred million dollars, presumably if the United States wished to buy the maximum voting power it would be thirty-five million dollars, for which you would have to pay seventeen million at once and the rest on call.

H.M.Jr: How did you arrive at thirty-five?

White: We wanted to get enough so as to insure veto power, which would be anything over twenty percent and not so much that it would appear that - either that we are dominating the bank or that we are the chief participants. Thirty-five we just picked out of the air. Forty seemed too high, twenty-five too low, but it is subject to any modification. There is no more in the figure than just that. Is there any other reason you can think of, Bernie?

Bernstein: With a figure around thirty or thirty-five, if you got perhaps one other big country or a group of small countries to go along with you, you would tend to have majority control. It is an arbitrary thing.

H.M.Jr: All right.

White: "There is general agreement within the Treasury on the capital structure. There is some question whether the minima are too high for some of the weakest countries,"

Some of the countries might have difficulty getting together half a million dollars in cash.

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"but the answer to such a question waits on comment from the countries involved."

We didn't think that we ought to attempt to decide that here.

"There is also a question as to whether payment for shares might be allowed in items other than gold."

We didn't think so, but there was some possibility of that. We thought that the bank ought to start off with either gold or dollars.

H.M.Jr:

Oh, yes.

White:

Do you feel that way?

H.M.Jr:

Oh, yes, definitely. You get a lot of crap.

White:

The second point of importance is, "There is a difference of opinion on who shall be the stockholders." Should it be Treasuries only or Governments only or central banks as well?

"Cochran and Cotton, and Gardner of Federal Reserve believe that the ownership of the stock shall not necessarily be confined to governments."

They thought that might well be left either to the committee or to the particular State.

"The rest of us, however, feel it desirable to confine the participants to governments; each government would then determine what agency shall represent it."

The rest of us feel rather strongly that it would be an error to have the residual control, the final control, in anything but the hands of Governments, or to go into the pros and cons of that, if you like --

H.M.Jr:

I certainly think it ought to be the Governments. I don't know - when they say other - who else could be?

White:

Central banks.

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- H.M.Jr: No, definitely not.
- Bernstein: Other possibilities that Berle mentioned are that in many of these countries there are such things as mortgage institutions or other fiscal institutions of the Government, perhaps comparable to our Export-Import Bank or R.F.C.
- H.M.Jr: The thing that always bothers me on this thing particularly is that if you once begin to make it something else that - I don't want the Central Bank.
- Gaston: I think anything else would be just one degree worse than the Central Bank. I should think that if you were going to exclude that you ought to make it Governments only.
- H.M.Jr: I wouldn't even say Treasuries, I would say Governments.
- Cotton: The only thing is that the sentiment of the committee is apparently the other way.
- H.M.Jr: I know.
- Cotton: It is a question of whether you get more cooperation.
- H.M.Jr: Berle is with me on this and when I spoke to the President the President of the United States feels very strongly and Berle said - I argued with him on this then when I was with the President, I remember.
- White: I think it is awfully important --
- H.M.Jr: Excuse me. He said I am in complete control and the Treasury is the agent for the Government.
- Bernstein: I think Berle may vary a little from that point of view he expressed to you, because he called me the other day after one of the meetings that we had here and said that he feared that in the case of some of the Governments they were so weak it might be preferable to have something else and hoped that the plan would permit that choice.

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- White: I think that is a specious argument, Mr. Secretary, which they are using a good deal and one reason why the committee seems to be rather stronger for it than one would suspect is because the chairman plays an important role in that committee and he is the central banker, Jaramillo, of Colombia, and gives it that kind of a twist.
- H.M.Jr: You tell them that I insist that only Democrats subscribe and I will settle on the Governments. If you put in the word "Democrats", I think there would be two subscribers. I am absolutely adamant on that. I have waged a battle here ever since I have been here against central banks as opposed to Governments as I feel very strongly on that.
- Cotton: That isn't the issue. This Government would do what it wanted through the Treasury. It is just the question of whether the other participant countries would be given an optional.
- Gaston: That is the same question the Secretary is speaking about. He has always insisted on dealing with Governments.
- Foley: If you have enough optionals, you will perhaps get control of this bank in private rather than in public interests.
- H.M.Jr: I have waged the fight in Government to Government against central banks and Merle Cochran was a swell ally and he carried out my orders explicitly and I won. That was a unique combination. I have been all through this with the European people. If you don't mind, I have had six years experience now and I would like - I take it you wonder how I feel and this is something I feel very strongly on.
- White: Shall we go to the next point?
- H.M.Jr: I have waged this fight for six years. When I was out of the country for one month - g. ahead.

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White: "How is American control assured? Important decisions require four-fifths -"

H.M.Jr: Herbert, you are with me on this, aren't you?

Gaston: Yes.

H.M.Jr: You have seen the fight ever since we have been here together.

Gaston: Yes. I think there are a good many reasons for making the Government take the responsibility.

Cochran: Don't think I wasn't sympathetic with that, Mr. Secretary. My only point is that it isn't a bank when we get the Governments running it.

H.M.Jr: The Governments are going to put up the money.

White: What would you call it?

Cochran: I would incorporate this committee of Government representatives.

White: What would you call the institution after it was going?

Cochran: I don't know what we would call it.

White: We would have to get a new name for it.

Cochran: I still think it is not a bank.

H.M.Jr: Well, that might be good if it wasn't a bank. Look, you who have been in on this with me for years, you know how I feel about and I don't - if I am going to put - I want to be dealing with Governments and I don't want to be dealing with mortgage banks or agricultural banks down in Mexico or anything. I want to be dealing with - at least if I am going to be double-crossed, I want to be double-crossed by a Government.

White: You are particular who double-crosses you, are you?

H.M.Jr: I am very particular.

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White: "Important decisions require four-fifths vote of the Board." And that makes it possible for any large holder that is having over twenty percent to stop any action but whether there will be more than two or three countries that will have that number of shares is doubtful.

H.M.Jr: I don't care.

White: Well, the rest is - "By holding twenty-one percent of voting power, United States can block action. The same is true of any Government holding more than twenty percent of the stock."

This is a rather disputable point, but rather a minor one, I believe.

"On Board of Directors is a director and an alternate from each country. No long-term credits can be extended without the approval of this Board. The Board names a President," and they all stated at the meeting that it should be an American. They may change their minds.

H.M.Jr: I don't care.

White: "... and two Vice Presidents who run the Bank in its day-to-day operations."

H.M.Jr: That stuff doesn't interest me.

White: There was some question as to whether power ought to be lodged in the executive committee, etc. Now then, let's go to the functions of the bank's power. I think since we have made so much progress up to that point, you might prefer to go to the exact details on the powers.

H.M.Jr: On page 2?

White: On page 4 of the other memorandum.

H.M.Jr: Can't I read page 2 here?

White: All right, if you like.

(Pause)

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- H.M.Jr: On that paragraph, could they take deposits, I think they ought to have that privilege and then they could always --
- White: We were afraid it would give a great deal of opposition on the part of the banks in the areas who would immediately say that this bank, which will be in a very privileged position and have a lot of prestige that the other banks don't have, will draw away a lot of the deposits of those who are otherwise worried about exchange losses, etc.
- H.M.Jr: If they can get away with it, it helps the bank.
- White: You have no objection, then, to their having --
- H.M.Jr: No.
It ought to, Joe?
- Cotton: Some think it ought to.
- H.M.Jr: You say they do now?
- Cotton: They implicate they do.
- H.M.Jr: Now, what do you want me to read after that?
- White: These others, the statements about Nicaragua and Salvador and so on. They have cabled back their answers to the questionnaire and it might be of some interest to see their reactions, but I think it would be preferable at this time to go through the specific powers or plans, through them to see whether --
- H.M.Jr: All right, it will take me a minute to read them.
(Pause)
Now, do you want me to go to page 4?
- White: There are some points there I would like to raise for your attention.

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- H.M.Jr: Herbert, have you seen all this?
- Gaston: I haven't had time to read it before.
- White: It is the yearly net profits of the bank shall be applied as follows on page 4 of the other memorandum.
- H.M.Jr: I don't want to get in on that. Don't you want to read the objectives and power?
- White: All right, if you want to pass by that, then the next thing you might be interested in is the stated objectives, although we have included everything under the sun there that sounds good. Then under the powers, the only one that might - the only one is (e), "Buy, sell, hold and deal in precious metals." We want to include silver and gold in there.
- H.M.Jr: I guess you have got everything in there but manufacturing, haven't you?
- White: Pretty nearly. There is everything in there that - except it is clear that they can't make a loan to any part of a Government unless the Government itself guarantees it. That was in the other. Then there is some question about the extent of the immunity from taxation and freedom from exchange controls that this bank will have. With regard to exchange controls, we thought that we might be willing to agree that the assets that the bank might have in the United States would be free from any exchange controls that might subsequently be imposed in order to get the same thing among other countries.
- H.M.Jr: Now that would be all right to have that. That doesn't tie our hands.
- White: No, it doesn't.
- H.M.Jr: Does it?
- Bernstein: Well, to a limited extent, to the extent that we also would be giving the bank tax immunities and freedom from exchange control.

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White: But to that extent, in other words, if the bank had twenty million dollars on deposit in the United States, exchange controls would not apply to the privilege of withdrawing those twenty million if we were to grant them that immunity.

H.M.Jr: But of course - well, that is the unwritten law with central banks, isn't it?

Cochran: Yes, between central banks, but here you are getting deposits from individuals, presumably.

White: This wouldn't apply to deposits. It would apply only to the bank's assets, though the bank in turn might hold deposits of others. The exemption from exchange control, I take it, would apply directly to the bank's assets or at least that is as far as we have been willing to go here.

Then with regard to tax immunities, that raises some problems that we haven't gone into. I don't know how far they will want it or how far you would wish to make an exception of the bank having its assets exempt from Federal taxation.

H.M.Jr: Every country is different because they pay the normal tax. I think they ought to be subject to the same tax as any national bank.

White: Or possibly given the same treatment as any Central Bank.

Bernstein: You might get an argument from some of these countries that that would be a device for this country draining off the profits of the bank.

H.M.Jr: I will tell you gentlemen the way I feel. Without stopping doing what I am and devoting two or three or four days or a week to this thing, I don't feel that my comments are of sufficient value, because I haven't studied this. I don't like to comment on the thing unless I am going to - and I am not going to give up a week to study it. I am going to rely on you fellows. The only thing I

feel strongly on is, I would like to deal Government to Government. I want to ask one other question.

Where is the capital going to come from that we raise?

White: Mr. Bernstein has a tentative draft of a statute and the way in which the bank would have to originate, as far as American powers are concerned, is on the last stage, I think, of that, and he has a draft of the statute which he hasn't given you.

H.M.Jr: Where would the money come from?

Bernstein: Through a Congressional appropriation, so far as our contribution is concerned. I think that in addition to that you might want Congress to give you powers to buy the debentures of the bank, to make deposits with the bank of moneys and precious metals, and of course to appoint the directors and delegates.

H.M.Jr: I say, without giving up a week to study this thing, I am not that conceited that I can contribute anything, so I am willing to leave it with this group and see what happens. I just haven't got a week's time to devote to it.

White: The next stage of this is to present just that portion of the draft of the powers of the bank and the management, etc., as we have stated, to Berle with the statement that the Treasury is favorable to this without necessarily committing you specifically to each item.

H.M.Jr: I would like this to go to the 3 E's and ask them to give us their comments.

White: You would like to do that before we - before Mr. Berle has his meeting?

H.M.Jr: Get it as fast as you can, I mean, but they are not going to adopt the thing - but I would like the 3 E's to get a copy and ask

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them please to give us their criticisms.

- White: Would you like also to send a copy at this stage of the game to the S.E.C. to have them go over it to see whether there is anything in it --
- H.M.Jr: Sure.
- Cotton: I think there is some feeling in the State Department that Mr. Jones ought to be called in.
- White: Why should that be our job?
- Cotton: I was just going to mention it.
- H.M.Jr: We have got all we can do to keep Jones - you saw yesterday. Were you here?
- Cotton: Yes.
- H.M.Jr: From going to see Traphagen and --
- Cotton: I merely mentioned that.
- H.M.Jr: Well, that is up to them.
- Cotton: They think it will be important on the Hill.
- H.M.Jr: Well --
- White: After all, this is merely for Mr. Berle.
- H.M.Jr: That is all right, Joe, you bring these things up, that is what you are here for, but advising me - I would like to have the advice of the 3 E's. Now, Adolph Berle, what he does with this thing, that is his business. If he wants to give it to Jesse, that is O.K. Jesse always has his own ideas. He is an individualist. He has been very successful, but he is very difficult to work with. He wants you to go his way. Is that right?
- Foley: Right.
- Cochran: Does the appropriation come to the Treasury Department, Bernie, and then the Treasury subscribes?

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Bernstein: What would happen is the Act of Congress would authorize the Secretary of the Treasury with the approval of the President to use funds in the Treasury to buy the stock and debentures and so on. The money always comes out of the Treasury. The authorization is an Act of Congress and presumably the Act would authorize the Secretary to act with the approval of the President.

H.M.Jr: You fellows, this is a nice job and you are having a lot of fun and I wish you all a good time.

Cotton: Is this going to be given to Berle now?

White: My thought was as follows, to see whether there was any point that anybody wanted to raise after they got out of here, any changes to be made, and then to tell Mr. Berle that the Secretary's first reaction to this is favorable, without having gone - examined each point carefully enough so that he does not get - doesn't want to be in the position of being committed.

H.M.Jr: I reserve all rights.

White: And then we will send the 3 E's and then --

H.M.Jr: I am reserving all rights.

White: Yes, I will tell him that.

H.M.Jr: In the meantime, get the letters off to the 3 E's. Please ask them to - that I am asking you to send it. I would like to have their comments and advice.

White: All right.

H.M.Jr: Then we will get along.

White: O.K.

Cotton: I have a feeling, Mr. Morgenthau, that if this thing was discussed frankly enough in the sense that it will be made plain that the veto power of the United States will probably be used to block

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any allowance to any Government, making a reasonable effort on existing debts which would be in default, that the thing would blow up, and I think it is a little dangerous to have it go on without getting down to some talk like that. I think those boys are ready for it. I don't know whether Berle ever contemplates --

- White: I don't see why we have to take this position at this time, to say what the Board will or will not do in the matter of these loans.
- H.M.Jr: Is this a question or a recommendation?
- Cotton: Well, it is a question of how Berle will discuss this and present it. It will become a Treasury project.
- H.M.Jr: But do I understand that - are you advising me to --
- Cotton: All I am saying is whether this bank will ever do anything substantial or not, probably its long-term investment function is the most important one and the other type of business wouldn't justify the creation of the bank. That means large scale lending of Government money through the medium of this bank and immediately the same old question is going to come up when the United States stands for the veto power and Mexico or somebody else comes in for a loan, what happens. If you don't lend, there is political disillusionment over the whole thing. If you do lend, there is something else.
- H.M.Jr: Again, I am going to nail you down. If this bank was running and the Treasury had a representative and I asked you the question, "Now, shall we make Colombia a loan," and the Colombian debt was still in default, what would your advice be?
- Cotton: I would say, probably, no, I think. That is the kind of thing the committee, it seems to me, is thinking of, whether they are going to be able to get long-term loans.

H.M.Jr: Maybe I am too casual, but the way I feel is, they wanted us to take it to do a job or sort of draw up a charter for them because we have got technicians. Now, we have done it and this is something that Mr. Welles wants very much and Mr. Berle wants very much and the President wants very much. You have done the technical work, why not let them have it.

Cotton: All I am saying is, I think if this Government would back that project in that committee and then later on it turned out that its policy was what appears to be an existing policy in regard to that matter of loans, it would be a terrific disillusionment. I don't know whether Berle will get to that plane of discussion or not.

H.M.Jr: Do you mind me raising this? I take it from what you say you don't think the Export-Import Bank should make a loan to any country in South America that is in default.

Cotton: No, I am not saying that, Mr. Morgenthau. I don't know, but the policy, I mean the policy of this Government up to the point has been to try and encourage settlements and there has been sort of discriminatory lending on that basis by the bank.

H.M.Jr: I think you are wrong. I haven't seen anything like that. I think you are wrong.

Cotton: Well --

H.M.Jr: Well, what country?

Cotton: Well --

H.M.Jr: I haven't been conscious of it.

Cotton: The only two places that it has been done, it has been done some in Brazil, a little bit in Colombia, and a little bit in Chile. The other cases --

H.M.Jr: Not as far as the Treasury is concerned. I have never been conscious of the fact

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and - that if a country owed money we wouldn't give them any credit. If you asked me if the two things go together, I wouldn't say yes.

Cotton: I don't propose to say what the policy of the administration should be, but if this project was put up in such a way that they were led to believe it was a change of policy, I don't know whether that is what you mean to do, that is all I am trying to say.

H.M.Jr: Let me get this. Harry, you sat over there. Have they withheld loans or haven't they? I am interested.

White: I think possibly what Joe has in mind is that they have used their lending power and no one is more cognizant of that than you, I am sure, because that was the basis of the whole discussion with the State Department. I take it that Joe has in mind that there has been some withholding of potential loans awaiting settlement of defaulted debts and using the possibility of making those loans as pressure, but I don't think there has been a definite statement of policy to the effect that we will not make a loan because a country is in default.

H.M.Jr: Have you ever heard me --

Cotton: I think you have stated that just right, Harry.

H.M.Jr: Have you ever heard me in this room ever say that?

White: The latter, no, I say, definitely not.

H.M.Jr: Or anything on that end?

White: I think you have taken the position, which I am not sure that that is the issue, that a Government, if it is going to make a settlement prior to a loan, if that is going to be the condition of the loan, then we oughtn't to require of them that they make an unreasonable settlement, that if we make the granting of a loan,

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any kind of a condition --

H.M.Jr: No, let me tell you what I have said. I said that I hoped we could take some country and consider it just as we would with a business man that had a fire or collapse, and completely reorganize his business and lend him enough money to see that he could go on and be sufficiently productive that he could pay off his old loan or part of his old loan, write down his own loan if necessary, and then he could go ahead and make enough money to pay off his new one.

White: That is how I understand your position and that is why I don't feel that Joe is concerned about stating at this stage of the game any conditions as to under what conditions the loan shall or shall not be made, because your position has been up to now that you wanted to consider the condition which the country is in, see what you can do for them, see what you can do to put it on its feet.

H.M.Jr: I think where Cotton is most likely right, what happened in the case of Brazil was that Francis White and his gang had enough influence to kill our doing anything there until there was a settlement.

Cotton: Well, what is in the back of my mind, a condition of that sort is --

H.M.Jr: What is in the back of your mind?

Cotton: This project is going to be a Treasury baby, that is inevitable. Does this mean large scale lending in South America? If you go up to Congress and back it, you will have to take the responsibility for it.

H.M.Jr: No.

White: Yes.

Cotton: I think that is the position you are --

H.M.Jr: I am not going to present this to Congress.

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White: They may ask the Treasury whether it approves and the Treasury can definitely on this basis say, if it emerges something like this, that it feels the thing has sufficient possibilities to warrant going ahead. Now, when some one asks the specific question, "Do I understand that you are going to use this bank to make a loan to Mexico," why I suppose the appropriate answer under those circumstances is that the Board of Directors will have to consider the whole situation at the prevailing time. It is a group project.

Cotton: It is right on your doorstep, probably right away, in the sense of the Treasury holding the voting power.

White: The Treasury isn't now called upon to decide whether or not it is going to make a loan for Mexico, because in the first place the institution doesn't exist and in the second place Mexico hasn't asked for a loan. When it does exist and has asked for a loan and the representative, I take it, will confer with the Government and what position they will take at that time, I don't see how you could tell ahead of time.

H.M.Jr: I hope that this bank or our interest in this bank wouldn't be abused by more than our gold or silver policy has against any country who happened to be doing some unfriendly act to our nationals at the moment, see. Now, I have always resisted that. But I think what you ought to do is make perfectly plain to Berle that if it comes to selling this thing on the Hill, I am going to expect the State Department to sell it. Maybe that will accelerate his getting a memorandum over to Mr. Jones, which is all right.

White: That does not mean the same thing, I take it, as - in response to any question that you might be well asked, as to how does Treasury feel, how does the Secretary of the Treasury feel on it. That is different.

H.M.Jr: We would give them a letter which you fellows can write, that is different, but I am not going to go through again what I went through

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on the self-liquidating program.

Cochran: Doesn't this setup call - I mean, the appointee would be yours, presumably, and he would come to you for instructions. If he needed more capital and so on, bigger appropriations, it would be the Treasury's responsibility.

Cotton: Isn't it true in an economic sense, too, Harry, that this bank could only lend, say, about twenty-five million dollars in long-term unless you maintain very large deposits and - or bought an enormous amount of debentures.

White: Unless they could use what I take it is the medium they will be able to use, and that is underwriting by guaranteeing loans, floating them on various principles. You might be willing to accept a contingent liability of a pretty substantial amount.

Cotton: I am just a little afraid that is going to be a Treasury baby and that is certainly what Mr. Berle is trying to push you into, don't you have that feeling? I just want you to realize what you are getting into.

White: I don't know what you mean by Treasury baby. It is the United States Government that is represented on the Board and the Secretary of the Treasury will doubtless have some - what sense is there to Treasury baby, per se?

Cotton: He asked the Treasury to prepare it and he - it is going to be the Treasury's baby.

Gaston: You are thinking of the prospect that the operating responsibility will be largely the Treasury's, I suppose, in addition to other things.

White: The thing has got legitimate parentage. Even if it is our baby, we need not be ashamed.

Cotton: Mr. Morgenthau seems to think we should send over a document and have the feeling that our technical people have just prepared something and I think we are getting into a large responsibility.

White: One of the ways of avoiding that is what I think they are going to do, send this over

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to the Federal Reserve Board and get them to make suggestions and changes and also the S.E.C., so that every - and possibly Mr. Jones, so that every agency that is related in any way to the lending problem will have had an opportunity to comment on this procedure. All that we have done to date is --

H.M.Jr: Well, I appreciate what you are doing, Joe. You are running up a red signal light and I am also saying that we will send it over. I am reserving all rights. I want to see what the 3 E's have to say. I am saying just perfectly frankly I haven't got the time to give this a week's study, so we will just have to rely on you people. I have done it before. But thanks for running up the red light. We will take the chances. Look, they come in here and they get me in a corner here and Jones and Welles - Jones says, "How about a loan to Norway?" I don't know about a loan to Norway. Why does he want to make a loan to Norway? So that the loan to Finland doesn't look so bad, see. They do these things.

Incidentally, the English have now agreed - we are not supposed to know that they are going to buy whatever commodities Finland gets through the loan of the Export-Import. They are going to furnish them with dollars. I mean, all that kind of stuff is - let's say tricky - in the sense not that we are trying to fool them but delicate so that this seems to be very regular by comparison.

Cotton: That is probably true. That sounds reasonable to me.

Gaston: I doubt that there will be any criticism.

H.M.Jr: It seems very regular by comparison, which also doesn't make two and two. I know what I am saying and I am sure you men have done a good job. You have checked it with these other people and then we will see what happens.

Gaston: I doubt if there will be any great shock or disillusionment on the part of the South or Central American countries if this tentative

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setup should go through. I don't think they would think we are absolute suckers and there are some pretty reasonable men there. I think they would be pleased, those who are advocating the Pan-American Bank idea, to get something along this line. I think they would be greatly pleased.

H.M.Jr: All right, gentlemen, God bless you all.

January 9, 1940

Secretary Morgenthau

Mr. White

Subject: Highlights of plan for Pan American Bank.

1. Capital: Authorized \$100,000,000. -- Initial subscriptions to be paid 50 percent of par at time of subscription, remainder on calls. -- Minimum subscription for participation is arranged according to population groups and ranges from \$1 million for countries with under 2,000,000 population to \$5 million for countries over 10,000,000 population. -- Shares can be paid for only in gold and dollars. -- Countries may buy more than minimum amount of shares, but no country can have over 35 percent of voting power.

There is general agreement within the Treasury on the capital structure. There is some question whether the minima are too high for some of the weakest countries, but the answer to such a question waits on comment from the countries involved. There is also a question as to whether payment for shares might be allowed in "good values within the country" i.e., mortgages, rather than only gold and dollars.

2. There is a difference of opinion on who shall be the stockholders, the central banks or the Treasuries. -- Cochran and Cotton, and Gardner of Federal Reserve believe that the ownership of the stock shall not necessarily be confined to governments. The rest of us, however, feel it desirable to confine the participants to governments, each government would then determine what agency shall represent it.

3. How is American control assured? -- Important decisions require four-fifths vote of the Board. By holding 21 percent of voting power, U. S. can block action. -- The same is true of any government holding more than 20 percent of the stock. -- On Board of Directors is a director and an alternate from each country. No long-term credits can be extended without the approval of this Board. -- The Board names a President (probably an American) and two Vice Presidents who run the Bank in its day-to-day operations.

Cotton believes it desirable to have a small executive committee, elected by the Board, to function as the actual management.

4. Functions: The Bank's powers will include:

1. Long-term operations. -- Loans and credits may be made to governments, local governments, governmental entities and nationals providing that their government guarantees the loan. -- The Bank can lend out of capital, can guarantee the obligations of governments and agencies above mentioned, or it can sell debentures in order to get capital for making loans.

2. Short-term operations. -- Discounting and rediscounting government bills and other eligible paper, dealing in gold and silver, taking a position in local currencies, acting as a clearing house, providing expert advice, assistance in stabilizing currencies. -- The Bank may accept government deposits but not private deposits.

There was some question as to whether private deposits should be excluded. Although it is recognized that funds now going to Europe and the United States might be attracted for use in Latin America by deposit in such a Bank, the major objection is that local banks might be drained of deposits or feel that the Bank is acting as competitor.

5. Views of the five governments that have already answered the questionnaire.

NICARAGUA. Definitely favors a Bank. Reports that it has paper suitable for rediscount, sees the Bank as useful for clearing operations, needs aid for financing seasonal demands. But it emphasizes desire for long-term developmental assistance. It would want \$1 million for currency stabilization in addition to current Export-Import Bank credit provided the term is long and interest not over 2 or 2½ percent.

SALVADOR. Does not feel a need for a Bank, apparently. Its central Bank provides ample rediscounting facilities, it wants no funds for currency stabilization, sees no obstacles to trade within Latin America that the Bank could remove, its seasonal demands are well met by existing institutions. It does mention that the Bank would aid in perfecting the clearing process.

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HONDURAS. Does not need the Bank for seasonal demands for financing or to increase trade within Latin America. Does not have Treasury bills market locally. Would welcome foreign capital for development and is always ready to afford it proper protection. Might use long-term loan for currency stabilization, but would need make special study before knowing such requirements.

GUATEMALA. Is satisfied with existing institutions for handling seasonal peaks, does not see that interest rates be much lowered by Bank guaranteeing commercial paper, nor would Bank remove obstacles to Latin American trade, does not want loan for currency stabilization.

HAITI. Reply is unofficial, but it stresses adequacy of existing institutions for seasonal demands and Latin American trade; indicates that little Haitian money goes abroad. Is concerned with capital for long-run development and admits that if coffee sag of war is not offset by gains in cacao and in trade with U. S., a serious situation requiring outside aid might arise.

HDW:esh
1/9/40

The proposed Pan-American Bank would be set up somewhat in the following manner:

All participating American countries will subscribe to a convention which will be approved in each country according to its laws. By the terms of the convention the participating countries will grant the bank, its employees, and its operations certain tax immunities (to be considered further) and protection from expropriation and exchange controls (to be considered further), etc., and the countries will agree to pass any legislation necessary to effectuate such immunities, etc. The United States (where the bank will have its principal office) will undertake to grant the bank a charter for a specified time and agree not to abrogate or amend the charter during such time otherwise than pursuant to a resolution of the bank approved by a four-fifths majority vote of the Board of Directors. Each participating country will agree to permit the functioning in its territory of the bank, through a branch or otherwise, and to enact any necessary legislation. The charter setting up the bank will approve the by-laws, a draft of which is annexed.

When five or more countries subscribe to the convention and agree to subscribe to the minimum stock, the bank will be organized. Any American countries which do not originally participate in the bank but later desire to do so would have to subscribe to the convention at the time of entry as well as subscribe for the minimum shares of stock and comply with any other terms and conditions imposed by the Board of Directors.

Suggested Outline for a Bank to
be Called the Pan-American Bank

1. Location

The principal office of the bank shall be in the U.S.A. and branches may be established anywhere in the Western Hemisphere.

2. Capital Structure and Participation

A. The capital stock shall be expressed in U. S. dollars (hereafter referred to as dollars) and shall be authorized in the amount of \$100,000,000 consisting of 1000 shares having a par value of \$100,000 each to be paid for in gold or in dollars. The stock shall be issued at par and 50% of the par value of each share shall be paid up at the time of subscription. The balance may be called up at a later date or dates at the discretion of the Board of Directors of the Bank. Two months' notice shall be given of any such calls.

B. Stock shall be available for subscription only to independent American governments. For a government to participate in the bank it must subscribe to a minimum number of shares depending upon the population of the country. The population of the eligible countries are estimated as follows:

	2,000,000 or less	Costa Rica, Dominican Republic, Honduras, Nicaragua, Panama, Paraguay, Salvador.
Over	2,000,000 and up to 5,000,000 -	Chile, Bolivia, Cuba, Ecuador, Guatemala, Haiti, Uruguay, Venezuela.
Over	5,000,000 and up to 10,000,000 -	Colombia, Peru.
Over	10,000,000	- United States, Mexico, Argentina, Brazil.

The minimum number of shares shall be: 10 shares for countries having a population less than 2,000,000; 20 shares for countries having a population of from 2,000,000 to 5,000,000; 30 shares for countries having a population of from 5,000,000 to 10,000,000; 50 shares for countries having a population over 10,000,000. Each participating country may subscribe to stock in addition to the minimum. Where the demand for such additional stock exceeds the amount to be issued by the bank, the demands, in

excess of the minimum, will be met on an equal basis.

C. Eligible governments which do not participate in the bank at the time of its formation shall be permitted to participate in the bank, upon subscribing for the minimum number of shares, subscribing to the convention and after complying with any other terms and conditions designated in regulations of the bank.

D. Liability of a shareholder on its shares shall be limited to the par value of the shares held by it.

E. If a government fails to pay any call on a share on the day appointed for payment thereof, or defaults on any obligation to the bank, the bank may, after giving reasonable notice to such government, forfeit an appropriate number of such government's shares. The fair value of the shares shall be determined by the bank, and such value shall be applied to the payment of the amount due by such government to the bank. The bank may also sell such forfeited shares to any other participating or eligible government. The value of the shares or the proceeds of the sale over and above the amount due to the bank shall be paid to the government whose shares were forfeited.

F. Shares of stock may be transferred only to the bank or to other participating governments at a price to be agreed upon between the parties and upon the approval of the transfer by a four-fifths majority vote of the Board of Directors. If, as a result of the transfer or forfeiture of shares of stock or for any other reason, a government holds less than the minimum amount of shares of stock required of it, such government shall cease to participate in the bank, but its obligations and duties with respect to the bank shall continue.

G. The capital structure of the bank, including the number and par value of shares and the minimum holdings of participating governments, may be increased or decreased by a four-fifths vote of the Board of Directors.

H. The voting power of each government on the Board of Directors shall be distributed as follows: 10 votes for each government for its minimum shares, and 1 vote for each additional share. However, regardless of the amount of stock owned by it, no government shall exercise more than 35% of the total voting power of the outstanding stock.

3. Management

A. The administration of the bank shall be vested in the Board of Directors composed of one director and one alternate appointed by each participating government. Each government shall have complete freedom in the method selected by it in appointing its director and alternate. Such director and alternate shall serve for such period or periods as shall be determined by their government.

B. Meetings of the Board of Directors shall be held not less than four times a year and may be held either at the principal or any branch office or at any other city in a participating country as the Board of Directors may determine.

C. The Board shall select a president of the bank who will be the chief of the operating staff of the bank and who also shall be ex officio chairman of the Board of Directors, and one or more vice presidents, who shall be ex officio vice chairmen of the Board of Directors. The president and vice presidents of the bank shall hold office for one year and shall be eligible for reelection.

D. The Departmental organization of the bank shall be determined by the Board. The heads of departments and other similar officers shall be appointed by the Board on the recommendation of the president. The remainder of the staff shall be appointed by the president.

E. The Board may also appoint from among its members an executive committee to supervise the administration of the bank.

F. The Board may appoint advisory committees chosen wholly or partially from persons not regularly employed by the bank.

G. Before the Board approves an intermediate or long-term loan or extension of credit it shall have before it a full written report on the merits of the proposed transaction prepared by a committee of experts which may include officers and employees of the bank.

H. Except as herein otherwise provided, decisions of the Board shall be by simple majority of the votes cast. In the case of equality of votes, the chairman shall have a deciding vote. The Government may vote at meetings either through the director or alternate or through a nominee or proxy in such manner as the Board may provide by regulations. When deemed by the president to be in the best interests of the bank, decisions of the Board of Directors may be made

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without a meeting by polling the directors on specific questions submitted to them in such manner as the Board of Directors shall by regulations provide. The Board of Directors shall by regulations determine what constitutes a quorum for a meeting.

I. Approval by four-fifths majority vote of the Board of Directors shall be required for the making and granting of intermediate and long-term loans and credits, including intermediate and long-term loans and credits guaranteed by the bank; the acquisition and sale of intermediate and long-term obligations and securities; the discounting or rediscounting of intermediate or long-term paper; the issuance of debentures and other securities and obligations of the bank; the determination of the functions and duties of the officers and principal employees of the bank, and who may legally commit the bank vis a vis third parties and in what manner; and for amending the by-laws. Four-fifths majority vote of the Board of Directors, as used herein, means four-fifths of the votes cast.

4. Accounts and Profits

31. A. The financial year of the bank shall end on December
- B. The books and accounts of the bank shall be expressed in terms of the United States dollar.
- C. The bank shall publish an annual report and at least once a month a statement of account in such form as the Board may prescribe. The Board shall cause to be prepared a profit and loss account and a balance sheet for each financial year. All published documents shall be printed in the official languages of the participating governments.
- D. The yearly net profits of the bank shall be applied as follows:

1. Not less than 25% of such net profits shall be paid into surplus until the surplus is equal in amount to the par value of the authorized capital stock of the bank;

2. The remainder of such net profits shall be applied towards the payment of a dividend of not more than 3% per annum on the amount of the paid-up capital of the bank: Provided, however, that dividends shall

be non-cumulative and no dividends shall be paid so long as the capital of the bank is impaired.

3. The balance of such profits shall be paid into surplus and be designated a dividend reserve.

E. The Board of Directors by a four-fifths majority vote may declare dividends out of the dividend reserve in surplus of the bank provided, however, that total dividends in any one year shall not be more than 3% of the paid-up stock.

F. The bank may not be liquidated except by a four-fifths majority vote of the Board of Directors. Upon liquidation of the bank and after discharge of all the liabilities of the bank, the assets remaining shall be divided among the shareholders.

G. The shares shall carry equal rights to participate in the profits of the bank and in any distributions of assets upon liquidation of the bank.

V. OBJECTIVES AND POWERS

The Bank is created by the American States to carry out the following purposes:

(a) Facilitate the prudent investment of funds and stimulate the full productive use of capital.

(b) Assist in stabilizing the currencies of American States; encourage the maintenance of adequate monetary reserves, promote the use and distribution of gold and silver; and facilitate monetary equilibrium.

(c) Function as a clearing house for, and in other ways facilitate, the transfer of international payments.

(d) Increase international trade, travel and exchange of services in the Western hemisphere.

(e) Promote the development of industry, agriculture, commerce and finance in the Western hemisphere.

(f) Foster cooperative action among the American States in the fields of agriculture, industry, marketing, commerce, transportation and related economic and financial matters.

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(g) Encourage and promote research in the technology of agriculture, industry and commerce.

(h) Engage in research and contribute expert advice on problems of public finance, exchange, banking and money as they relate specifically to the problems of American States.

(i) Promote publication of data and information relating to the objectives of the bank.

For the purpose of carrying out the foregoing objectives the bank shall have the following specific powers:

(a) Make short-term, intermediate and long-term loans in any currency and in gold or silver to participating governments and to fiscal agencies, central banks, political subdivisions and nationals thereof on such security as the bank may require; provided that the government of the borrower shall specifically recommend and guarantee any such loan to such fiscal agency, central bank, political subdivision and national.

(b) Buy, sell and deal in the obligations and securities of participating governments and of fiscal agencies, central banks, political subdivisions and nationals thereof provided such obligations and securities are guaranteed by participating governments.

(c) Guarantee loans made from any source to participating governments and to fiscal agencies, central banks, political subdivisions and nationals thereof, provided that the loans are guaranteed by the government of the borrower.

(d) Act as a clearing house of funds, balances, checks, drafts, acceptances.

(e) Buy, sell, hold and deal in precious metals, currencies and foreign exchange for its own account and for the account of others.

(f) Issue debentures and other securities and obligations to secure additional assets for the purposes of the bank.

(g) Borrow from participating governments and from fiscal agencies, central banks and political subdivisions thereof if approved by the government of the lender.

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(h) Accept demand and time deposits and custody accounts from governments and fiscal agencies, central banks and political subdivisions thereof if approved by the government.

(i) Discount or rediscount for participating governments bills, acceptances and other short-term obligations and instruments of credit of participating governments and fiscal agencies, central banks, political subdivisions and nationals thereof and rediscount with any participating government or any fiscal agency or banking institution designed by such government bills, acceptances and instruments of credit taken from the bank's portfolio.

(j) Open and maintain time and demand and custody accounts with governments and banking institutions and arrange with governments and banking institutions to act as its agent or correspondent.

(k) Accept deposits and act as trustee in connection with arrangements that may be made in connection with inter-American settlements.

(l) Act as agent or trustee of any participating government and fiscal agencies, central banks and political subdivisions thereof if approved by the government.

(m) Engage in financial and economic studies and publish reports thereof.

B. The Board of Directors shall determine the nature of the operations which may be undertaken by the bank in the exercise of its powers and for the purpose of effectuating its objects. The operations of the bank shall at all times, so far as possible, be conducted in conformity with the policies of the participating government directly concerned.

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Legation, Quito, Ecuador

NO.: 1

DATE: January 9, 1940, 9 p.m.

For the attention of the Honorable Boaz Long.

Reference is made to telegram no. 1 from the Department, dated January 6, 4 p.m. The following is Mr. Hart's report:

"Referring to the Legation's despatch no. 559, dated July 10, 1939, I would change the southern route to go from Saracay near Piedras to Santa Rosa to Aremillas and from there to Tumbes. Six Allis Chalmers tractors and related equipment which is now arriving is taking care of the part between Pinas and Piedras. In addition I have recommended gravelling and rolling equipment but this has not yet been ordered.

"My suggestion for a loan project would be the completion of the Pan American route. I believe this could be done for \$1,000,000 by using two tractor units of four each together with allied equipment and rock plants, one unit to begin at Guamote and work approximately 130 kilometers southward to Tambo and the other unit to begin at Tarqui and work approximately 200 kilometers southward to Loja. There should be included several American

instructors

-2-

instructors and engineers.

"Referring to telegram no. 2 of January 6, 5 p.m. from the Department, a road has been proposed from Cuenca to Puerto Bolivar via Giron and Pasaje, but it would be necessary to cross very rough country. Besides, the railway from Cuenca to Guayaquil already provides an outlet to the coast. I recommend passing through Loja since Loja ought to be connected to Cuenca as part of a main trunk highway. I have read Engineer Gevallos' correspondence and have conferred with him. Since it appears that Peru has a good highway to Tumbes, it was his idea to construct by Loja to Santa Rosa and from Santa Rosa to Tumbes. A spur from Loja to Macara was offered for use when the Government of Peru completes the highway up to Macara. Since all of the Loja-Macara construction would go through steep mountains which are sparsely populated, I believe that it should be postponed until roads which are more urgently needed have been completed.

"With reference to the telegram from the Minister, the following shows the projects under way with the number of men employed on each: Piedras Pinas 150 day labor, Pinas Loja betterment 600, Loja Saragura 400 piece work, Quito Santo Domingo 500 by piece work.

Piedras

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Piedras Pinas, Pinas Loja and Loja Saragura use South American development funds. The Hacienda Lumbahua (not Zarama) to Macuchi mine is to be constructed with South American development funds which will be available during the next year. Army work is as follows: Pun road 410 men, large contract, Banosmera, 610 contract, Paute Mendez to begin before long. No work of any size is being done on Sibambe Tambo, and from Santo Domingo to Manta there is no work in progress. I believe that in economic importance this route outranks the Pan American highway; not administratively, however. Grading would be required on 150 kilometers and graveling on 250 kilometers. A contract has been let for emergency construction. They are often two months behind on pay; however, the work continues, although on a reduced scale. In most of the Sierra region there is considerable hand labor available, but this becomes scarcer at lower elevations. I would suggest, with respect to technical aid, that an adviser and several American mechanics to instruct be provided for each group. A summer road with floating bridges is being considered for the Quevedo Porto Viegjo route; however, I would not recommend that the United States participate in a road of this kind. The river and a summer road now provide Quevedo with an outlet to Guayaquil.

"It

"It is my opinion that the United States should put a loan on the Pan American highway but I believe that Ecuador should agree that it will not cut down or divert its current rate of expenditure for roads but that such appropriation should be used on other routes of economic importance."

EA:EB

TO THE SECRETARY OF STATE
WASHINGTON, D.C. 20520
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RECEIVED
DEPARTMENT OF STATE

JAN 9 1940

My dear Senator:

Further reference is made to your letter of December 22, 1939, requesting certain information with respect to obligations and capital stock of Government agencies or corporations held by the United States Treasury; whether such obligations or stock could be sold in the market or redeemed by the issuing corporation without involving liquidation of the corporation; and if sold or redeemed, whether the proceeds would be covered into the general fund of the Treasury and be available for disbursement for ordinary expenses without specific authorization or appropriation by Congress.

The questions will be answered in the order presented in your letter:

Paragraph 1: At the present time the Treasury holds obligations of Government corporations (exclusive of capital stock) as follows:

Reconstruction Finance Corporation 1% notes, Series Q-2, due Jan. 1, 1942	\$ 5,898,445
Federal Farm Mortgage Corporation 3/4% bonds, due Sept. 1, 1940.	10,000,000
Home Owners' Loan Corporation 1/2% bonds, Series N, 1939-40.	20,000,000
Tennessee Valley Authority 2-1/8% bonds, Series A, due Dec. 15, 1948.	272,500
Tennessee Valley Authority 1/2% Interim Certificate, due from Feb. 15, 1943, to Aug. 15, 1969	50,000,000
U. S. Housing Authority 1/2% notes, Series C, due June 30, 1940.	10,000,000

Paragraph 2: Under the Acts authorizing the purchase of the above-mentioned obligations by the Secretary of the Treasury, there is authorization for their sale in the market. The securities, however, are in large denominations and in interim or registered form, and, therefore, would have to be exchanged before they could be sold in the market. Should arrangements be made for their redemption the Treasury would prefer, where authorized by law, that the redemptions be accomplished through the sale by the corporations concerned of new obligations in the market, the proceeds of which would be applied by the corporations to retire the obligations held by the Treasury. Except in the case of the Tennessee Valley Authority the corporations and agencies have sufficient statutory authority to issue new obligations for this purpose. The statutory authority under which the

Mailed from Daniel Bell's office
File to Mr. Bartelt

above-described Series A bonds of the Tennessee Valley Authority were issued, terminated as to additional issues on June 26, 1939, and the authority under which the interim certificates were issued is subject to certain limitations which would prevent a complete refunding of such certificates. Obligations owned by the Treasury, if sold in the market, would be guaranteed by the United States. This would also be true of new obligations sold by the corporations, where authorized, for the purpose of redeeming the obligations held by the Treasury.

Paragraph 3: It is assumed that the reference to capital stock of corporations in the third paragraph of your letter relates to capital stock of the so-called Governmental corporations. The Treasury holds capital stock of a number of such corporations, but there appears to be no authority of law for the Treasury to sell such stock to the general public. The President's Budget for 1941 contains an estimate of \$700,000,000 to cover the return to the Treasury of surplus capital funds of governmental corporations. The accounts to be credited will be determined by the laws under which the securities are redeemed or retired. Some of the moneys will be credited to revolving funds and made available for new subscriptions when, as, and if needed, while others will be covered into the Treasury as miscellaneous receipts. A complete list of the corporations on account of which the Government holds capital stock or subscriptions to paid-in surplus, together with the statutory references relating thereto, is enclosed for your convenient reference.

Paragraph 4: The proceeds of notes, debentures, or other obligations held by the Treasury, sold or redeemed, would be deposited in the Treasury as repayments to the accounts charged when they were acquired. Except where otherwise authorized by law, the proceeds of capital stock retired would be covered into the general fund of the Treasury. Funds thus covered into the Treasury would augment the cash in the General Fund and would be available for any expenditures heretofore or hereafter authorized by the Congress. In this connection it should be understood that all money received by the Treasury is deposited into a single cash account known as the "General Fund". This fund consists not only of money subject to expenditure on appropriations made by the Congress but includes also funds belonging to corporations which are carried in checking accounts with the Treasurer of the United States. However, money covered into the Treasury by law is available for expenditure only pursuant to appropriations made by the Congress.

I am also enclosing a copy of the Daily Statement of the United States Treasury for December 29, 1939, on page 6 of which appears a combined statement of assets and liabilities of governmental corporations and credit agencies of the United States as of November 30, 1939. These figures are compiled from the latest reports received by the Treasury.

Very truly yours,

(Signed) H. Morgenthau, Jr.

Secretary of the Treasury.

Honorable Robert A. Taft,
United States Senate,
Washington, D. C.

TREASURY DEPARTMENT

41

INTER OFFICE COMMUNICATION

DATE

January 9, 1940

TO Secretary Morgenthau

FROM E. H. Foley, Jr.

Re: Wire Tapping

The attached is a copy of a memorandum on wire tapping which I gave to Elmer Ireby last Saturday. You will be particularly interested in the second part.

E. H. F. L.

Attachment

JAN 6 - 1940

Mr. Ireby

Mr. Foley

Your memorandum to me of December 15, 1939, raises the following questions with respect to section 605 of the Communications Act of 1934, 48 Stat. 1103 (U.S.C. title 47, sec. 605).

1. Is it a violation of the Federal Communications Act when an investigator, in his official capacity and under the direction of an authorized officer of the Department, listens on a telephone tap to the conversations of an employee of the Department with other persons and reports them to his superior for consideration in connection with proposed administrative action which falls short of a recommendation for criminal prosecution?

2. Is it a violation of the Federal Communications Act for an official of the Department to use mechanical equipment for recording conversations held with another person and to reproduce them by sound effect to refresh his memory regarding the conversation?

I.

It is my opinion that the action described in the first question clearly comes within the interdict in section 605. That section provides, inter alia:

"* * * and no person not being authorized by the sender shall intercept any communication and divulge or publish the existence, contents, substance, purport, effect, or meaning of such intercepted communication to any person; * * *."

- 2 -

Section 501 provides penalties for willfully and knowingly doing, causing to be done, or suffering to be done any act, matter, or thing prohibited or made unlawful by the quoted portion of section 605.

It was held in Nardone v. United States, (1937) 302 U.S. 379, that the word "person" in section 605, quoted above, included Federal officers, and that evidence of communications obtained by them through wire tapping was illegally obtained and hence inadmissible. The communications involved were interstate in nature. After some conflict of decision in the Circuit Courts of Appeal,¹ the Supreme Court of the United States held that the prohibition in the statute extends to the interception of intrastate as well as of foreign and interstate communications. Weiss v. United States, (No. 42, U.S. S. Ct., Dec. 11, 1939). In the second Nardone case, (No. 240, U.S. S. Ct., Dec. 11, 1939), decided the same day as the Weiss case, the Court held that evidence rendered accessible through wire tapping is inadmissible and that, once the fact of illegal interception has been established, the injured party may make inquiry to determine whether information derived from such illegal interception has not been the source of other testimony produced at the trial. Thus, not only may illegally intercepted messages not be introduced in evidence, but they may not be used, at least directly to obtain other evidence.

It is clear, from the foregoing, that the prohibition quoted above from section 605 is applicable to interception by Federal officers

1. Valli v. United States, (C.C.A. 1st, 1938) 94 F.(2d) 687; Diamond v. United States, (C.C.A. 6th, 1938) 94 F.(2d) 1012; Sablowsky v. United States, (C.C.A. 3d, 1938) 101 F.(2d) 183; United States v. Weiss, (C.C.A. 2d, 1939) 103 F.(2d) 348.

and is applicable to interception of both interstate and intrastate communications. Divulgence to Federal officers is included within the phrase "divulgence * * * to any person", for it must be assumed that the word "person" used twice in the same clause has the same meaning in both places. In the statement of your question, you say that the communications will be intercepted by Federal officers and that the contents of the communications will be divulged to other Federal officers. I assume that neither party to a communication will be informed that an interception is being made. In those circumstances, all the requirements for the application of the quoted portion of section 605 seem to be met, and it is my opinion, therefore, that what is proposed in your first question is squarely within the prohibition of section 605 as that section has been interpreted by the courts.

II.

Your second question is answered in the negative. A search has revealed only one case in point. That case is United States v. Yee Ping Jong, (W.D. Pa. 1939) 26 F. Supp. 69. The court said (at page 70):

"Another allegation of error is based upon the reception of a phonographic record of a conversation between Yee Haim and Loui Wong. The latter was a Chinese interpreter and informer used by Agent White in his investigation. At White's direction, Wong called Yee Haim from St. Louis on the telephone, the call being made from the house of an associate of White. With the help of the occupant of the house a device was attached to the telephone wires inside the house and by it the conversation was recorded upon a prepared plate. The court allowed this conversation to be reproduced

- 4 -

upon trial, and its reception is alleged by counsel for the defendant to have been error. He bases his position upon the Communications Act, Section 605, 47 U.S.C.A., which reads in part as follows: '* * * and no person not being authorized by the sender shall intercept any communication and divulge or publish the existence, contents, substance, purport, effect, or meaning of such intercepted communication to any person.'

"The manner in which the conversation in question was recorded does not seem to present such an interception as is contemplated by the quoted statute. Webster's New International Dictionary defines the verb 'intercept' in part as follows: 'To take or seize by the way, or before arrival at the destined place; * * *.' The call to the defendant was made by Agent White, and the conversation between his interpreter and the defendant was not obtained by a 'tapping of the wire' between the locality of call and the locality of answer by an unauthorized person, but was, in effect, a mere recording of the conversation at one end of the line by one of the participants. It differed only in the method of recording from a transcription of a telephone conversation made by a participant. We are of opinion that the admission of the record in evidence was not error."

The authority of that case has never been questioned, and I find no reason now to doubt the soundness of its holding.

Though section 605 has been declared to be remedial and, therefore, must be liberally construed (Nardone v. United States, (1937) 302 U.S. 379), it must not, in view of its penal character², be extended beyond reasonable limits. It does not seem, moreover, that the employment of a device by one party to a conversation to record the conversation violates the ethical standards and principles of personal liberty which the statute was intended to preserve. In the words of Mr. Justice Frankfurter in the

2. See section 501 of the Communications Act of 1934.

- 5 -

more recent Nardone case, the decision rests, not on a "meticulous reading of technical language", but on "broad considerations of morality and public well-being."³ It surely would not be a violation of section 605 for one person engaged in a telephone conversation to take down notes thereon for future reference. It is common knowledge that it is a usual business practice, on important calls, to do so. I do not believe that the Congress would have considered such a practice unethical. It is somewhat more cautious perhaps, but certainly no less ethical, to employ a mechanical device to assure a more accurate recordation of such communications. That is not the "dirty business" that wire tapping has been stated to be,⁴ and it is not, in my opinion, the type of interception referred to in section 605.

(Signed) E. H. Foley, Jr.

General Counsel.

-
3. Nardone v. United States, (No. 240, U.S. S. Ct., Dec. 11, 1939).
 4. See the dissent of Mr. Justice Holmes in Olmstead v. United States, (1928) 277 U.S. 438, 470.

MTG/avp
Typed: 12/22/39
Copied: eb 1/9/40

Secretary Morgenthau

January 9, 1940

E. H. Foley, Jr.

Re: Wire Tapping

The attached is a copy of a memorandum on wire tapping which I gave to Elmer Irey last Saturday. You will be particularly interested in the second part.

EHFJr/fa
Typed 1/9'40

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

Attachment

Memo of 1/8'40 in reply to Irey's memo of 12/15'39 raising two questions.

1. Is it a violation of the Federal Communications Act when an investigator, in his official capacity and under the direction of an authorized officer of the Department, listens on a telephone tap to the conversations of an employee of the Department with other persons and reports them to his superior for consideration in connection with proposed administrative action which falls short of a recommendation for criminal prosecution?
2. Is it a violation of the Federal Communications Act for an official of the Department to use mechanical equipment for recording conversations held with another person and to reproduce them by sound effect to refresh his memory regarding the conversation?

Mr. Irey

JAN 6 - 1939

Mr. Foley

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doing, causing to be done, or suffering to be done any act, matter, or thing prohibited or made unlawful by the quoted portion of section 605.

It was held in Hardone v. United States, (1937) 303 U.S. 579, that the word "persons" in section 605, quoted above, included Federal officers, and that evidence of communications obtained by them through wire tapping was illegally obtained and hence inadmissible. The communications involved were interstate in nature. After some conflict of decision in the Circuit Courts of Appeal,¹ the Supreme Court of the United States held that the prohibition in the statute extends to the interception of intrastate as well as of foreign and interstate communications. Reiser v. United States, (No. 43, U.S. S.Ct., Dec. 11, 1939). In the second Hardone case, (No. 240, U.S. S.Ct., Dec. 11, 1939), decided the same day as the Reiser case, the Court held that evidence rendered accessible through wire tapping is inadmissible and that, once the fact of illegal interception has been established, the injured party may make inquiry to determine whether information derived from such illegal interception has not been the source of other testimony produced at the trial. Thus, not only may illegally intercepted messages not be introduced in evidence, but they may not be used, at least directly, to obtain other evidence.

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1. Yalla v. United States, (D.C.A. 1st, 1938) 94 F.(2d) 677; Blumenthal v. United States, (D.C.A. 6th, 1938) 94 F.(2d) 1012; Blumenthal v. United States, (D.C.A. 2d, 1938) 101 F.(2d) 125; United States v. Selms, (D.C.A. 2d, 1939) 105 F.(2d) 549.

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- 4 -

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- 5 -

more recent Hardens case, the decision rests, not on a "meticulous reading of technical language", but on "broad considerations of morality and public well-being."³ It surely would not be a violation of section 605 for one person engaged in a telephone conversation to take down notes thereon for future reference. It is common knowledge that it is a usual business practice, on important calls, to do so. I do not believe that the Congress would have considered such a practice unethical. It is somewhat more cautious perhaps, but certainly no less ethical, to employ a mechanical device to assure a more accurate recordation of such communications. That is not the "dirty business" that wire tapping has been stated to be,⁴ and it is not, in my opinion, the type of interception referred to in section 605.

(Signed) E. H. Foley, Jr.

General Counsel.

3. Hardens v. United States, (No. 240, U.S. S.Ct., Dec. 11, 1939).

4. See the dissent of Mr. Justice Holmes in Olmstead v. United States, (1928) 277 U.S. 438, 470.

HTG/avp

Typed: 12/22/39

January 9, 1940.

MEMORANDUM FOR SECRETARY MORGENTHAU

SUBJECT: Income Certificate Plan

In preparation for the meeting of the Fiscal and Monetary Committee, Wednesday, January 10, 1940, at 10:30 A.M., to discuss the Income Certificate Plan, you may be interested to learn what results have been obtained in getting the various technical people to reach an agreement on factual and other matters.

Mr. Ecker-Racz and I worked on the problem for the Treasury. To facilitate discussion and to clarify the issues, we prepared an additional memorandum and sent copies to the other departments. A revised draft of this memorandum will be ready for the meeting of the Fiscal and Monetary Committee.

Mr. Harold Smith said he had no economists on his staff and accordingly did not appoint anyone to serve.

Mr. Thomas C. Blaisdell was designated by Mr. Delano. Mr. Blaisdell did not feel that he could participate in any joint statement since Mr. Delano looks upon himself as an observer rather than as an active member of the Fiscal and Monetary Committee. However, discussion with Mr. Blaisdell revealed a substantial agreement between him and the Treasury technicians.

Mr. John Garfield was designated by Mr. Goldenweiser of the Federal Reserve to consider the matter with the other technical people. Mr. Goldenweiser did not participate in any of the joint discussions. Mr. Garfield did not wish to join in any statement. However, it appeared that there was no substantial disagreement between him and the Treasury technicians. I had the impression that he did not feel he was authorized to commit himself to any position.

Two meetings were held, one on December 29, 1939, and the other on January 9, 1940.

RB Lough

January 9, 1940.

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Two meetings were held, one on December 29, 1939, and the other on January 9, 1940.

HR:fab
1-9-40

January 9, 1940.
10:17 a.m.

H.M.Jr: Hello.

Operator: Mr. Traphagen:

H.M.Jr: Thank you.

O: Go ahead.

H.M.Jr: Hello.

John Traphagen: Hello, Mr. Secretary.

H.M.Jr: How are you?

T: I'm fine, I hope you're well.

H.M.Jr: I'm all right. Mr. Traphagen, we had a little meeting here yesterday, Mr. Welles and Jones and I.

T: Yes.

H.M.Jr: And at which we decided that Mr. Welles would call up the Colombian Ambassador and see how he felt on this so-called flexible plan.

T: Yes.

H.M.Jr: Well he found that he was very much against it and said it'd be almost impossible to put it through.

T: Well I was afraid that might be so.

H.M.Jr: So I guess we'd better forget about it. Now, I gathered that the Colombian Ambassador would like very much to see you again.

T: Yes.

H.M.Jr: And the thought that we had in mind was this that if you could see him Friday afternoon.

T: Yes.

H.M.Jr: Then we'd like to see you Saturday morning.

T: Right.

H.M.Jr: At ten o'clock. - I mean Saturday at ten.

T: Yes.

H.M.Jr: If you could arrange to see the Colombian Ambassador Friday afternoon.

T: I will have difficulty I'm sorry to say. I could see him Friday evening.

H.M.Jr: Well, why don't you call him up and see - he ought to be able -

T: Yes, I think that would probably be agreeable to him.

H.M.Jr: Why, he ought to cancel whatever he has.

T: Has he some new suggestion to make?

H.M.Jr: Well the only thing that, the feeling that we have is this, as we get it, he'd like you people now if you would make a counter proposal.

T: Yes.

H.M.Jr: And it seems to us that, if the first year, your committee would take a little less.

T: Yes.

H.M.Jr: And then gradually work it up to a higher figure, that that would help them a lot.

T: Yes.

H.M.Jr: Now you asked for a hint, and that's the hint that I'd like to give.

T: Right. Well that's very good of you.

H.M.Jr: And -

T: May I ask you this, Mr. Secretary?

H.M.Jr: Ask me anything you want to.

T: We had in mind two million three a year, on the national obligations alone.

H.M.Jr: Yes.

T: I take it that you don't feel that your group don't feel that that's too high for the ultimate figure or figure to take place, let's say, the end of the

second year, something like that.

H.M.Jr: Well I wouldn't want to say that because after all, I don't know just what the Colombians said but it looks to me as though they - if this was a private deal, you people asking two three and they keep talking about a million and a quarter - three-quarters.

T: Yes.

H.M.Jr: It looks as though that they'd be ready to go to two, I don't know, I haven't talked with them, you see?

T: Yes.

H.M.Jr: But the thing that's so close that I'd hate to see it fall through now.

T: Yes. Well, I rather took it from Mr. Jones' letter that he thought our offer was a little bit low.

H.M.Jr: Well, what offer was that?

T: That was the two million three offer, our so-called minimum offer.

H.M.Jr: You mean that you should get more?

T: Yes. I rather took it that he felt that the arrangement that we had made on the back interest -

H.M.Jr: No -

T: Was not sufficiently good.

H.M.Jr: Well he never said that to us.

T: He didn't.

H.M.Jr: No. No, I - I'm not sure that you can get the two three, but I think both sides will have to give away a little bit.

T: Right.

H.M.Jr: I think you both will have to give way a little bit.

T: Well, I'll go down - I will try to arrange to see him on Friday evening.

H.M.Jr: Yes.

- 4 -

T: And then I'll get in touch with you on Saturday at ten o'clock.

H.M.Jr: If - well yes, and Mr. Welles and Mr. Jones will be here at that time.

T: First rate.

H.M.Jr: In my office.

T: I'll be there.

H.M.Jr: Thank you so much.

T: Thank you. Goodbye.

H.M.Jr: Goodbye.

January 9, 1940.
9:45 a.m.

GROUP MEETING

Present: Mr. Bell
Mr. Sullivan
Mr. Haas
Mr. Schwarz
Mr. Thompson
Mr. Cochran
Mr. Cotton
Mr. Harris
Mr. Gaston
Mr. White
Mr. Foley
Mrs. Klotz

H.M.Jr: Herbert?

Gaston: You asked me to look into the note from the White House attached to a letter from Bob Reynolds as to John Bright Hill, our Collector of Customs at --

H.M.Jr: Well, the President is particularly anxious to do the one for Senator - which is the one from North Carolina?

Gaston: Bailey is the latest. Both Bailey and Reynolds have endorsed Hill and also Governor Hoey and a number of other people.

H.M.Jr: Is he all right?

Gaston: He is a good man, they tell me.

Harris: He was in a couple of days ago. He is a fine type of fellow.

Gaston: He is a Harvard Law graduate, graduate of the University of North Carolina. I have met him. I think the boys consider him a very good collector, don't they, Mr. Harris?

H.M.Jr: Is it a new appointment?

Gaston: There are two vacancies on the Customs Board in New York and it is our understanding that one of them is being held for Frank Walker's brother, which leaves the one vacancy.

H.M.Jr: I thought it was a collector.

- 2 -

Gaston: Oh, no. Some time back Bob Reynolds wrote recommending him for Commissioner of Customs, on having heard that Mr. Moyle was to resign and then there were various letters recommending him for the position of Customs --

H.M.Jr: How old is he?

Gaston: Those are life-time jobs, same as a judge, ten thousand a year for life.

H.M.Jr: Has Foley gone into his legal record?

Foley: Herbert spoke to me about it on the telephone this morning but I haven't looked it up.

H.M.Jr: This is something the White House is very keen about and if you read the memorandum you will see that if we give him this one, he said he would be a good boy for the rest of the session, so --

Foley: Drop the silver shirts?

H.M.Jr: Well, the White House is making the arrangements, I am not. This is something that they stressed. So you take a look at it and I would like, if you could, all of you, to let me know by tomorrow morning so that Gaston can let Pa Watson know, see.

Anything else, Herbert? I turned your friend George Creel over to you.

Gaston: Yes, George Creel. I told him that I thought it would be better to wait on this Rossiter appointment at least until we saw what happened to the Leek nomination for Collector of Customs out there.

Harris: Downey put forward two candidates. One is in jail and the other has been disbarred.

H.M.Jr: You like that, don't you?

Harris: That tickled me.

Gaston: But that fellow is out now, Basil.

H.M.Jr: This crowd is getting awfully finicky. A fellow can't be a silver shirt or go to jail. Well, anyway, Herbert, you keep it rolling, will you? ✓

Gaston: The thing to do is to keep it still.

H.M.Jr: The White House didn't put any pressure on, but they would like this one for Reynolds if we will go along.

Gaston: I think John Bright Hill is a high class of man. I have met him.

Harris: He is a very high class fellow. He is very well spoken of.

H.M.Jr: Anything else, Herbert?

Gaston: No.

H.M.Jr: That memorandum that you sent me about the Attorney General's remarks on Mr. Bioff, was that off the record? Is that yours or his?

Gaston: Chick didn't know definitely whether it was off the record or not.

Schwarz: I have learned since that it was off the record.

Foley: Here is a memorandum on powers of the New York State Legislature to alter the executive budget. They have increased the executive budget.

Here is a memorandum on the way in which the New York State income tax was treated in order to raise that nineteen million dollars in 1931.

H.M.Jr: Give copies of both of these things to John Sullivan.

Foley: Yes.

Gaston: I don't think I told you that J. R. Mitchell will be in at 10:15.

- 4 -

H.M.Jr: Good.

Now, Foley called me up at 7:30 and told me what you all agreed on. I think the telegram was already gone, but he went through the motions.

Bell: I didn't know anything about it until this morning.

Foley: He was the only one that wasn't there.

H.M.Jr: I didn't look up the time of the telegram, but they called me up and asked my advice.

Foley: Dan, what happened was this: Delano's man on the West Coast called and said that --

H.M.Jr: Tell him afterwards, if you don't mind.

Bell: Delano called me this morning at 9:00 o'clock and told me what happened.

H.M.Jr: I thought you had cleared it first.

Foley: No, couldn't get him.

Bell: They said they couldn't get hold of me.

H.M.Jr: Anything else?

Foley: No.

H.M.Jr: If anything happens on this thing at the meeting, I think you ought to go into a huddle and see what happens. I am not very much worried. If he sounds off at this meeting today, what the heck.

Bell: You know what happened yesterday?

H.M.Jr: Yes, I think so. You mean about sending the telegram?

Bell: No, I mean at the Board meeting.

H.M.Jr: No, what is going to happen?

- 5 -

Bell: They are going to explain to the Board today this thing they talked about yesterday, and they hoped they would be able to call Delano this morning and tell him the attitude of the Board.

H.M.Jr: All I know is that Foley threw himself up and said, "God, he was tough yesterday." Mr. Foley admitted he was.

Bell: I thought he was very good. He didn't put his feeling in it at all. He was very calm.

H.M.Jr: All right, what else, Ed?

Foley: Nothing.

Cochran: Pincent is due to come in at 11:45 and asked if he could come just a few moments early or stay a little late. He is coming a little earlier to my room.

H.M.Jr: All right.

White: I think you ought to get a machine that could take down Ed's laughter. It should be preserved for posterity, really.

Gaston: The Supreme Court won't let us do that.

Foley: Interception.

H.M.Jr: Well --

Foley: I have got a memorandum for you.

H.M.Jr: I haven't said a word to anybody.

Foley: I gave a memorandum Saturday to Elmer Irey and I meant to bring in a copy yesterday morning. I will send it right in.

H.M.Jr: You know what I am talking about?

Foley: Yes, I know what you are talking about. That is why I gave him a memorandum.

H.M.Jr: All right. Pincent wants to whisper before or after, is that the idea?

- 6 -

Cochran: Yes.

H.M.Jr: Well, we will give him a chance.

Cochran: He will be in my room ten or fifteen minutes ahead, if you want to call him.

H.M.Jr: Chick?

Schwarz: Did you see Burt Wheeler's story?

H.M.Jr: No.

Schwarz: He thinks the purchase of gold and silver was a good idea.

H.M.Jr: He does?

Schwarz: Yes.

H.M.Jr: On that, Harry, a newspaper man asked me what I thought about Lord Beaverbrook saying that the United States was responsible for England going off the gold. You might get what Lord Beaverbrook said and give me a little answer on that, will you?

White: I will do that.

Cotton: You wanted to be reminded to call Traphagen after Welles calls you.

H.M.Jr: Right.
John?

Sullivan: You inquired yesterday about the aeroplane engine companies and neither Glenn Martin or Douglas have approached us on anything. Lockheed is taking care of their expansion with a stock issue. The Pratt Whitney, that is United Aircraft, in Hartford is putting up a new plant and added facilities at a total of about six and a half million, for which the French are paying three million six hundred thousand. They are asking us for permission to charge off the entire six and a half million against the French contracts.

- 7 -

Similarly, the French are paying about a million dollars for expansion of the Curtiss Wright Company and they want similar treatment.

H.M.Jr: But in the case of Pratt Whitney and Curtiss, they went ahead and didn't wait for us?

Sullivan: Oh, no, they have gone right ahead.

H.M.Jr: Just remember the figure, Pratt Whitney is six and a half?

Sullivan: Six and a half million. That is the plant and additional machinery of which the French are paying three million six hundred thousand. In fact, the French advanced money to them before they started to talk as an advance payment on the price.

H.M.Jr: And cut it?

Sullivan: About a million dollars.

H.M.Jr: That is both of those on the engines?

Sullivan: That is right.

H.M.Jr: Did Curtiss do anything at Buffalo?

Sullivan: I don't know where that is, sir.

H.M.Jr: Can you give me just those two items, just Pratt and Whitney and Curtiss?

Sullivan: Yes sir.

H.M.Jr: Anything else, John?

Sullivan: That is all, sir.

H.M.Jr: Did Mr. Thompson fix you up with an office?

Sullivan: Yes sir.

H.M.Jr: Next to his?

Sullivan: I haven't seen it yet.

H.M.Jr: Yes, it is next to his. It is a nice room. Have you (Gaston) seen it?

Gaston: Yes. A nice view of the White House.

- 8 -

White: You have to first get to know it from the outside.

Sullivan: I see.
I might add on that Pratt Whitney business, they have had, of course, no encouragement.

H.M.Jr: I think that is a good idea.
George?

Haas: I have nothing but some routine affairs (handing report to Secretary).

H.M.Jr: On that matter that I asked you (Bell) to do on parity payments, I think George's shop could help you quite a lot on that.

Bell: All right.

H.M.Jr: I think George could help you, because he is familiar with all that Agriculture stuff.

Bell: I haven't called up over there yet but I have an idea Smith is out of town taking a little vacation after the budget.

H.M.Jr: The memorandum to the President on parity payments. You (Haas) could help.
Anything else?

Haas: I have nothing.

H.M.Jr: Basil?

Harris: No.

H.M.Jr: Basil, would you ask your people to give you a little review of what is happening down South of the border in Tijuana, I mean how they are getting along?

Harris: Senator Sheppard has introduced a Bill to meet the wishes of that group out there, so that is about the only thing we have heard.

H.M.Jr: No, how it is working.

- 9 -

Harris: Yes, I will find out.

H.M.Jr: I mean how it is working. We ought to have a close check, but I am sure it will come up.

Harris: I will get that right away.

H.M.Jr: Harry?

White: George Eddy got a letter from Mr. Davenport of Fortune to the effect that he would send him a copy, but not the proof. We had anticipated, expected to get a proof. So what will be in it we don't know, but he had said that he was going to send us a proof.

H.M.Jr: Are you going to be in this morning?

White: Yes.

H.M.Jr: I want to see you. You are down for this afternoon, aren't you, Harry?

White: At 3:00, there is a group --

H.M.Jr: You are arranging who is coming?

White: Yes.

H.M.Jr: All right.

Bell: I have nothing.

H.M.Jr: Silver certificates?

Bell: Oh, that has increased to about nineteen million but we have to keep silver certificates in gold to meet lawful money liabilities so we have to keep about fifteen million gold plus the silver certificates to meet those lawful money liabilities and until the silver certificates have reached about thirty-five million we won't be able to issue them.

H.M.Jr: Have they cleaned up those sales of Government bonds?

Bell: Yes, they have. The market was rather weak yesterday but I got two and a half million more of them. The prices are right now.

- 10 -

H.M.Jr: You are watching it?

Bell: Yes.

H.M.Jr: Is the Federal selling?

Bell: No, they haven't sold. There are very few in the market. They are generally concentrated on our quarters.

H.M.Jr: Now, if something comes up today about Bank of America, you will get in touch with me?

Bell: Yes, first thing.

Thompson: I have nothing.

H.M.Jr: If Bell and Gaston and you (Thompson) could stay a minute, I would like to see you all.

Secretary Morgenthau

JAN 9 - 1940

E. H. Foley, Jr.

Power of New York Legislature to Alter Executive Budget

The people of the State of New York adopted an amendment to the Constitution, known as the Executive Budget, in the fall of 1927. [Const., Art. IV-A/ Although there has been a change in phraseology the purpose of this constitutional amendment has not been changed by the Constitution of 1938. [Const., Art. VII]

Under the Executive Budget the head of each department of the state government, except the legislature and the judiciary, submits to the Governor such estimates and information which he requires, copies of which are simultaneously furnished to the appropriate committees of the legislature. On the basis of these estimates, the Governor holds hearings at which representatives of such committees are entitled to be present and to make inquiry. [Const., Art. VII, §1]

In this way the needs of the various executive departments are thoroughly examined into by the Governor and the legislature before the budget goes to the legislature. After the examination of these needs, but not later than February 1, the Governor makes up his budget for the ensuing fiscal year and submits it to the legislature with an explanation of the basis of the estimates. [Const., Art. VII, §2] At the same time the Governor submits a proposed appropriation bill which contains the items in the budget. [Const., Art. VII, §3]

The Constitution then provides what the legislature may do with this budget bill. The legislature may require the heads of the departments to appear and answer relevant inquiries [Const., Art. VII, §3], but: "The legislature may not alter an appropriation bill submitted by the governor except to strike out or reduce items therein, but it may add thereto items of appropriation provided that such additions are stated separately and distinctly from the original items of the bill and refer each to a single object or purpose." [Const., Art. VII, §4 (underlining mine)]

The items of appropriation which the legislature may add must be distinct from the original items of the budget bill and must be for something other than items stricken out or

reduced. Only last June the Court of Appeals unanimously held that the legislature can not strike out the itemized appropriations in the governor's appropriation bills and substitute therefor lump sums for the same personal services and maintenance. [People v. Tremaine (1939), 281 N.Y. 1, 21 N.E. (2d) 891]

If the legislature passes the budget bill as proposed by the Governor, it does not have to be submitted to him for his approval, but separate items added by the legislature must be submitted in the usual way to the Governor for his approval. [Const., Art. VII, §4] If the Governor withholds his approval from any such item, the provisions of the Constitution apply which relate to the passage over the Governor's veto of a bill by two thirds of the members of each house of the legislature. [Const., Art. IV, §7]

Once the budget is adopted the members of the legislature are constitutionally incapable of carrying on any duties in the expenditure of the appropriations, and accordingly a clause in a budget bill requiring the approval of the Chairman of the Senate Finance Committee and the Chairman of the Assembly Ways and Means Committee before certain appropriations could be expended was held void. [People v. Tremaine (1929), 252 N.Y. 27, 168 N.E. 817] In the words of Governor Roosevelt the fundamental question involved was:

" . . . whether administration is to be in the hands of the Governor elected by all the people to be the head of the executive branch, or whether it is to be shared between the Governor and the Legislature in such a way that all responsibility will be lost." [I Public Papers and Addresses of Franklin D. Roosevelt (1938) 341, 343; see also pp. 345-348 discussing the significance of the Executive Budget victory]

The budgets of the legislature and the judiciary are separate from the executive budget. Itemized estimates of the financial needs of the legislature, certified by the presiding officer of each house, and of the judiciary, certified by the Comptroller, are submitted to the Governor not later than December 1 for inclusion in the budget without revision but with such recommendations as he may deem proper. [Const., Art. VII, §1] None of the restrictions concerning alteration of the items of a budget bill apply to appropriations for the legislature or the judiciary. However, the Governor exercises the same power of veto over appropriations for the legislature and the judiciary as he does over separate items added to the governor's bills by the legislature. [Const., Art. VII, §4]

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

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1-8-40
Copied eb 1/9/40

Secretary Morgenthau

E. H. Foley, Jr.

JAN 9 - 1940

Increase in New York State Personal Income Tax in 1931

Personal income tax rates on returns for the calendar year 1931 (or for the fiscal year returns due during the calendar year 1932) were increased 100% over the existing personal income tax rates by an amendment to the tax law enacted at the Extraordinary Session of the New York State Legislature in 1931, and approved by the Governor on September 23, 1931. [L. 1931, Chap. 795 (Tax Law, §351-b)]

Until this increase, the tax rates had been 1% of the amount of net income not exceeding \$10,000, 2% of the amount of net income in excess of \$10,000 but not in excess of \$50,000, and 3% of the amount of net income in excess of \$50,000. The new rates for the three brackets were increased to 2, 4 and 6% respectively.

The law stated that its objective was "to provide moneys to pay appropriations for the relief of unemployed persons and the alleviation of distress occasioned by the present economic depression." This conformed to the recommendation made by Governor Roosevelt in a message to the Legislature on August 28, 1931 that a tax be laid on personal incomes to provide the necessary moneys to meet an appropriation "for the relief of distress and the amelioration of unemployment." [I Public Papers and Addresses of Franklin D. Roosevelt (1938) 457, 467-8]

This message recommended the creation of the "temporary Emergency Relief Administration" and the appropriation to the TERA of \$20,000,000 of which \$1,000,000 would be retained for expenditure by the State, leaving \$19,000,000 for apportionment among the counties and cities of the State. The message stated:

"The necessary money for this unemployment and distress relief should be raised by a tax on personal incomes. It seems logical that those of our residents who are fortunate enough to have taxable incomes should bear the burden of supplementing the local governmental and private philanthropic work of assistance. I believe that this tax should fall proportionately on all incomes, over and above existing exemptions. If each person paying an income tax were required to pay merely half again as much, I am informed by the State Tax Commission, the necessary twenty million dollars will be raised."

Ibid, p. 465/

One third of the revenues derived from the personal income tax imposed by the 1931 law was paid into the State Treasury to the credit of the General Fund. The remaining two thirds was allocated between the state and local governmental units in accordance with the usual formula for distribution of the income tax. [Tax Law, §382, as amended by L. 1931, Chap. 512]

The State's share of the personal income taxes collected under the new rates prescribed by the 1931 law was about \$19,500,000. [Ann. Rep. State Tax Commission, 1932 (Leg. Doc., 1933, No. 11), p. 81]

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

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1-8-40
Copied eb 1/9/40

January 8, 1940

73

Secretary Morgenthau
Herbert Gaston

Murphy told newspapermen today that he expected an indictment of Bioff by Wednesday.

January 9, 1940

74

Secretary Morgenthau

E. H. Foley, Jr.

Re: Wire Tapping

The attached is a copy of a memorandum on wire tapping which I gave to Elmer Ireys last Saturday. You will be particularly interested in the second part.

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

EHFJr/fm

Typed 1/9'40

Attachment

Memo of 1/8'40 in reply to Ireys' memo of 12/15'39 raising two questions.

1. Is it a violation of the Federal Communications Act when an investigator, in his official capacity and under the direction of an authorized officer of the Department, listens on a telephone tap to the conversations of an employee of the Department with other persons and reports them to his superior for consideration in connection with proposed administrative action which falls short of a recommendation for criminal prosecution?
2. Is it a violation of the Federal Communications Act for an official of the Department to use mechanical equipment for recording conversations held with another person and to reproduce them by sound effect to refresh his memory regarding the conversation?

JAN 6 - 1940

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Mr. Irely

Mr. Foley

Your memorandum to me of December 15, 1939, raises the following questions with respect to section 605 of the Communications Act of 1934, 48 Stat. 1103 (U.S.C. title 47, sec. 605).

1. Is it a violation of the Federal Communications Act when an investigator, in his official capacity and under the direction of an authorized officer of the Department, listens on a telephone tap to the conversations of an employee of the Department with other persons and reports them to his superior for consideration in connection with proposed administrative action which falls short of a recommendation for criminal prosecution?

2. Is it a violation of the Federal Communications Act for an official of the Department to use mechanical equipment for recording conversations held with another person and to reproduce them by sound effect to refresh his memory regarding the conversation?

I.

It is my opinion that the action described in the first question clearly comes within the interdict in section 605. That section provides, inter alia:

"* * * and no person not being authorized by the sender shall intercept any communication and divulge or publish the existence, contents, substance, purport, effect, or meaning of such intercepted communication to any person; * * *."

Section 501 provides penalties for willfully and knowingly doing, causing to be done, or suffering to be done any act, matter, or thing prohibited or made unlawful by the quoted portion of section 605.

It was held in Nardone v. United States, (1937) 302 U.S. 379, that the word "person" in section 605, quoted above, included Federal officers, and that evidence of communications obtained by them through wire tapping was illegally obtained and hence inadmissible. The communications involved were interstate in nature. After some conflict of decision in the Circuit Courts of Appeal,¹ the Supreme Court of the United States held that the prohibition in the statute extends to the interception of intrastate as well as of foreign and interstate communications, Weiss v. United States, (No. 42, U.S. S. Ct., Dec. 11, 1939). In the second Nardone case, (No. 240, U.S. S. Ct., Dec. 11, 1939), decided the same day as the Weiss case, the Court held that evidence rendered accessible through wire tapping is inadmissible and that, once the fact of illegal interception has been established, the injured party may make inquiry to determine whether information derived from such illegal interception has not been the source of other testimony produced at the trial. Thus, not only may illegally intercepted messages not be introduced in evidence, but they may not be used, at least directly to obtain other evidence.

1. Valli v. United States, (C.C.A. 1st, 1938) 94 F. (2d) 687;
Diamond v. United States, (C.C.A. 6th, 1938) 94 F. (2d) 1012;
Sablowsky v. United States, (C.C.A. 3d, 1938) 101 F. (2d) 183;
United States v. Weiss, (C.C.A. 2d, 1939) 103 F. (2d) 348.

It is clear, from the foregoing, that the prohibition quoted above from section 605 is applicable to interception by Federal officers and is applicable to interception of both interstate and intrastate communications. Divulgence to Federal officers is included within the phrase "divulgence * * * to any person", for it must be assumed that the word "person" used twice in the same clause has the same meaning in both places. In the statement of your question, you say that the communications will be intercepted by Federal officers and that the contents of the communications will be divulged to other Federal officers. I assume that neither party to a communication will be informed that an interception is being made. In those circumstances, all the requirements for the application of the quoted portion of section 605 seem to be met, and it is my opinion, therefore, that what is proposed in your first question is squarely within the prohibition of section 605 as that section has been interpreted by the courts.

II.

Your second question is answered in the negative. A search has revealed only one case in point. That case is United States v. Yee Ping Jong, (W.D. Pa. 1939) 26 F. Supp. 69. The court said (at page 70):

"Another allegation of error is based upon the reception of a phonographic record of a conversation between Yee Halm and Loui Wong. The latter was a Chinese interpreter and informer used by Agent White in his investigation. At White's direction, Wong

called Yee Haim from St. Louis on the telephone, the call being made from the house of an associate of White. With the help of the occupant of the house a device was attached to the telephone wire inside the house and by it the conversation was recorded upon a prepared plate. The court allowed this conversation to be reproduced upon trial, and its reception is alleged by counsel for the defendant to have been error. He bases his position upon the Communications Act, Section 605, 47 U.S.C.A., which reads in part as follows: '* * * and no person not being authorized by the sender shall intercept any communication and divulge or publish the existence, contents, substance, purport, effect, or meaning of such intercepted communication to any person.'

"The manner in which the conversation in question was recorded does not seem to present such an interception as is contemplated by the quoted statute. Webster's New International Dictionary defines the verb 'intercept' in part as follows: 'To take or seize by the way, or before arrival at the destined place; * * *.' The call to the defendant was made by Agent White, and the conversation between his interpreter and the defendant was not obtained by a 'tapping of the wire' between the locality of call and the locality of answer by an unauthorized person, but was, in effect, a mere recording of the conversation at one end of the line by one of the participants. It differed only in the method of recording from a transcription of a telephone conversation made by a participant. We are of opinion that the admission of the record in evidence was not error."

The authority of that case has never been questioned, and I find no reason now to doubt the soundness of its holding.

Though section 605 has been declared to be remedial and, therefore, must be liberally construed (Nardone v. United States, (1937) 302 U.S. 379), it must not, in view of its penal character,² be extended beyond reasonable limits. It does not seem, moreover, that the employment of a device by one party to a conversation to record the conversation violates the ethical standards and principles of personal liberty which the

2. See section 501 of the Communications Act of 1934.

- 5 -

statute was intended to preserve. In the words of Mr. Justice Frankfurter in the more recent Nardone case, the decision rests, not on a "meticulous reading of technical language", but on "broad considerations of morality and public well-being."³ It surely would not be a violation of section 605 for one person engaged in a telephone conversation to take down notes thereon for future reference. It is common knowledge that it is a usual business practice, on important calls, to do so. I do not believe that the Congress would have considered such a practice unethical. It is somewhat more cautious perhaps, but certainly no less ethical, to employ a mechanical device to assure a more accurate recordation of such communications. That is not the "dirty business" that wire tapping has been stated to be,⁴ and it is not, in my opinion, the type of interception referred to in section 605.

(Signed) E. H. Foley, Jr.

General Counsel.

3. Nardone v. United States, (No. 240, U.S. S. Ct., Dec. 11, 1939).

4. See the dissent of Mr. Justice Holmes in Olmstead v. United States, (1928) 277 U.S. 438, 470.

MTG/avp

Typed: 12/22/39

Copied: eb 1/9/40

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE January 9, 1940

TO Secretary Morgenthau

FROM Mr. Cochran

CONFIDENTIAL

The sterling rate continued the improvement which was inaugurated yesterday, and today's turnover exceeded that of yesterday by about £300,000. After opening at 3.94-3/4 in New York, the rate steadily advanced to the high of 3.97 at noon. Toward the close of the day sterling receded and the final quotation was 3.95-3/4.

The demand for sterling was similar to that of yesterday, coming from commercials with a large proportion of buying by rubber houses. The interest of the rubber houses in the market was attributed to rumors that a tax was to be placed on exports of rubber from producing countries. Such rumors caused the rubber market to advance and in turn the purchasers of rubber went into the sterling market to cover their commitments.

Another factor contributing to the better price for sterling was the regulation instituted yesterday by the British Control whereby transfers of sterling from the balances of residents to those of non-residents would, in the future, require the submission of a detailed report explaining the reason for transfer, in place of the former simple declaration stating that such a transfer did not contravene the Defence (Finance) Regulations. This new procedure should have the effect of reducing the available supply of sterling in the outside market.

Sales of spot sterling by the four reporting banks totaled £543,000, from the following sources:

By commercial concerns.....	£192,000
By foreign banks (Europe and South America).....	£351,000
Total.....	£543,000

Purchases of spot sterling amounted to £531,000, as indicated below:

By commercial concerns.....	£367,000
By foreign banks (Far East and Europe).....	£164,000
Total.....	£531,000

The following reporting banks sold cotton bills totaling £35,000 to the British Control on the basis of the official rate of 4.02-1/2:

£ 18,000 by the Guaranty Trust Co.
10,000 by the National City Bank
7,000 by the Chase National Bank
£ 35,000 Total

- 2 -

An improvement was also registered in the forward rates for sterling. One-month sterling was quoted at 1-1/4¢ discount, while the three-months quotation was 4-3/8¢ discount.

The rate for the Cuban peso again improved, being quoted at 10-1/4¢ discount.

The other important currencies closed as follows:

French francs	.0224-1/2
Guilders	.5331
Swiss francs	.2243
Belgas	.1678
Canadian dollars	12-1/8% discount

The Federal Reserve Bank purchased 100,000 Swiss francs for the account of the Bank of Latvia.

We purchased \$10,000,000 in gold from the earmarked account of the Bank of France. Since the outbreak of the war we have purchased a total of about \$195,000,000 in gold from the French bank.

The Federal Reserve Bank of New York reported to us the following shipments of gold:

\$ 8,734,000 from the Netherlands, representing three shipments by the Netherlands Bank to the Federal Reserve Bank of New York, to be earmarked for account of the Netherlands Bank.

4,441,000 from Canada, shipped by the Bank of Canada to the Federal Reserve Bank of New York for sale to the U. S. Assay Office.

\$13,175,000 Total

Spot and forward fixing prices for silver in London were quoted at 21-7/8d and 21-13/16d respectively, both up 1/16d. The U. S. equivalents figured out to 38.81¢ and 38.40¢. The Bombay silver quotation has been moving in a fairly narrow range during the past week and is currently quoted at an equivalent (after deducting the import tax) of 42.87¢.

The prices fixed for foreign silver by both Handy and Harman and the Treasury were unchanged at 34-3/4¢ and 35¢, respectively.

We made seven purchases of silver totaling 738,000 ounces under the Silver Purchase Act. Of this amount 200,000 ounces represented a sale from inventory by one of the refining companies and 263,000 ounces were derived from secondary materials. Both of these purchases were for delivery tomorrow. The remaining 275,000 ounces consisted of new production silver from foreign countries purchased for forward delivery.

We also purchased 500,000 ounces of silver from Canada. This represents the first purchase that we have made in January from that country under our regular monthly agreement.

- 3 -

When Mr. Pinsent, Financial Counselor of the British Embassy, was with me this morning he mentioned as of possible interest to us the reported activities of one Leopold Klotz. This individual, who is believed to be a German, is understood to have been selling securities and buying oil in New York on such a scale as to impress very much the broker who was operating for him. Pinsent did not mention the broker's name. It is understood that Klotz was registered at the Waldorf-Astoria Hotel until December 28, and proceeded from there to Mexico City.

B. M. F.

CONFIDENTIAL

STRICTLY CONFIDENTIAL

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TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE January 9, 1940

TO Secretary Morgenthau

FROM Mr. Cochran

The Secretary this morning received Messrs. Pinsent and Leroy-Beaulieu, with Chairman Frank of the Securities and Exchange Commission present, to discuss the question of the disposal of dollar securities. Mr. Cochran also attended the meeting and Miss Chauncey took notes.

After this group meeting, the Secretary received Mr. Pinsent along with Mr. Cochran, since Mr. Pinsent had an interim report from his Government on the question of gold and securities which he wished to communicate confidentially and informally to the Secretary. At the Secretary's request, Mr. Pinsent came to my office following this meeting, to assist me in drawing up a memorandum of the conversation. Mr. Pinsent was good enough to dictate the following memorandum:

"NOTES FOR THE SECRETARY OF THE TREASURY
REGARDING SALES OF SECURITIES AND GOLD
BY GREAT BRITAIN

(1) We are communicating with the French with a view to replying to the Secretary's inquiries (we do not at present know the French figures). We have no reason at present to revise our own estimate of 100,000,000 pounds for our net dollar requirements in the first year of the war, but we are reexamining the figures with special reference to the requirements of the sterling part of the British Empire.

(2) Mr. Whigham may possibly sail again from England on about January 16, though this is not yet decided. If he cannot come for personal reasons Mr. Gifford will come in his place.

(3) Sales of dollar securities by British holders since the war began have totaled about 25,000,000 pounds. The recent sales have now fallen off and the British Government now contemplates the issue of vesting order early in the new year. I suppose this would be timed to coincide with Mr. Whigham's arrival here. (This must, however, be reconsidered in view of the proposals put forward by the Secretary today.)

One factor that seems to have contributed in part to the postponement of a vesting order in December is that the issue of the first British war loan, formerly contemplated in December, has also been postponed to the new year. Financing of the purchase of British held securities by the British Treasury is obviously easier in conjunction with a war loan, although this is not decisive.

- 2 -

(4) There is, however, great uncertainty in any estimate of our dollar requirements. Our actual need for purchasing arms is not a fixed quantity and may develop. We do not know how far United States citizens may use their freedom to withdraw pre-war balances from the United Kingdom. There seems to be some uncertainty whether we are receiving the full proceeds of exports from the United Kingdom, and steps will probably be taken to tighten up the procedure.

(5) There have been some unexpected demands for dollars. At the outbreak of war we were heavily oversold in dollars and had to cover these sales. The withdrawal of credit resulting from the Neutrality Act has meant that our payments in the first few months of the war had to cover imports made over a longer period. (As a particular case the pre-war airplane contracts originally provided for the payment of the last 10% on the arrival of the planes in England, but this had to be altered and the last 10% paid before the planes left the United States.)

(6) We have further been forced to provide insurance and freight in dollars in most cases where neutral interests are involved. As dollar requirements are apt to be irregular in incidence, the times when demand overtakes supply can only be met by sales of the gold which we have readily available in the United States and Canada. It remains our intention to cover the substantial part of our dollar requirements by the sale of securities, but we have felt ourselves free on occasion to offer gold for sale at the periods when our requirements could not be immediately covered otherwise."



January 9, 1940. 85
3:55 p.m.

H.M.Jr: Hello.

Operator: Mr. Frank. Go ahead.

H.M.Jr: Hello.
Jerome
Frank: Yes, sir.

H.M.Jr: How are you Jerry? Henry Morgenthau.

F: Yes, Henry.

H.M.Jr: We have heard nothing from the Federal Reserve Board today and I wondered whether you didn't want to call up now and then maybe see him around cocktail time, or something.

F: All right, I'll do that.

H.M.Jr: See?

F: Yes.

H.M.Jr: Ed's in here with me and he's pointing out something which I suppose is perfectly obvious to you that if our report is discredited in any way, what it does to your Transamerica.

F: Oh terrible.

H.M.Jr: What?

F: Terrible.

H.M.Jr: Well I was sure that you got that.

F: Of course.

H.M.Jr: But I think tonight's the night - evident - would be the best time if you could would be to get -

F: All right I'll try and do that.

H.M.Jr: What?

F: I'll try to get in touch with him right away.

H.M.Jr: Thank you so much.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE January 9, 1940

TO Secretary Morgenthau
 FROM Mr. White
 Subject: Domestic Exports to U.S.S.R.

We have just received reports that on January 4 large shipments to U.S.S.R. occurred, including \$2.5 million of copper, brass and bronze and products, \$872 thousand of molybdenum and \$84 thousand of aircraft engines, instruments and parts.

Following is a list of the principal exports reported on this date:

	<u>Value in thousands of dollars</u>
Total domestic exports	\$4,561
Copper, brass and bronze and products	2,509
Molybdenum	872
Forging machinery and parts	254
Power driven planers, shapers and grinding machines	223
Power driven boring, milling and drilling machines	144
Electric motors, starters and controllers	108
Sheet and plate metal working machines and parts	96
Aircraft engines, instruments and parts	84
Other power driven metal working machinery	75
Other industrial machinery	70
Other electrical machinery and apparatus	67
All other commodities	59

January 9, 1940.

My dear Mr. President:

I thought the enclosed memorandum from Basil Harris, on the shipping situation, would be of interest to you.

Sincerely yours,

(Signed) H. Morgenthau, Jr.

The President

The White House

By hand
500 pm 1/9/40

January 9, 1940.

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Sincerely yours,

(Signed) H. Morgenthau, Jr.

The President

The White House

By hand
5:00 pm 1/9/40

MEMORANDUM FOR THE SECRETARY:

JANUARY 8, 1940.

Subject: Shipping situation.

A quick check warrants the statement that awaiting shipment to England, Ireland and France alone there are not less than 150,000 weight tons of general cargo.

At the Port of New York, in shore elevators, canal barges and railroad cars, there are 8,000,000 bushels, approximately 200,000 tons of Grain. The greater portion of this, it is believed, will be moved to the United Kingdom.

The demand for ship's space to move freight to both England and France is so acute that both the British and French governments are availing themselves of the non-Conference Isbrandtsen-Moller service, on the vessels of which the freight rates are materially higher than the Conference rates which are the maximum assessed by the French Line and the regular British lines.

Aside from the airplanes to go to both England and France there are in the Staten Island Free Port awaiting shipment, 2400 large motor trucks for France. A few other of the more important commodities stored at the Free Port awaiting shipment to England or France are, 9000 tons Sisal and large quantities of canned beef imported from the Argentine; Swift alone having approximately 750,000 cases there.

Two commodities that are running in extraordinary volume and which, it is reported, will shortly be given preferred priority by the British Ministry of Shipping, are Starch and Glucose. Corn Products Refining Company alone have 20,000 tons of starch and

3500 tons of Glucose, a portion of which is already at seaboard and the rest available at their plants for immediate movement when ship's space is obtained.

A. E. Staley Manufacturing Company, Penick & Ford, National Starch Company, all are pleading for space. The Vice President of A. E. Staley Manufacturing Company states that the orders available to them would require their entire plant capacity to the exclusion of domestic business.

The demand for refrigerator space in which to ship bacon and hams is many times the capacity of the ships available. One large packer alone has indicated his intention to ship 500 tons weekly on one line if the space can be made available to him. The lines operating from Canadian ports are not able to cope with the demand for refrigerator space and the Canadian hams and bacon offering for shipment from New York exceeds by far the available refrigerator space.

Both the British and French purchasing commissions are reported to have bought large quantities of American copper recently. In addition, 6000 tons of copper monthly will be brought from Chile to New York for re-shipment to England and France.

Machinery of all kinds to both England and France, and especially to France, is available in very large quantities. The same is true of tractors, road scrapers, road graders and trench diggers.

Food stuffs, such as canned milk, canned fruits and vegetables and flour are available in practically unlimited quantities.

* * * * * (Signed) Basil Harris.

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TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE

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

January 9, 1940

Power of New York Legislature to Alter Executive Budget

The people of the State of New York adopted an amendment to the Constitution, known as the Executive Budget, in the fall of 1927. [Const., Art. IV-A] Although there has been a change in phraseology the purpose of this constitutional amendment has not been changed by the Constitution of 1938. [Const., Art. VII]

Under the Executive Budget the head of each department of the state government, except the legislature and the judiciary, submits to the Governor such estimates and information which he requires, copies of which are simultaneously furnished to the appropriate committees of the legislature. On the basis of these estimates, the Governor holds hearings at which representatives of such committees are entitled to be present and to make inquiry. [Const., Art. VII, §1]

In this way the needs of the various executive departments are thoroughly examined into by the Governor and the legislature before the budget goes to the legislature. After the examination of these needs, but not later than February 1, the Governor makes up his budget for the ensuing fiscal year and submits it to the legislature with an explanation of the basis of the estimates. [Const., Art. VII, §2] At the same time the Governor submits a proposed appropriation bill which contains the items in the budget. [Const., Art. VII, §3]

The Constitution then provides what the legislature may do with this budget bill. The legislature may require the heads of the departments to appear and answer relevant inquiries [Const., Art. VII, §3], but: "The legislature may not alter an appropriation bill submitted by the governor except to strike out or reduce items therein, but it may add thereto items of appropriation provided that such additions are stated separately and distinctly from the original items of the bill and refer each to a single object or purpose." [Const., Art. VII, §4 (underlining mine)]

The items of appropriation which the legislature may add must be distinct from the original items of the budget bill and must be for something other than items stricken out or reduced. Only last June the Court of Appeals unanimously held that the legislature can not strike out the itemized appropriations in the governor's appropriation bills and substitute therefor lump sums for the same personal services and maintenance. [People v. Tremaine (1939), 281 N.Y. 1, 21 N.E.(2d) 891]

-2-

If the legislature passes the budget bill as proposed by the Governor, it does not have to be submitted to him for his approval, but separate items added by the legislature must be submitted in the usual way to the Governor for his approval. [Const., Art. VII, §4] If the Governor withholds his approval from any such item, the provisions of the Constitution apply which relate to the passage over the Governor's veto of a bill by two thirds of the members of each house of the legislature. [Const., Art. IV, §7]

Once the budget is adopted the members of the legislature are constitutionally incapable of carrying on any duties in the expenditure of the appropriations, and accordingly a clause in a budget bill requiring the approval of the Chairman of the Senate Finance Committee and the Chairman of the Assembly Ways and Means Committee before certain appropriations could be expended was held void. [People v. Tremaine (1929), 252 N.Y. 27, 168 N.E. 817] In the words of Governor Roosevelt the fundamental question involved was:

" . . . whether administration is to be in the hands of the Governor elected by all the people to be the head of the executive branch, or whether it is to be shared between the Governor and the Legislature in such a way that all responsibility will be lost." [I Public Papers and Addresses of Franklin D. Roosevelt (1938) 341, 343; see also pp. 345-348 discussing the significance of the Executive Budget victory]

The budgets of the legislature and the judiciary are separate from the executive budget. Itemised estimates of the financial needs of the legislature, certified by the presiding officer of each house, and of the judiciary, certified by the Comptroller, are submitted to the Governor not later than December 1 for inclusion in the budget without revision but with such recommendations as he may deem proper. [Const., Art. VII, §1] None of the restrictions concerning alteration of the items of a budget bill apply to appropriations for the legislature or the judiciary. However, the Governor exercises the same power of veto over appropriations for the legislature and the judiciary as he does over separate items added to the governor's bills by the legislature. [Const., Art. VII, §4]

E. S. F. L.

Secretary Hergenthan

E. H. Foley, Jr.

1001 9 - 1931

Increase in New York State Personal Income Tax in 1931

Personal income tax rates on returns for the calendar year 1931 (or for the fiscal year returns due during the calendar year 1932) were increased 100% over the existing personal income tax rates by an amendment to the tax law enacted at the Extraordinary Session of the New York State Legislature in 1931, and approved by the Governor on September 23, 1931. [L. 1931, Chap. 795 (Tax Law, §351-b)]

Until this increase, the tax rates had been 1% of the amount of net income not exceeding \$10,000, 2% of the amount of net income in excess of \$10,000 but not in excess of \$50,000, and 3% of the amount of net income in excess of \$50,000. The new rates for the three brackets were increased to 2, 4 and 6% respectively.

The law stated that its objective was "to provide moneys to pay appropriations for the relief of unemployed persons and the alleviation of distress occasioned by the present economic depression." This conformed to the recommendation made by Governor Roosevelt in a message to the Legislature on August 28, 1931 that a tax be laid on personal incomes to provide the necessary moneys to meet an appropriation "for the relief of distress and the amelioration of unemployment." [I Public Papers and Addresses of Franklin D. Roosevelt (1938) 457, 467-8]

This message recommended the creation of the "Temporary Emergency Relief Administration" and the appropriation to the TERA of \$20,000,000 of which \$1,000,000 would be retained for expenditure by the State, leaving \$19,000,000 for apportionment among the counties and cities of the State. The message stated:

"The necessary money for this unemployment and distress relief should be raised by a tax on personal incomes. It seems logical that those of our residents who are fortunate enough to have taxable incomes should bear the burden of supplementing the local governmental and private philanthropic work of assistance. I believe that this tax should fall proportionately on all incomes, over and above existing exemptions. If each person paying an income tax were required to pay merely half again as much, I am informed by the State Tax Commission, the necessary twenty million dollars will be raised." [Ibid, p. 465]

-2-

One third of the revenues derived from the personal income tax imposed by the 1931 law was paid into the State Treasury to the credit of the General Fund. The remaining two thirds was allocated between the state and local governmental units in accordance with the usual formula for distribution of the income tax. [Tax Law, §382, as amended by L. 1931, Chap. 512]

The State's share of the personal income taxes collected under the new rates prescribed by the 1931 law was about \$19,500,000. [Ann.Rep. State Tax Commission, 1932 (Leg. Doc., 1933, No. 11), p. 81]

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

CLK:t
1-8-40

RFP

RECEIVED
THE SECRETARY OF THE STATE

GRAY

Paris

43 JAN 9 1940

Dated January 9, 1940

Rec'd 5:43 p.m.

OFFICE OF THE
SECRETARY OF THE STATE
WASHINGTON

Secretary of State

Washington

40, January 9, 7 p.m.

FOR THE TREASURY FROM MATTHEWS.

My telegram No. 23 of yesterday. The Franco-Anglo-Turkish economic and financial accord was signed here last evening.

The Paris financial press reports resumption of German coal and coke shipments to Belgium at the rate of 80,000 to 100,000 tons per month following their complete suspension around mid-November. This is taken to indicate progress in present negotiations for a commercial agreement between the two countries which are reported to involve German efforts to purchase rolling stock in Belgium.

The Paris securities market improved somewhat in early dealings today but weakened toward the close. I believe that the over-bought condition of the market and the cessation of the flow of repatriated capital are more responsible for yesterday's weakness than the international conference developments to which it is attributed. Rentes gained today from 10 centimes to 1.10 francs.

BULLITT

NPL

HSM

GRAY

London

Dated January 9, 1940

Rec'd 3 p. m.

Secretary of State,
Washington.

71, January 9, 6 p. m.

FOR TREASURY FROM BUTTERWORTH.

STRICTLY CONFIDENTIAL.

One. I gather with reference to my telegram 28 January 4, 3 p. m., that it has been more or less definitely decided to proceed with the vesting plan if Gifford on reaching the United States finds the situation propitious.

Two. The British Treasury's representative has returned from Spain since the Anglo-Spanish negotiations are nearing termination and the British Treasury seems thoroughly satisfied with the course the negotiations have taken. It states in confidence that it has agreed to lend Spain 2,000,000 pounds which will be used to pay off about half of the debts owed to British nationals which date back to 1936; the other half is to be gradually paid off by the Spanish Government. The latter has

slowly

hsm -2- No. 71, January 9, 6 p. m., from London

slowly but surely come to realize that Spanish prices
are out of line with world prices and is prepared to
subsidize the export of the commodities in which Great
Britain is mainly interested, namely, iron and pyrites
until such a time as the Spanish level of prices can be
adjusted presumably through devaluation of the peseta.
The 2,000,000 pounds loan was obviously designed not
only to facilitate the negotiations but also to bring
nearer the time when the peseta could be devalued.

JOHNSON

CSB

REB

GRAY

Bucharest

Dated January 9, 1940

Rec'd 3:50 p. m.

Secretary of State,
Washington.

4, January 9, 11 a. m. (SECTION ONE)

FOR TREASURY FROM EDSON.

In accordance with Department's telegram No. 1,
January 2, 7 p. m.

In statistics quoted below Germany includes Austria and Czechoslovakia; and the three month period September through November 1939 has been compared with corresponding period of 1938.

(SECTION ONE). Imports into Rumania from Germany during first three months of the war totaled 60.4000 metric tons, an 8% decrease from 1938 period. The lei value of these imports was 2,705,000,000, a 23% increase over 1938 period. Customs statistics do not indicate whether this value increase was due entirely to higher price level or in part to qualitative changes in imports from Germany though it is generally believed that armaments from Germany, Czechoslovakia, and Poland constitute a larger proportion of total imports than in prewar period.

(SECTION

REB -2- #4, From Bucharest, Jan. 9, 11 a. m.

(SECTION TWO). Exports to Germany during September-November period totaled 573,000 tons, a 10% increase over 1938 period. Their lei value totaled 3,436,000,000, a 100% increase over 1938 period due largely to oil price increases. Exports of petroleum products discussed in more detail below declined 15% from corresponding 1938 period because of transport difficulties and lumber exports declined to one-seventh. The increase in total exports is due to exports of 197,000 tons of cereals, an 86% increase over 1938 period, and 13.9 tons of animals and animal products which was three times corresponding 1938 exports.

(SECTION THREE). Petroleum exports to Germany during first eight months of 1939 totaled 961,000 tons, a 49% increase over corresponding 1938 period. Of this total, 479,000 was shipped ^{via} Danube and negligible quantities by rail, leaving deepwater Constanza-Hamburg route carrying about one-half of peacetime oil traffic. After imposition of the allied blockade shipments to Germany via Constanza ceased entirely (there is no evidence here of any (?) trans-shipment trade via Italy). Wartime shipments to Germany were as follows, in thousands of tons: September 65 by the Danube 4 by rail; October 68 by the Danube 20 by rail; November 62 by the Danube 21 rail. Three months total 240,000, 15% below the corresponding 1938 period.

(SECTION FOUR)

REB -3-#4, From Bucharest, Jan. 9, 11 a. m.

(SECTION FOUR). Future trends. Although the National Bank does not publish clearing balances by countries, customs figures indicate that during the year of October 1938 to September 1939 Greater Germany had a favorable merchandise balance with Rumania of 2,147,000,000 lei by the resulting largely from Czech arm shipments. Therefore Germany's unfavorable balance of 731,000,000 lei during the first three months of war, while larger than the usual seasonal adverse balance, is not sufficiently large to cause payment difficulties in the near future. Germany's exports are, however, subject to increasing qualitative restrictions; for example rubber cannot be exported at all and products containing more than 10% of copper, tin and lead may not be exported. With increasing pressure of work on Germany's metallurgical and chemical industries as blockade warfare continues Germany's ability to balance the clearing in the more distant future seems more doubtful. The revaluation of the mark last month (see Legation's telegram of December 28, 4 p. m.) improved Germany's terms of trade by only 13% but renewed political pressure could it is hinted force another revaluation if Germany deemed it necessary.

(END SECTION ONE)

HIBBARD

NPL

PARTIAL PARAPHRASE OF TELEGRAM RECEIVED; SECTION TWO,
NO. 4 OF JANUARY 9, 1940 FROM AMERICAN LEGATION, BUCHAREST.

Transport rather than payment difficulties therefore dominate the immediate future especially as regards oil shipments. Danube oil shipments to greater Germany in peace time averaged 60,000 tons a month and highest monthly peak in history to all Danubian area was 112,000 tons. The Danube was closed by ice on December 29th and usually is not reopened until March. Germany may be expected to increase river tanker tonnage by new construction and possibly by the transfer of Rhine tankers, though the latter would require expensive adaptation to maximum draft of one meter. No new river tanker construction is under way in Rumania and there is no reliable information here regarding German construction program. Oil industry believes that with most efficient use of existing tonnage 100,000 tons a month could be shipped to Germany via Danube.

Expansion of rail oil shipments beyond 40,000 tons a month is problematical. All Rumanian tank cars are needed for internal traffic and are still prohibited from crossing the frontier. November figures indicated Germany was then using about 1500 tank cars for Rumanian traffic, the industry expects December and January rail figures to be somewhat higher. However, in addition to tank car limitations, rail line capacity sets limits to expansion of rail traffic. The bottleneck pass between Ploesti and Brasov on the most direct route to Germany is already crowded with additional traffic due to the Rumanian troop movement, and double tracking of

- 2 -

this section will probably not be completed before September. Traffic on the recently reopened Gernauti-Lemberg route has thus far been severely restricted by Soviet red tape and inefficiency and no oil has yet gone by this route. The local oil industry estimates 40,000 tons a month as maximum amount for rail shipments regardless of number of tank cars Germany can send.

Present transport maxima may therefore be estimated at 40,000 tons a month during three winter months and 140,000 a month during the rest of the year.

CONFIDENTIAL:

I have heard reliable rumors that Rumania has agreed to furnish 130,000 tons a month to Germany, as part of the agreement; this figure is slightly larger than the transport maxima estimated in the preceding paragraph. Recently, however, there has been considerable evidence of an oil-buying campaign on the part of the Allies with the purpose of obtaining the greater part of the exportable surplus of Rumania - 4,000,000 tons a year. This campaign, if continued, will confront Germany with inability to fill transport capacity and when the Danube thaws, if not earlier, it may precipitate a crisis. The price of oil has already been forced to double the f.o.b. basic price level through the buying of the Allies; as a result of this, Rumania now
sells

- 3 -

sells only to belligerents or to neutrals to whom she has treaty commitments. The companies prefer to sell their product to England, because that country grants free exchange quota. According to informants in the industry, it is probable that the Rumanian Government may soon ask all companies, under threat of compulsion, to sell minimum quotas to Germany so that the Rumanian Government may implement its obligation to Germany. During the autumn the principal shippers to Germany were Allied companies, because of obligations contracted before the war; however, they are refusing to renew the contracts now, and pressure on the Allied companies on the part of the Rumanian Government would inevitably result in diplomatic intervention by the Allies, and possibly the Allied blockade would be used to exert economic pressure. Limitations of transport have up to the present protected the neutral position of Rumania, but when the Danube thaws, the conflict between the oil-buying campaign on the part of the Allies and the alleged commitment to Germany may force Rumania's hand.

END OF MESSAGE.

HIBBEARD.

EA:LWW

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, London, England.

DATE: January 9, 1940, 7 p.m.

NO.: 72

STRICTLY CONFIDENTIAL.

In strict confidence the British Treasury has stated that by the end of January it hopes to ship and deliver to Turkey gold in the amount of 15,000,000 pounds, which amount was provided for in the special protocol of the treaty between Turkey, France and Great Britain. Reference: telegram of October 19 from the Embassy, No. 2095. The British Treasury also states that sufficient war materials have been supplied to the Turks, so that upon delivery of the gold the treaty will come into full force (reference: telegram No. 2095 of October 19 from the Embassy and previous telegrams).

JOHNSON.

(Copy)

TO THE DIRECTOR
 FEDERAL BUREAU OF INVESTIGATION
 U.S. DEPARTMENT OF JUSTICE

APR 15 1940

RECEIVED

January 9, 1940.
10:13 a.m.

H.M.Jr: Hello.
Sumner
Welles: Hello Henry. How are you?
H.M.Jr: Well I - I'm alive.
W: Have you withstood the flood of oratory?
H.M.Jr: I - yes, I thought, for the time he spoke, I thought Jim Farley was by far the best.
W: I thought it was a pretty good average last night. Much the best we've had in some years.
H.M.Jr: Yes. I loved the President's talk.
W: Yes, grand. Henry, I've talked to the Colombian Ambassador.
H.M.Jr: Yes.
W: And he tells me that his reaction to that proposal is just about this, that it would be impossible -
H.M.Jr: Impossible?
W: Impossible from the standpoint of the Colombian Government to get approval there to what inherently is an indefinite amount of yearly payments scheduled for the future.
H.M.Jr: Yes.
W: And he also is very much worried about the opportunity for controversy that would arise each year as to what the correct amount ought to be.
H.M.Jr: Yes.
W: And he seems quite set in his views.
H.M.Jr: Well that ends that argument.
W: I think it does.
H.M.Jr: Well -
W: So my suggestion would be, as I said yesterday, that we ask Traphagen to come down on Friday to have his

- 2 -

meeting with the Colombians, Friday afternoon say, and then the meeting that you and I spoke of for ten o'clock in your office Saturday morning.

H.M.Jr: That's all right with me. I'll call him up right away.

W: Right.

H.M.Jr: I thought that Jesse was a little grouchy yesterday, and I think one of the reasons is that he feels he ought to be able to talk to, not only to Traphagen, but to the Colombian as well.

W: Well, I had that in mind when I made that suggestion. I thought if he wanted to get that off his chest, he could do it that way in your office.

H.M.Jr: I thought your suggestion was excellent, because I think it would be a great mistake to let him talk to either of them.

W: I quite agree.

H.M.Jr: It would just upset the applecart.

W: Yes.

H.M.Jr: Well I'll call Traphagen and tell him that I understand he's coming down Friday, is that it?

W: Well I don't think any definite time has been set. I gathered from what you told me that he was waiting to hear from you.

H.M.Jr: Yes, well I -

W: But I think it would help matters out a lot if he'd make a point of coming down Friday and then having that other meeting in your office Saturday.

H.M.Jr: I'll call him right away.

W: All right, Henry.

H.M.Jr: Thank you.

W: Thank you. Goodbye.

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: January 9, 1940, 3 p.m.

NO.: 33

CONFIDENTIAL.

FOR SECRETARY HULL AND SECRETARY MORGENTHAU.

The file of all telegrams exchanged by the British and French Governments with Purvis and Plevin in Washington was shown to me yesterday, together with the telegrams which Plevin and Jacquin sent after their conference on December 30 at the White House.

Everyone in the Government here express their most hearty thanks to me for your cooperation and that of President Roosevelt and those who work for you.

I wish to add my own congratulations on the wise and efficient way in which these matters were handled.

BULLITT.

TO THE SECRETARY
 TECHNICAL ASSISTANT
 OFFICE OF THE

NO 721 10 22 4 11

EA:LWW

AMERICAN DESPATCH
 RECEIVED



DEPARTMENT OF STATE
WASHINGTON

January 10, 1940.

The Secretary of State presents his compliments to the Honorable the Secretary of the Treasury, and encloses one copy of paraphrase of telegram No. 33 of January 9 from the American Embassy, Paris.

TO THE SECRETARY
TECHNICAL ASSISTANT
OFFICE OF THE

AND TO THE
OFFICE OF THE

RECEIVED
DEPARTMENT

January 9, 1940

11:45 am

Present:

Mr. Pinsent
Mr. Purvis
Mr. Jerome Frank
Mr. Cochran

Note: Mr. Frank came in ahead of the others and the following is a record of HM, Jr's conversation with him alone.)

HM, Jr: I thought I would take a second before these gentlemen came in. I was with the President yesterday and told him about my idea plus your improvement. Crazy about it! Said best suggestion he has heard yet! He said he would be glad to have us make it to them. He said, "That's good from every standpoint, business and everything."

Mr. Frank: Before them come along, I would like to tell you I checked on what I told you yesterday. They need no approval from us if the company that buys has no intention of offering to the public they would not have to register the issue. They will have to report after of the transaction. This I would not want to say to them: within our discretion we could, as a matter of -- on the basis of public interest, grant confidential treatment, if they so requested, of such report. I talked to the Commission about it and their inclination was it would not be desirable to give confidential treatment of the fact. I think it would be darn good for the business of the country to say we have kept this stock off the market.

HM, Jr: Could I go this far? To say if they designate somebody, that that person could drop in to see the S.E.C.? That you will designate somebody?

Mr. Frank: Certainly!

-2-

HM, Jr: But the President was crazy about it!

Mr. Frank: I thought it was marvelous!

HM, Jr: Did your boys like it?

Mr. Frank: Thought it was excellent.

* * * * *

(At this point the group came in.)

HM, Jr: I think I am going to have to send you (Mr. Leroy-Beaulieu) over on a battleship or something.

Mr. L-B: Mr. Secretary, I hear I am delayed once more for three days because of post office requirements.

HM, Jr: Somebody, they tell me, who is coming over here, has been in the Azores for the last two weeks.

Mr. Cochran: Thirteen days; too rough to land.

Mr. Pinsent: They have got in now.

HM, Jr: Now, to get down to business!

Mr. Frank and I have been talking over the question of what we felt was the best way for your respective Governments to dispose of their American owned securities, both from the standpoint of our market and the standpoint of getting the most money for you people. I have worked out the idea that if the French and English Governments, either together or separately, plus the Canadians, let's say, own so many thousands of shares of United States Steel, that the best customer for United States Steel stock would be the United States Steel Company itself. Mr. Frank improved on my suggestion and I thought this would be particularly interesting to your Government, that all negotiations could be made for the sale of this stock before you vested. Having made the sale and signed the contract, you could then vest and announce it. That's Mr. Frank's contribution, which

-3-

is very important. Now I had an opportunity to go over this with the President yesterday and he likes it very much.

Mr. Frank can talk for himself, but I personally think it is distinctly worth while trying and it seems to me your respective Governments have nothing to lose by it, because if they designate somebody to go see the President of the United States Steel and say "We can control so many thousand shares. Would you be interested in buying it?"

"Let me take it up with my Board of Directors." And if he said yes, you could sit down and arrive at a price. Having arrived at a price, you could then vest and take title.

Mr. Frank: Just to round out the story, as far as the requirements of our Statute are concerned, if the sale were being made solely to an individual company they would not be required to register, nor would you be required to; in other words, you would not have anything to do with S.E.C. in advance of the transaction unless they contemplated a reselling campaign, which they probably would not, and all that would be required when the transaction was completed, the purchasing company would have to file notification of it with us, but that's all, so there would be no red tape involved assuming they do not contemplate resale.

Mr. Pinsent: I think we already had it in mind to adopt some procedure of that nature in particular cases and I take it this would be for particular cases rather than a general method.

Mr. Frank: For any case where it works.

Mr. Pinsent: I heard Mr. Whigham speak of that method, perhaps in relation to railway bonds.

Mr. Frank: I think the difference is -- right in this room or in our office Mr. Whigham talked of that, but what he had in mind was that he would use that device only in special situations like companies -- like Nickel, where there was a very large holding, so large that the

-4-

market ordinarily could not be expected to absorb it. The Secretary is suggesting that you apply it more extensively -- that you take United States Steel, which I don't think was in Mr. Gifford's mind. He had in mind that the market would take that. The Secretary's suggestion is you would not restrict it to special cases, but take it wherever you have a ponderable block of stock.

HM, Jr: And whatever company was involved, would have enough money in its treasury to buy it and you go to them and, say, buy at the average or the price over a few months.

Mr. Frank: And that would be true of Steel and Motors and other companies.

Mr. Pinsent: Do you think the time element would make it difficult to conclude transactions of that kind? It takes, I don't know how long, but ordinarily a week, to get a decision.

Mr. Frank: I don't think that would be much of a problem.

Mr. Pinsent: Could one carry out sales of that kind for forward delivery, in a fortnight's delivery?

Mr. Frank: I think so, particularly if you adopted the Secretary's suggestion -- if you decided on average price rather than market price on date of delivery.

HM, Jr: I don't know what would be fair -- the average price or three months' price, whatever you agreed on. That would be after you had finished three or four transactions. But if you agreed tomorrow on United States Steel on prices for October, November and December, United States Steel would not mind waiting 30 days for delivery.

Mr. Frank: I don't think that would be unsurmountable.

Mr. Pinsent: Delivery could be made quicker in case of shares already physically deposited here. It would be rather slower on shares held in England.

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Mr. Frank: But in any event you could give them some kind of a receipt. They always could work that out. That delay won't be an important one.

HM, Jr: They would do things for themselves that they would not do for individual stockholders. They would act differently where they are buying for their own treasury rather than where they were doing it for individuals.

Mr. Frank: Most of them are able to buy their own shares. Some few States where there is difficulty involved. Most of them, their charters and State laws under which they operate would permit it. I don't think in most instances you would find that obstacle.

HM, Jr: I am fearful they are going to blame the market's gyrations more and more on the French and English and I don't see that you have anything to gain by waiting, and what I would like very much is not to wait until one of these two gentlemen comes back again, which takes a week. There are enough people over here representing England and France that some one person ought to be designated to try it out. Both of you have enough people in your missions here now so that one person could say 'let this person try it out' but not wait until somebody comes back in a month or two.

Mr. Pinsent: I would like to say, although I have not heard definitely, there is a prospect Mr. Whigham may sail on the 16th.

HM, Jr: I got that from Butterworth. These sailings are all so uncertain. Why can't they designate somebody? You have so many missions here now.

Mr. Pinsent: I think that could be done if the actual negotiations themselves don't occupy too much time.

HM, Jr: What I would like you to do, if you would, I would like this to go as a message from me to the Minister of Finance of France.

Mr. L-B: Yes.

HM, Jr: By cable.

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Mr. L-B: Yes.

HM, Jr: And the Minister of Finance in England. We think this is worth trying out; like to see it, if your Governments think it is worth trying, that they do it fairly promptly and try to use somebody over here or you can designate -- you don't have to designate your own Nationals. You can designate anybody to do it for you.

Mr. Frank: Yes. After all, you can do any negotiating you want before you vest, as we suggested, and if you have some advisers, American advisers, they could be designated to start your negotiations for you, as you would want American advisers in any event.

Mr. Pinsent: We would need American advisers in any event and I don't think that's difficult to arrange. Well, I will certainly telegraph at once along those lines, Mr. Secretary. I don't know whether our French friends are ready to proceed yet.

Mr. L-B: We have a sort of idea we might postpone it, this date, this inventory date. The first date was set before the 15th of November; returns had to be made the 15th of November. Then it was extended to the 15th of January and I think that this period of two months showed us that many people had returned and so I have not been aware that there has been some new delay contemplated.

HM, Jr: Here's the thing -- after all, as I explained to you the other day, you people are just as much interested as we are to have a healthy market here.

Mr. L-B: Yes.

HM, Jr: If this thing is going to work. That's why I mentioned from the standpoint of America it would be important to know that all United States Steel owned in England and France and Canada was off the market. If only a part, then there is still the French stock to come; still the Canadian stock to come, and it would not be accomplishing what I had in mind, although I am not going to say the English should go not go ahead, but it would be much better if they know all United States Steel coming on the market in

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the next 12 months was off, and then one company after another, and it can't help but help our market.

Mr. Frank: If you had joint authority for negotiating in each instance.

Mr. L-B: I think that could be done.

Mr. Pinsent: I think that could be done if you are ready. If you are in a position to vest, your Treasury, the French holdings of any particular holding as soon as the contract has been concluded here.

Mr. L-B: We are late compared with them in that matter.

Mr. Pinsent: But there is this: between now and January 15th, which is only a week, and even if you did a few more registrations in that, the matter would not be important?

Mr. Frank: That additional amount could be sold on the market later on.

Mr. Pinsent: Yes.

HM, Jr: But you understand it very well?

Mr. L-B: Oh, yes! I understand very well. But, as you said, it's worth trying.

HM, Jr: You get your money promptly and you get it on this side. You get it where you need it.

Mr. Frank: I am sure if there were a delay, there is a way of accomplishing it -- delay incident to shipping; it can be worked out.

Mr. Pinsent: I did not know whether the practice or business customs in this country would stand in the way.

Mr. Frank: I don't think so on the question of delivery. They can have their agent abroad handle it. Delivery over there. They could put it in an incinerator. That would be considered cancellation. I don't see why

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they can't work it that way.

Mr. Pinsent: When an American company bought its own shares, would that be for cancellation?

Mr. Frank: What I meant is cancellation of the certificates. Then they could re-issue if they knew they were destroyed. They could restore it over here. That stock is called Treasury stock.

Mr. Pinsent: In our country it is against the law for a company to hold its own shares.

Mr. Frank: Well, literally, the stock is, so to speak, in a state of suspended animation. It is Treasury stock and can be re-sold under certain conditions other than in the case of new subscriptions. Treasury stock. For instance, to use the lawyers' lingo, can be sold "free of pre-exemptive rights." There are differences and they can't vote those shares; in other words, while those shares are in the Treasury, they cannot be voted by the company because that would give the company domination of assets belonging to all the stockholders, but in most States they can repatriate their own securities.

H.M., Jr.: If you will, gentlemen, pass that on, I will appreciate it. Again, bon voyage!

oOo-oOo

January 9, 1940.

Dear Mr. Keeshin:

On behalf of the Secretary I am acknowledging your letter of January 6th, which encloses a copy of a communication from Mr. Andy Bassi, as well as a memorandum written by Mr. Sheahan. Mr. Morgenthau is glad to have these documents and the information they contain.

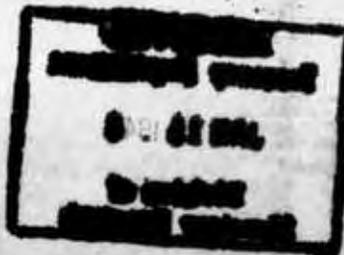
Sincerely yours,

(Signed) H. S. Klotz

H. S. Klotz,
Private Secretary.

Mr. J. L. Keeshin,
President, Keeshin Freight Lines,
Incorporated,
221 West Roosevelt Road,
Chicago, Illinois.

GEF/dbs



*Mr. Tolson
Pls ack*

KEESHIN FREIGHT LINES, INC.

J. L. KEESHIN
PRESIDENT

221 WEST ROOSEVELT ROAD
CHICAGO

January 6, 1940

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

My dear Mr. Secretary:

I am forwarding to you,
herewith enclosed, a copy of a letter I
received from Andy Bassi, written at Pechih,
Kweichow, under date of December 5, 1939;
also a copy of a memorandum Mr. Sheahan
addressed to Dr. Francis K. Pan, under date
of December 4, 1939.

Very truly yours,

J. L. Keeshin
J. L. Keeshin

JLK:LR

Encs. (2)

Fechih, Kweichow,
December 5, 1939

Dear Jack:

It has been a while since I've written you, not as long however, as you might think. I have torn up three letters and let them pass. I know of two Maurice tore up also. One thing we have learned, if nothing else, and that is to suppress the urgent desire to blow up. My hair is grey on top now, but not from worry, just from trying to hold my temper.

Maurice has had the brunt of the burden on the corporate structure which while quite important, assumed all too large a proportion in the entire picture - it takes too long to write about it and as I know you have received copies of everything that has transpired, you have I know a comprehensive picture of everything as it exists up to date.

Make no mistake about these people, no one from the outside world is coming in here and take charge of anything. We have found that out many times over. They just will not take anything as you give it to them. They must scramble up the whole dam thing into an inextricable mess which requires starting all over again. Gradually when every "ward healer" gets his patronage arranged for, they then come to some sort of compromise and as in the case of the Corporation, it is then rewritten and agreed upon and sent to the Executive Yuan where it is passed, after some more changes, and there it is whether you like it or not. All the while this goes on "Rome Burns", transportation goes absolutely to hell. They don't know what they want nor what is good for them, but they are going to have something and all they want from us is advice and suggestions, so that they can use the outline for something they feel is original with them.

There is no question about this commission having accomplished more on paper than any in recent years, but insofar as anything specific having come out of it, time alone can tell and I won't be here when it does and seriously I won't care.

We all have traveled over the practical whole of this place, meaning Free China. We know what is needed, have written reports, held discussions, tried to get action but always that procrastination that drives you mad. More than two months ago I went to Haiphong to find some machinery, parts, tools and several other items. Records were such that nothing could be found. I made a tour of the godowns and located most of the equipment I wanted, ordered it shipped immediately. It hasn't arrived as yet and the road is closed from every direction from Kunming, and now China has only the Burma Road and the French "toy railroad" left from the South, and Russia of course is still supplying materials on the North.

I am now making an investigation of the new Szechwan Lunnan Highway from Chungking, west to Long Chan and then South to Kuming. So far so good. I am writing this at Fechih, also spelled Pichieh. We expect to be in Kuming by the weekend. Van Patter should be there by that time as we have had the shops equipment rerouted over the French Railroad for trans-shipment from Kuming. You remember the Big Shops that were to be at Kwiyang and in operation before we left? Well they are not there as yet.

The two hundred tractors and semi-trailers, International D-50 are stuck in Haifong until a new cut-off to Hochik is completed or the Japs driven out.

C O P Y

- 2 -

The Japs operated an aircraft carrier outside of Pakhoi, for months, bombing and strafing the Dondang, Nanning road, and when they decided to land, there were no troops there to stop them or delay them, but a few green recruits whose commanding General was in Chungking. Laugh that off.

I made a survey of that road while it was being bombed daily, from 9 A M until 3 P M. The road was in terrible condition and a brand new unit traveling over it into China, was a wreck by the time it reached safety, if it didn't get a shower of machine gun bullets or a pineapple. With labor a dime a dozen, that road could have been maintained at night or after 3 P M and with any kind of surface, a truck could have made the run from Dusk to dawn to safety, and all together, in one piece.

If this road I'm doing now will handle semi-trailers, we will have the two hundred units used here, if we can ever get them into China. I will do everything I can to help these people, but worry about their shortcomings, I definitely decided upon that - after driving myself to bed in Haifong, a nervous wreck and with a wrecked stomach.

Maurice came back from Burma with Yellow Jaundice, and I still think Malaria. Van was down when I met him in Kweiyang and when we ended up at Chungking, we had lost among the three of us, 60 or 65 pounds. I lost 24, and if you can imagine me with 24 pounds off, you can picture what the rest of us look like.

You probably realize by this time that there will never be a Keeshin Oriental Line in China. They just don't let foreigners own anything and a foreigner cannot become a citizen. The Government wants a 51% slice of everything and they "Staff" everything to death. There are some fine people among them and we have met the very best of them, and you can lay your bottom dollars on K.P C and Bang as being head and shoulders over all the others. Francis Pan with whom we live and who is "Larson Officer", between the Commission and the Ministry, or more particularly the Minister, is another outstanding person but plays both ends from the middle. He just has to, under the circumstances. So Jack, if you can do more than "squeeze" some traffic out of this thing, you are still on the short end of the deal, as well as ourselves.

I'd hate like hell to see you come over here. You would just go mad. First you could not stand the filth we are getting used to, and there wouldn't be any sense to it in the second place. All I can promise you is to carry on in a creditable way and when this is over with, try to get some satisfaction out of seeing at least some semblance of order out of a mad scramble.

I want to wish you a Merry Christmas and a Happy New Year, and the same to your good family. It wouldn't be amiss to ask you to drop us at least your first letter letting us know what your reactions are.

Sincerely,

(Signed)

"Andy" Bassi

P.S. We have gotten along quite well to date, just a few sharp cracks at each other when the nerves are at raw edges.

C
O
P
Y

c/o Ministry of Communications
Chungking, China
December 5th, 1939

Mr. K. P. Chen
Universal Trading Corporation
630, 5th Avenue
New York City, New York
U. S. A.

Dear Mr. Chen,

Furthering my letter to you of December 4th with which I transmitted a memoranda concerning the production of wood oil. In reviewing this letter I find an error appears on page 2. In the last complete paragraph on that page, will you please change the average production of wood oil per farm from 75 Shih Catties and 82.5 Llbs. to read 36 Shih Catties and 39.6 Llbs.

Very truly yours,

(Signed) M. E. Sheahan

cc. H. E. Minister Chang Kia-NGau
Mr. J. L. Keeshin

Memorandum

to

Dr. Francis K. Pan

A few days ago you asked me to suggest a formulae for evaluating properties coming into the China Transport Corporation; in view of the absence of reliable records, suggest that an inventory be requested through the field offices of the various divisions of the Ministry and Foo Shing, of all automotive equipment, segregated as to types, models, year of manufacture, motor and chassis numbers, etc., with the party taking the inventories best estimates of the remaining life of the equipment. When this inventory is received from all parties, an additional inventory should be requested with the identical information, as the equipment should have moved in the interim between the two inventories, it would have the benefit of a separate appraisal on each active piece of equipment. The information with respect to each piece of equipment should be collated to a single card and where too wide a discrepancy is noted, special investigation should be made.

If the foregoing is considered by the Organization Committee I should be pleased to aid in setting up proper machinery for the dual inventory.

(Signed) M. E. Sheahan

Chungking

Dec. 4, 1939

To

H.E. Minister Chang Kia-NGau

We have completed inspection of the Chungking repair shops and garages of the Szechwan-Kwangsi Highway Administration, the Foo Shing Corporation and the Ministry of Communications' shop buildings and repair sheds located on the north bank of the river.

The Szechwan-Kwangsi Highway Administration facilities are located approximately 2 Km. from the Yangtze Ferry. Considerable congestion of trucks and busses awaiting and undergoing service was noticed, and according to information furnished us some of the vehicles were not operating due to gasoline shortage. Some repair work was in progress outside the sheds which necessitated mechanics lying on the muddy ground while making chassis and motor repairs. The greater portion of the yard at this location was slushy and mud-covered and a portion of the ground in the repair sheds was also found quite muddy due to water running from the yard. Due to lack of parking space vehicles were parked in a double row directly in front of the trucks that were being worked upon. This parking cuts off a part of the daylight where the mechanics work and make it impossible to service late arriving equipment. The mechanics of necessity therefore, work outside in the rain or lying on the damp ground, working conditions that are not conducive to the best efforts of the working personnel.

The shop and yard we do not believe to be located in such a way that further expansion would be economically sound or practical. Should the surrounding buildings be torn down to permit expansion, the problem of excavation would arise, as this land is higher than the surrounding area.

In planning location of maintenance shops or expansion of existing facilities prime consideration must be given to the contemplated operation of trucks and busses, for example, the Foo Shing properties, located about 16½ Km. from the Hai-Tang-Chi bus depot, along the Kweiyang Highway. We are informed that a road is to be built from this location to the Yangtze River, a distance of

approximately 2 Km., in order that incoming and outgoing cargo may be diverted to river junks for distribution to Chungking proper or to Luhsien on the new Kunming cut-off. If such an operation is found economical it would mean that very few trucks will operate as close to Chungking, as the aforementioned Szechwan-Kwangsi Highway Garage, eliminating the need for the latter's facilities, except for the servicing of busses and occasional trucks. We believe there will be sufficient use of the Szechwan-Kwangsi Garage to warrant necessary improvement to eliminate the present unsatisfactory working conditions and recommend that the Garage be equipped as originally planned, at least until such time as a better arrangement can be worked out.

In visiting the Foo Shing properties some 16½ Km. from the bus depot along the Kweiyang Highway it was quickly noted that the godowns, shop and garage buildings were located in closer proximity to each other than would ordinarily be recommended in view of the ever present danger of air-raids. (It should also be considered however that the properties are located some distance from congested areas and may be more safe for this reason.) The entire properties are well planned and ample room has been allowed for expansion. The properties consist of drivers quarters, loading platforms, machine shop and repair sheds, both of the latter having cement floors and substantial roofs. Some of the loading platforms are built to truck floor heights with 2½" beams running crosswise, permitting transfer of cargo across the platforms by sliding or rolling on these beams which are anchored to the cement floor, other parts of the platform are only ordinary cement floor heights and are intended for storage purposes.

The machinery shop is so laid out and illuminated by sky lights as to permit the use of the line system of rebuilding motors. To eliminate the use of expensive and dangerous gasoline, a parts washing tank should be installed. The repair sheds are located quite close to the machine shop with space for housing about 20 units, between the

sheds. The Sheds have cement floors and good walls on three sides of each building. The yards have been paved with crushed stone and clay and rolled smooth. Necessary shop tools and equipment should be transferred to this location as quickly as possible to facilitate the maintenance program in the Chungking area.

The shop building and repair sheds on the north bank of the river are of sufficient size to service and repair 30 to 35 units of equipment daily. The machine shop building is of sufficient size to permit installation of any machinery and tools necessary for complete rebuilding of motors, transmissions, differentials, etc. The building is well constructed with good roof and cement floors. The 5 repair sheds are conveniently located and similarly well constructed with good roofs and hard floors. One of the sheds has 9 pits available for lubrication and chassis inspections. It is suggested that the pits be equipped with electric lights.

The parts manufacturing building equipment and ground located about 7 Km. north of Chungking on the Chengtu road were reviewed in detail with your Mr. C. C. Tsui, who explained the present and future plans for the manufacturing of parts and shop equipment. Their present equipment permits the manufacture of pistons, bushings, tire pumps, hydraulic jacks and hand cylinder reboring bars, however the production of this plant is quite limited, and awaits only additional equipment to speed up production and manufacture of other essential motor parts as well as transmission and differential gears. A river loading dock is under construction and all of the buildings are of good construction and conveniently located. They are apparently of sufficient size to accomplish the purpose for which they are intended. We do not believe that further expansion of this plant should be undertaken until such time as the present plant is working efficiently.

We have also reviewed 4 large and 10 small parking lots and housing sheds, the property of the Szechwan-Kwangsi Highway Administration located on the south bank. The property nearest the first

mentioned garage cannot be utilized until the bridge and road now under construction between the facilities is completed. The road will run across a rather deep gorge as no other entrance to the parking lot is available. Several thousand cubic yards of dirt and stone will be necessary to complete the fill after the bridge is completed to bring the level to a height that will make it possible to connect the short road on each side of the gorge. The parking ground is practically completed but of course is useless until the entering road is completed. The consolidation of Foo Shing and the several civil government facilities may make this location of less importance and consideration should be given to this eventuality. Other parking spaces were in the final stages of completion and one in particular, located about 7 Km. along the Kweiyang Highway, was in use. About 50 trucks were in parking sheds and it was noted that between 35 to 40 trucks, (of which 27 were new Dodges,) were apparently in good condition for highway use. It would seem more practical to operate these trucks that are in good condition, in preference to many other trucks presently operated, that are so clearly in need of repairs and servicing. The 4 large parking lots appear to adequately serve present operation. The 10 smaller lots can accommodate only a few pieces of equipment each and were all made possible by leveling a section along the highway.

In view of the as yet, indefinite plans for operation of the combined properties of the Ministry of Communications and Foo Shing, it is our recommendation that none of the existing facilities in the Chungking area be disturbed except for possible improvements as herein suggested until such time as the newer shops are properly equipped to maintain and service the equipment.

(Signed) M. E. Sheahan

Chungking

Dec. 4, 1939

To

H.E. Minister Chang Kia-NGau

The enclosed memoranda further explains the usual duties and functions associated with the positions of Traffic Manager, Controller and his assistants, the General Auditor, Auditor of Receipts and Disbursements, and Supervisor of Safety and Insurance. I have not attempted to detail the work to be performed in these particular positions as each of them are executive positions and require the exercise of mental initiative on the part of the individual selected to head the various departments and it is my thought that rigid and detail specifications at the inception might do an injustice to whoever is ultimately selected to head the several departments.

(Signed) M. E. Sheahan

Chungking

Dec. 7, 1939

Traffic Manager

The Traffic Manager assumes the dual responsibility of (1) securing a compensatory return for all traffic and (2) securing sufficient traffic to assure a compensatory return to the Corporation.

The Traffic Manager must be a keen student of economics, both national and international, as his work will involve both domestic and foreign trade. Under his direction there should be prepared a classification of the various items likely to be transported, with proper packing requirements to assure safety of cargo in transit. In this classification he must weigh the probability of damage, loss, and the ability of the cargo to pay, and many other factors, to the end that the classification as ultimately prescribed will permit the free flow of commerce and a compensatory return to the Corporation. Presently the matter of securing traffic particularly of import goods presents no problem. The matter of securing export on the other hand will be serious, and exports are of vital necessity in the securing of foreign exchange essential to the welfare of the Nation. The Traffic Manager must work very closely with the Controller in analysing expense of operation, business trends and other factors, and prepare a tariff with governing rules and regulations that will attract export trade and at the same time encourage the import of necessities. In all his undertakings the Traffic Manager must bear in mind the necessity of securing an "over-all" compensatory return, for example; Steel may be transported at a non-compensatory rate. If through a factory fabricated from such steel a shoe plant may be constructed, shoes being an article of relatively high value that can "pay" transportation charges, the transport charges upon the output of the plant eventually overcomes the losses incurred in transporting the steel. Truly the Traffic Manager must be a keen student of economics and his work cannot be reduced to a formulae. The only staff necessary in support of the

-2-

Traffic Manager are those subordinates to assist him in obtaining information and in the printing, publishing and distributing to known shippers and receivers of freight, of freight classifications and tariffs. In this connection it is suggested that a charge be made for each such classification and freight tariff supplies. In connection with passenger traffic similar problems concerning the publication of tariffs will confront the Traffic Manager.

In addition to the foregoing and in furtherance of the second concept of the Traffic Manager's duties, he must schedule in conjunction with the Operating department the departure and arrival of freight and passenger operations.

(Signed) M. E. Sheehan

Chungking

Dec. 4, 1939

Controller

The responsibility of the Controller under the proposed Organization chart of the China Transport Corporation differs somewhat from accepted procedure in that, he has under his jurisdiction the Accounting, Auditing, Treasury, and Insurance and Safety Departments. With the proper salesman's instinct the Controller should prepare his reports and supplementary analysis in such form that the Managing Director and the Board of Directors will be made to appreciate the full value of his contributions toward the successful management of the Corporation. He should supply the Managing Director with current reports which shall show, among other things the effectiveness of the Managing Director's lieutenants at various points in the Organization. It is the Controller's function to point out to the individuals in charge of various operations, their points of failure and to inspire them to greater achievements. In a corporation as large as the China Transport Corporation, the Managing Director will undoubtedly be a long-range executive who will not have the advantage of personal contact and visual conception of operation, being more or less dependent upon the Controller's reports and graphs for his guidance. Such reports must be prepared in such form that the Managing Director and other executives can construct an accurate picture of the happenings and conditions which lie back of the reports, and thus have a sound basis for conclusions and recommendations.

While the Treasurer is the chief custodian and disbursing officer of the Corporation's funds and handles all of the financial requirements, the Controller must serve as a check upon and through his General Auditor, audit the funds received and disbursed by the Treasurer. The Controller should also develop that analytical readings of events, both within and without, which is so essential to large scale undertakings.

The Controller contacts with other department heads in many matters pertaining to statistics and office routine, however, the actual physical jurisdiction of office work must quite necessarily belong to the head of whatever office is in question, as it is quite out of the question for the Controller to have any direct jurisdiction in offices other than his own. No man can serve two masters, neither can two master direct one man.

The Controller should prepare all statistics and reports of the Corporation's operations as may be required and must have the authority to require from all departments such information as may be necessary to prepare such statistics and reports. He may question excessive or unwarranted expenses and in conjunction with other department heads confer regarding revisions of budgets and reasons for deviations from the estimates in actual performance. Through his General Auditor the Controller checks commitments and disbursements applying on specific appropriations made by the Board of Directors and certifies to the correctness of reports covering such specific appropriations before they are presented to the Board of Directors for closing. It is his duty to interpret to the various departments, reports prepared under his jurisdiction particularly those reports dealing with expense of operations. He must compile budget estimates; make such studies of statistics of employment and wages as may be advisable to determine the Corporation's policy on these questions. The Controller's responsibility for advising other corporate officials as to general business conditions of this and other countries as a guide to the determination of general purchasing policies. He keeps in contact with provincial and national agencies that furnish statistical information. He makes studies of the statistics of the Corporation and makes forecasts and recommendations as a result of these studies, to the end that the Corporation may act intelligently and quickly in formulating its service to the shipping and traveling public.

Practically all forms of insurance require first of all a determination of what is to be insured, what the insurable values are, and what the amount of risk is, all falling within the scope of the Controller.

The Controller should prescribe the rules and conditions, observing the limitation imposed by the Board of Directors, under which payments are authorized in all departments of the Corporation. Through his General Auditor he must audit the accounts of the financial officers and all employees entrusted with corporate funds. He should examine recommendations for proposed expenditures for additions to capital account, and express an opinion as to their earning value to the Corporation. In like manner he should examine and report upon all proposed expenditures for repairs, improvements, or replacements. Whether they are within the figure fixed by the Board, or in accordance with any established policy, the General Auditor later determine whether or not expenditures have been kept within the appropriations. In brief a Controller is a broad-gauge man, adviser of the Managing Director and the Board of Directors and responsible for the compilation and presentation of all reports and statistics of the Corporation's progress. The General Auditor, Auditor of Receipts, Auditor of Disbursements, the Supervisor of Safety and Insurance and the Treasurer, are for all intents and purposes assistants to the Controller.

(Signed) M. E. Sheahan

Chungking
Dec. 4, 1939

General Auditor

In general the duty of the General auditor is to assure the Controller that the accounting work of the Corporation including decentralized departments, outlying agencies and subsidiary and associated companies, is being done in an accurate manner and in accordance with the general policies and instructions issued by the Controller. The General auditor's organization also includes Traveling Auditors who make periodical examinations at the various outlying locations.

General accounting is centered in the office of the General Auditor, and includes accounting allocations, book-keeping, statements and reports as required by the Controller. Under this Department is also performed the accounting and preliminary statistics of time keeping, pay-roll, inventory control, book-keeping, cost, estimating, analysis, statements and reports.

Assisting the General Auditor are the Auditor of Receipts and Auditor of Disbursements. As their title implies, the Auditor of Receipts handles accounts receivable including bills collectable, and the Auditor of Disbursements handles accounts payable, claims, pay-roll and other items of a disbursement nature.

It is intended, that under the general direction of the Controller, his various assistants shall establish internal checks. These are made continuously in the regular course of business through the adoption of proper routines and systems, so designed as to leave as little as possible to the judgement of the clerical personnel, and definite instructions should be issued in a systematic manner, covering policies, definitions of accounts, and routines, particularly those affecting transactions which have to be dealt with frequently, such as accounts receivable, pay-roll routine, and costs. It is also important that the routine provide

in the regular procedure automatic proof of the accuracy of the work. Routine checking should be so assigned that the work of one group of individuals automatically checks the accuracy of the work performed by other groups thus minimizing the possibility of both errors and collusion.

I personally favor the more simple plans of internal checks as my experience has been, that collusion cannot be stopped, but can best be discovered through simplicity. Involved procedures that are not readily understood sometimes pave the way for collusion.

(Signed) M. E. Sheahan

Chungking

Dec. 5, 1939

NO. 257

Rangoon, Burma, January 10, 1940.

CONFIDENTIAL

SUBJECT: Motor trucks for China at Haiphong to be reshipped to Rangoon because of destruction of Nanning highway; China's supplies at Hong Kong moved to Rangoon; record transit shipments in December; Burma Railways gain materially and reduce rates; some duties and port charges refunded to Chinese; American gasoline for China; imports at Rangoon.

THE HONORABLE

THE SECRETARY OF STATE,

WASHINGTON, D. C.

SIR:

I have the honor to report that motor trucks purchased by the Chinese Government and now at the port of Haiphong, Indochina, awaiting shipment into China, are to be reshipped to Rangoon, according to information received here. Chinese representing the War Department and the Aviation Commission, who came here recently to look into port, assembly, and transport facilities, informed the local office of the Southwest Transportation Company that 1,060 trucks were to be forwarded to this port as soon as possible, and advices received from Hong Kong by the local branch of the Standard Vacuum Oil Company are to the effect that all trucks at Haiphong, with the exception of 180 Renault units, will be reshipped to Rangoon. The total number of trucks now at Haiphong is reported to be 2,200.

It is stated that reshipment of the trucks has been made necessary by the destruction of sections of the Nanning highway, following the Japanese invasion of southeastern China and the occupation of

Nanning

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Hanning and adjacent areas. The movement of motor trucks into China from Haiphong has been over that eastern highway.

It is said that 750 of the 1,060 trucks that are to be reshipped to Rangoon at an early date are for the Chinese Army, 250 for the Chinese Aviation Commission, and 60 for the Ministry of Communications. It is reported that the Army units consist of G.M.C. and International trucks, and that the other units are also American vehicles. The motor trucks now at Haiphong are said to include 408 belonging to the Foo Shing Trading Corporation.

Supplies at Hong Kong Moved to Rangoon.

During the last several months Chinese Government supplies stored at Hong Kong have been moved to Rangoon for shipment into China. These have included, in addition to some war materials, steel products, shop equipment, tools, army blankets, chemicals, and a variety of other articles, and the total has reached several thousand tons. It is stated that 1,500 tons additional are now en route to Rangoon, leaving less than 1,000 tons of materials at Hong Kong, and that these latter consist of old and useless articles not worth shipping. Some of the supplies received at Rangoon are said to be likewise useless, and they will not be shipped into China.

The Southwest Transportation Company, which is in charge of Chinese Government traffic over the Yunnan-Burma highway, has rented additional local warehouses having a capacity of about 10,000 tons. The company's principal

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principal storage facilities at this port since it commenced operations in Rangoon have consisted of salt warehouses owned by the Port Commission, 30 of which, with a capacity of more than 20,000 tons, it was able to rent. Six of these warehouses have had to be vacated recently because of heavy salt imports. It is rumored that some of the supplies of various kinds destined for China which are now at Haiphong, and which are said to total at least 70,000 tons, are to be reshipped to Rangoon, but there has been no confirmation of this rumor here.

Record Shipments in December.

It is reliably stated that more than 5,000 tons of war materials, gasoline, and other supplies for China were shipped from Rangoon to Lashio during the month of December, and that about 4,500 tons were moved from Lashio to Chefang, the point in China about 24 miles north of the frontier where the trucks from Burma unload and turn back, and where trucks of the Southwest Transportation Company pick up the loads, and take them on to Yunnanfu and Chungking. The shipments by both rail and road were the heaviest made in any month up to this time.

For transport from Lashio to Chefang the Southwest Company still depends chiefly on trucks operated by S. Vertannes, the Armenian haulage contractor of Rangoon who has been transporting China's munitions from Lashio since shipments were commenced in February 1939, but in addition to the Vertannes trucks, which number 180, about 80 trucks of other

contractors

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contractors are also being used at present. The company wishes to use 200 of its own trucks in Burma, in connection with plans to forward 200 tons daily, or 6,000 tons monthly, from Lashio, but permission for their use has not yet been granted by the Defense Department of the Burma Government. Questions of reciprocal registration regulations are involved, as are also objections raised by contractors now operating trucks and by truck dealers in Rangoon, who fear losses in transport work and in truck sales if Chinese Government trucks are allowed to operate in Burma. The company maintains that it will be unable to reach the desired figure of 6,000 tons a month unless it can use some of its own trucks, as the trucks available for hire in the Lashio area are not sufficient.

Three to four days are at present required for the round trip Lashio-Chefang-Lashio. It has been done in two and a half days, but this is not usual. Some of the trucks in service are constantly under repair. Each truck carries about two tons, and to ship 6,000 tons monthly from Lashio it would be necessary to load an average of 100 trucks daily.

Burma Railways Cut Rates; Show Gain.

On war materials for China, exclusive of explosives, the Burma Railways have reduced their rate from Rangoon to Lashio by 10 shillings a long tone, making it £3, or Rupees 40 (about \$12.00 at present exchange). Explosives that are packed in such a manner that they can be handled with relatively little risk are now carried at a rate of £3 - 10 - 0, but others, such as

tetryl

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tetryl, pay a much higher rate. Only a limited number of cars loaded with explosives are permitted in a train, and the cars are painted white to show that they contain highly dangerous materials.

The Burma Railways expect to balance their budget in the present fiscal year, ending March 31, 1940, largely as the result of the transit traffic to China. The budget has not been balanced since 1929-30, and in the last fiscal year the Government-owned transportation system failed by Rupees 1,371,856 (about \$480,150) to pay interest charges. In the first nine months of the present fiscal year there was an increase in freight earnings of more than Rupees 2,000,000 (about \$600,000 at present exchange) compared with the preceding year, much of which was due to payments by the Chinese Government.

Some Duties and Port Charges Refunded.

The Burma Government has refunded about Rupees 500,000 (approximately \$150,000 at present exchange) as customs duty paid on war supplies for China which were imported at Rangoon but which were not cleared for re-export before April 20, 1939, the date on which the present rate of duty of one percent ad valorem became effective. The former rate of duty was one-sixteenth of the ordinary rate, which in the case of arms and ammunition is 50 percent ad valorem, and the amount refunded represented the difference between the two rates. A further refund of duty paid at the former rate on war materials cleared for re-export but not actually re-exported until after April 20th is being sought

by

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by the Chinese. The Port Commission has refunded about Rupees 80,000 (\$24,000) in demurrage charges, which resulted chiefly from the storage in barges in the Rangoon River, for many months, of high explosives. The concession was offered as an inducement to the Chinese to remove the explosives and ship them to China.

Increased Shipments of Gasoline to Rangoon.

American gasoline for China entered at Rangoon up to this time has totaled 35,750 drums of 53 gallons each, or 1,894,750 gallons. The total gross weight has been more than 7,000 tons. Some of this gasoline has come to Rangoon direct from the United States on American vessels, and some has been received from Hong Kong, where it was re-shipped. It is stated that 800,000 gallons of a shipment of 1,900,000 gallons of American gasoline which has just reached Hong Kong by tank steamer will be reshipped to Rangoon after being placed in drums there. Chinese interests here understand that hereafter half of the gasoline destined for China will be sent to Rangoon, and the other half to Haiphong, instead of one-third to Rangoon and two-thirds to Haiphong, as heretofore. However, according to information just received by the local office of the Standard Vacuum Oil Company from the office of that company in Hong Kong, Dr. H. H. Kung, Finance Minister of China, has ordered that all future shipments of gasoline be made to Rangoon. If this information is correct, the decision reached is probably due to the recent bombing by the Japanese of the French railway from Haiphong to Yunnanfu.

At

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At this port the gasoline is handled by the Standard Vacuum Oil Company, which is the only American oil concern with a branch here and having the required facilities and permits. It is understood that purchases of mineral oils for China by the Universal Trading Company of New York, under the Export-Import Bank credit, were divided equally between the Standard Oil of New York and the Texas Company.

Trial Shipment by River Shows Saving.

A trial shipment of 7,250 drums of gasoline received from Hong Kong has been made by river from Rangoon to Bhamo, for transport by truck from there into China, the road from Bhamo connecting with the Yunnan-Burma highway 105 miles north of Lashio. This road, which is about 100 miles long, is in poor condition, but it is motorable during the dry season. It is estimated that to make it a metalled road would cost Rupees 600,000 to 700,000 (\$180,000 to \$210,000 at present exchange), and that the cost of making it a tar-surfaced highway would be Rupees 1,600,000 (about \$480,000). There is no present plan for the extensive improvement of the road. The Chinese have found that there would be a substantial saving by the use of the Irrawaddy River instead of the railway, not only in freight charges, which are about \$2.50 a ton less, but in handling and port charges, as supplies could be discharged direct from steamers into river barges, but they have no desire to do anything that might affect their relations with the Government-owned Burma Railways, which are, and

have

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have been, cooperating with them. Also, the Burma section of the Yunnan-Burma highway, from the railway terminus at Lashio to the border, is being made an all-weather road.

Materials for China on Way to Rangoon.

The first American motor trucks for China to be shipped to Rangoon in a number of months are expected to reach this port tomorrow on the American steamship EXPORTER, which has in addition other cargo, the total exceeding 3,000 tons. The S.S. PUERTO RICAN, which left New York on November 4, 1939, is bringing the first of several shipments of aircraft parts for the new factory of the Central Aircraft Manufacturing Company at Loiwing, China. The S.S. SAN ANTONIO, a vessel said to be under the Panamanian flag, which left Hong Kong some time ago with 1,500 tons of Chinese Government freight and proceeded to the Netherlands Indies to take on board for Rangoon war materials for China carried by German vessels which sought refuge in Dutch ports, is due here within a few days. The war materials are said to amount to 3,000 tons or more. It is reported that additional cargoes of war supplies from Russia will be brought to Rangoon by the British steamers GRACEFIELDS and BLACK HEATHER, but Chinese interests here have no information concerning the probable dates of arrival.

Respectfully yours,

Austin C. Brady
American Consul

Distribution:

1. Original and four copies to Department.
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3. Copy to American Embassy, Chungking.
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800
ACB/cp

TO:

1-10-40

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MRS. KLOTZ

● The Secretary may wish to see this before he talks with Messrs. Doughton and Taylor today.

JPC, Jr.

From: MR. COTTON

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE January 10, 1940

TO Secretary Morgenthau
FROM Joseph P. Cotton, Jr.

Re: Status of Export-Import Bank—
RFC Credit to Finland.

As publicly announced, the credit is for \$10,000,000 to be advanced by the Export-Import Bank and by the RFC to a domestic corporation to be formed by Finnish interests, for purchases to meet civilian needs and of agricultural surpluses. The Finnish-American Trading Corporation has now been formed in New York. The Export-Import Bank acted formally to approve a \$3,000,000 credit along these lines, on condition that the Finnish Government guarantee repayment by the corporation, all purchases made under the credit to be approved by the Bank, it being understood that the RFC would assume the balance of the commitment, namely, \$7,000,000.

The RFC has not acted officially in the matter, hoping, no doubt, that the Export-Import Bank would get more funds from Congress and would be in a position to handle the whole credit before the Finnish purchases should exceed \$3,000,000.

There has been a delay in arranging the guaranty with the Finnish Government due to objections by the RFC lawyers to the form of the guaranty initially discussed with the Finns. It is expected, however, that this matter will be cleared up any day now.

As regards purchases, none have been made to date under the credit and cannot be until the guaranty is cleared up. The Finns asked the Bank whether the credit could be used to pay for certain purchases which they had already made in this country, and were turned down although the Bank could have agreed to this under the terms of its commitment. It is said, however, that this is a matter of little concern to the Finns. The Finns have indicated that they are arranging for purchases under the credit of gasoline, gas masks, peas and rye aggregating some \$2,000,000 of business now under way.

J.P.C.

January 10, 1940.
5 p.m.

H.M.Jr: Hello.

Operator: Mr. Welles

H.M.Jr: Right.

O: Go ahead.

Sumner
Welles: Hello.

H.M.Jr: Hello Sumner.

W: Hello Henry. I asked Doug to have Jarmillio to inform me this afternoon whether Mr. Traphagen had been in touch with them in regard to the appointment, conversation with them on Friday. They've had no word from him whatever and if our plan is going through according to schedule, it seems to me desirable that he be checked up and asked if he cannot arrange to come down and notify them that he is coming down.

H.M.Jr: He promised me he would and I'll have Joe Cotton call him at once.

W: All right.

H.M.Jr: He said he'd come down Friday night.

W: Well -

H.M.Jr: I'll have Joe call him.

W: My thought, Henry, was, you remember, that he ought to have a preliminary talk with them Friday afternoon before we have the meeting in your office, Saturday morning.

H.M.Jr: Yes he said he'd come down late Friday, but I'll have Joe call up and let you know.

W: Fine. I don't think there's any use in our having the meeting in your office.

H.M.Jr: No.

W: Unless he's had a prior talk with them and told them what he thinks is the minimum.

H.M.Jr: I'll - I'll have - if he's still there, I'll call you, otherwise - let you know one way, either tonight or tomorrow morning.

W: All right.

H.M.Jr: But they'll make a call immediately.

W: Sorry to bother you.

H.M.Jr: No. bother.

W: Thanks. Goodbye.

JT

PLAIN

LONDON

Dated January 10, 1940

Rec'd 3:08 p.m.

Secretary of State,
Washington.

81, January 10, 6 p.m.

FOR TREASURY FROM BUTTERWORTH

I understand that the Prime Minister's speech at the Mansion House last evening was designed to initiate what might be called an anti-complacency campaign, that other speeches by Cabinet Ministers are to follow designed to bring home, in the absence of air bombardment, the reality of war and the necessity for sacrifice to the vast non-income tax paying section of the population. In this general connection reference is made to my 2695 and 2698 of December 21, 7 p.m., incidentally an illustration of the absence of coordinated effort is afforded by the fact that just before Christmas the Ministry of Information published for wide distribution a pamphlet entitled "Assurance of Victory" the tenor of which runs counter to the purposes of the Prime Minister's speech and is in bold opposition to Reynaud's view that "time is a neutral". On the vital question of reducing domestic consumption and limiting or preventing rises
in

-2- #81, Jan. 10. 6 p.m., from London

in wages and prices the Prime Minister stated: "The wealthier classes have suffered a very heavy reduction in their income and we have left them mighty little prospect of being able to increase it again . . . it is not possible for them alone to solve the problem of how to reduce the consumption of unnecessary articles because two-thirds of the consumption of the people of this country is by those with only small incomes. It is necessary that they too should make their sacrifices, as is done not only in totalitarian Germany but also in the great democracy of France. I do not mean to imply by that that there must be no increase in wages but I do say that it would be a mistake to tie up wages to the cost of living which can do no good to anyone, because it can only give violent impetus to the vicious spiral of the alternate rising of prices and wages and that is a thing which all of us want to avoid. I do not believe any competent authority upon economics would dispute the truth of what I have just said." Mr. Ernest Bevin, one of the heads of the British trade unions, immediately answered Chamberlain in the Labor DAILY HERALD as follows: "The policy of the Government as I see it is to talk about sacrifices by people who had nothing to sacrifice when the war started. Of those wage-earners to whom Mr. Chamberlain talks of sacrifice, 90 per cent were on wage standards that left no margin. To reduce their purchasing power as is now being done only reduces the efficiency standard

-3- #81, Jan. 10, 6 p.m., from London

standard of the people and such a policy can only result if this war lasts a long time in outbreaks of labor troubles of a serious character", the first part of this statement is factually incorrect. There are low paid unskilled workers who are living close to the subsistence level if they are supporting large families but the skilled workers and the well organized wage earners in the transport and distributive trades are not working for such low wages and something more like 20 per cent or less would be nearer the mark than 90. The hardships are being suffered by the small shopkeepers in evacuated areas, the unemployed, old age pensioners and the casual laborers with large families. An interesting article on the wage problem will be found in the ECONOMIC JOURNAL for December by E.A.G. Robinson which also contains Keynes' statistical analysis on which his compulsory savings plan was based. An article in the ECONOMIST of December 16th (p. 405) which expressed the hope that the trade union attitude towards the wage-price problem would be realistic seems to be proved rather too optimistic by Bevin's statement quoted above, in spite of the swing over to substantially Keynes' point of view by much of the press which was opposed to it on its publication. Meanwhile the cost of living had risen by the 1st of December by $11 \frac{1}{2}$ per cent over August 1 and wholesale prices had increased in November by 11 per cent over the August average. There is no index of wage rates

rates available for the period since the outbreak of war but wage increases have been extensive. The DAILY HERALD stated on December 20 for example that wage increases had been obtained for 4,800,000 workers in the 15 weeks since the outbreak of war amounting to stlg 36½ million a year. Another 2½ million or more were reported to be negotiating for wage increases at the turn of the year including workers in the engineering and shipbuilding trades, railway workers and coal miners. At this rate the inflationary spiral is certainly being induced and the efforts of the Government gradually to woo the trade unions into an attitude of accepting an inevitable reduction in the standard of living would seem to be making little headway.

One other statement of the Prime Minister's is of particular interest: "This collaboration between France and ourselves for humanitarian purposes (i.e. Turkish relief) is just another instance of that close, that even intimate, association between us that now covers every aspect of the war, military, political, financial, and economic. I cannot help thinking that our experience of this association during the war will prove it to be so valuable that when the war is over neither of us will want to give it up, and it may even develop into something wider and deeper, because there is nothing which would do more to facilitate the task of peaceful reconstruction which has got to be undertaken some time. There

is

-5-#81, Jan 10, 6 p.m., from London

is nothing which would contribute more towards the permanence of its results than the extension of Anglo-French collaboration in finance and economics to every nation in Europe and indeed perhaps to the whole world."

I have come across no evidence to indicate that the British Treasury made the Anglo-French financial agreement with ideas in mind of permanency; on the contrary reference is made to the third from the last paragraph of my 2698 of December 21, 7 p.m. The same is no doubt true of the Anglo-French economic arrangement though procedure and practice may leave in time deeper marks. But in any case hypothetical prophecy is futile if for no other reason than the fact that the British instinct and habit of action is to pick up the tool for the job only when the job is before it and at this stage it is impossible to measure the character or condition of the peace-time job and which tool or tools can or will be grasped. Nevertheless this war time development seems well worth watching.

JOHNSON

KLP

10 JAN 11 1941

January 10, 1940

3:00 p.m.

PRESENT:

Mr. Purvis
Mr. Bloch-Laine
Capt. Collins
Mr. Cochran
Dr. White
Mrs. Klotz
Mr. Cairns (Short time just before meeting
ended.)

HM,Jr: Will you start?

Mr. Purvis: May I?

HM,Jr: Please.

Mr. Purvis: We have got some open items still on individual alloys and we have one on those general questions. Which would.....

HM,Jr: Any way you want.

Mr. Purvis: I telephoned to Mon. Monnett after I got word about the desirability of postponement. Is there anything I can learn on that or convey on that? Naturally there was great anxiety to learn on the other and what I could learn.

HM,Jr: Let's come back to that and maybe I can think of an answer before you leave.

(Mr. Purvis laughed.)

Not an answer but an explanation.

Mr. Purvis: Yes, quite.

Molybdenum. There was an open item on the Green Cananea Mine as to whether or not that was covered by your arrangement.

HM,Jr: Weren't you going to find out about that?

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Mr. Purvis: If so, I slightly misunderstood that. I understand they had a sales arrangement with Climax but I have had no contact with Climax as I thought it desirable I should not.

HM, Jr.: May I check who was to do that?

Mr. Cochran: Captain Collins.

Capt. Collins: No, sir. Not I.

HM, Jr.: It has not been done.

Mr. Purvis: Everybody is squirming slightly. If it were something I could pursue I would be happy. I have kept away from any of the molybdenum people thinking it was dangerous for me to mix in. What we would have to find out is whether they have a sales arrangement with Climax and whether that automatically would be covered with the Mexican mine. I did send some particulars on to you as to the setup.

HM, Jr.: It was in my mind that I had nothing to do with it, because I did nothing. Is it difficult for you to contact them?

Mr. Purvis: I don't think so. Let me try then. One thing I think you were going to have looked into and that was the possibility with the nations contiguous to Germany, Italy particularly, as to whether we could arrive at anything that would tend to close that avenue.

HM, Jr.: Italy isn't a very good example. If you say "a country contiguous to....."

Mr. Purvis: Yes, correct.

HM, Jr.:because -- well, let's take Belgium -- we have no excuses, you see? As a matter of information Dr. White has looked into the question of what happened on molybdenum in this country. This is a matter of information. What's the answer, Harry?

Dr. White: That the countries which are now receiving are small, no larger than those they have been receiving in the past. That speaking of Italy -- Italy imports from the United States.

HM, Jr.: Are unimportant.

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Dr. White: And no larger than they were before.

Mr. Purvis: And when you say no larger than they were before that does not mean any abnormal bid when stocking up might have been going on.

Dr. White: Our exports to Italy since the outbreak of the war were 37,000 in October, 38,000 in November, none during the first three weeks of December. In the first eight months prior to the outbreak of the war our exports of molybdenum to Italy averaged 35,000 per month. That is not much in excess of what they have been using themselves, but don't know exactly.

Mr. Purvis: It does not look like a considerable outlet.

Nickel. I got a cable from the other side in which they pointed out, on commercial grounds there was absolutely no excuse for doing what I had asked them to do. Actually 400 of the 835 tons were packed and in process of loading on boat, which was sailing January 9th. Felt they could not delay that. The 435 tons, balance, packed for boat sailing on February 1.

As a result, however, of my having rather stressed that it should be done, they have used the score of military necessity to postpone it. My understanding is that will not go forward, that 435 tons, until March, which will mean it will be spread over the first three months.

In addition to that, you remember they were pressing very hard for an undertaking as to what was going to be done for future months. My understanding is that is also being refused on the score of military necessity.

It does bring us back a little, however, to this point of arriving at what is the desirable and proper thing to do, which again brings us back to the study on the subject and back to my original question. Now I think I have achieved -- I made a strong point of this to achieve -- what you thought, to show a general spirit of cooperation from the other side.

- 4 -

I thought, some information that came to my hands, which I thought it would be interesting for you to have, knowing what you have done in the molybdenum situation and trying to -- the tonnage of International Nickel shipments to Russia in 1938 was, practically speaking, 16,000 tons. In 1939 it dropped to 2,720 tons.

HM, Jr: From where to where?

Mr. Purvis: Nickel to Russia. I was really trying to illustrate that something has been done in giving up on the side of the Nickel crowd and what it is they have done. They dropped to 2,700 tons in 1939 as a result of being asked to do so and no shipment has taken place since April, 1939.

HM, Jr: Do I understand that this plan went back as far as last April?

Mr. Purvis: I was very interested in that date of April and it looked to me -- though I have not verified it -- it came as a result of the occupation of Prague, when England first came to the conclusion that the game was up. I am theorizing there, but it looks to me so much like that date; I must verify that, but I think it must be right.

HM, Jr: That is very interesting.

Mr. Purvis: It is. I will verify that, because it is a little surmise on my part, when I heard the date, but I thought the figures might be interesting as showing there has been pressure on those interested to give up something.

In the case of Japan, the shipments in 1939 were 12,000 tons, which, in the light of the other figures I have, looks high.

HM, Jr: To Japan?

Mr. Purvis: Yes. And that again, however, as you know, tailed off completely towards the close of the year.

But I feel very anxious to put on the table such cards as are available. The last four months of the year, I understand that shrank very materially.

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Dr. White: Did you find out about the New Caledonia mine?

Mr. Purvis: I am sorry, not yet. I did not cable that. I put it on the airmail. It has been asked for. I could get it more quickly if you would like.

Dr. White: No. In view of what you are shipping from Canada, it is not important.

Mr. Purvis: I understand it's insignificant. I will cable them to give me a reply. I imagine the letter is in London. I will get that by cable.

Going on to tungsten. In the cable which we had before the theory was Turkey controlled 60%, which we all agreed was wrong. The reciphering department, after many efforts, says "we" can control - which means England and France, which is different. I also have by mail an inquiry outstanding whether the figure 60% was right because we all thought that over 50% was Chinese. I think 53% was given as the figure. However, that is an outstanding query. Then, in addition to that, the letter that I sent along giving information as to the position of that 7,000 tons of stock I received a cable much regretting that on further investigation they put over temporary what they had on hand December 6. It looks as though the information is wrong and will get to me as promptly as possible -- more accurate information.

HM, Jr: How did the Chinese divide it up?

Mr. Cochran: 4,500 tons of tungsten and 2,500 tons of antimony, but I am not sure of my figures.

HM, Jr: Could you check that over?

Dr. White: I don't have the breakdown.

HM, Jr: It was 7,500 tons.

Mr. Cochran: I can get the last figure.

(Mr. Cochran left the room.)

Mr. Purvis: Thank you very much because we have tried to clear it up. Apparently it isn't as easy as we thought when I forwarded that letter to you.

I think then we get back to certain of the queries -- whether there is any further development as to Chinese opposite tungsten as far as you are concerned.

HM, Jr: No.

Mr. Purvis: Nothing?

HM, Jr: No. I have not been able to go any further and I have nothing to report at this time. It does not mean we can't do anything.

Mr. Purvis: But for the moment.

HM, Jr: For the moment.

Mr. Purvis: And chrome, columbium and tantalum -- we talked about the possibility of action.

HM, Jr: Harry, have you people had a chance?

Dr. White: Which was the first one, chrome?

Mr. Purvis: Yes, chrome.

Dr. White: Now the British Empire controls 40% of the production of chrome. The Union of South Africa and British India.

Mr. Purvis: That checks with us.

Dr. White: Then you might also add the Philippine Islands, Cuba, which contain 5% each -- an additional 10% which I think we might have some measure of influence over.

Then there is Yugoslavia, Greece and Japan which are 5% each, and New Caladonia, which I take it you can do with -- that is an additional 5%. One large item that is beyond our control is U.S.S.R., producing 20% of the world production. Our Bureau of Mines does not indicate that we produce any but Procurement has recently accepted a bid from a mine in Alaska. Whether it's experimental or.....

Capt. Collins: That is an actual bid. Contract. And very high grade chrome.

Dr. White: This information we got from Procurement.

HM, Jr: Could you find out from the Governor of Alaska, Mr. Gruening?

Dr. White: We'll find out.

HM, Jr: But is it safe to say that as far as our 48 states are concerned we don't produce any chrome?

Dr. White: No records that the Bureau of Mines has, only a negligible quantity.

Capt. Collins: Negligible quantity; that's true.

HM, Jr: But let's find out about Alaska and where it is going.

(Mr. Cochran returns to the meeting.)

HM, Jr: This is from the Chinese Embassy, over 4,000 tons is tungsten and 3,000 is antimony which they claim -- which looks like the same figure you had, wasn't it?

Mr. Purvis: That's not far out. My figures, as we had it on December 8, 3,500 tons tungsten, 7,000 antimony, which were at Haiphong and ultimately taken by French groups. Further sources were stocks laying at Indo-China frontier 2,200 tons tungsten and 2,600 antimony. That totaled up to, well, about the 7,000 we talked about, those having been both under the same conditions. But we will get something more accurate on the end.

HM, Jr: What was the last metal?

Dr. White: Chrome. Germany is entirely dependent upon imports of this last year. She has gotten 1/3 of her imports from the Union of South Africa and 1/3 from Turkey; 10% from Greece -- all three.

Mr. Purvis: It's quite obvious they are preventing her from getting anything from South Africa because they say she is urgently trying to get it and they are trying to prevent it from going there, so I think we are pretty safe.

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Dr. White: I expect Russia's 20% is not enough to take care of Russia and Germany.

Mr. Purvis: Germany is very urgent according to my cables.

Dr. White: This would seem to indicate it so if you can take care of Turkey and Greece -- and chrome is a little more important than some of the other items.

Mr. Purvis: Agreed. That's what our people say. That's probably -- you don't want to say anything on the control possibilities. We are just exploring. We don't want to say anything more at this time.

HM, Jr: That's right.

Dr. White: On the other two items I take it you are probably familiar with the opinion they are not essential. They are newly discovered elements which are used, in alloys, in stainless steel, -- apparently makes steel a little more weldable but not as important as the other.

With that preliminary, the chief production now of tantalum is in Australia and the United States produces a small part of her domestic consumption and imports tantalum from Australia. Also imports certain raw materials from Algeria, out of which they make tantalite, so apparently Australia is the key for tantalum.

Mr. Purvis: That is quite a change because we thought the United States was the origin of that.

Dr. White: No. You see we import -- 1938 imports of tantalum was from 1,400 pounds to double practically within the year. Neither Germany, Japan or Russian have, as far as we know, any supplies of these metals, either tantalum or columbium. Now I was speaking of tantalum. Now, with regard to columbium, Algeria is the only large producer.

Mr. Purvis: May I ask this question? Though these are not as essential as the other alloys, we have been discussing, would you say for what producer worth they could be substituted?

- 9 -

Dr. White: There is a large area of substitution which all of these have some uses -- not all -- so it is worth while withholding these if you can but they are not as important as the others. They become more important if you.....

Mr. Purvis: That information becomes important because they cable me the United States was the source of those two alloys.

Dr. White: That's not our information, but this is a preliminary report, these are recent developments. We are still working on it and may get information which may serve to modify that information.

Mr. Purvis: I see.

Quartz crystal.

Dr. White: Quartz crystal, we are trying to get some information on. We import all or most of our needs but I am not sure. Quartz crystal has not been treated independently in any data brought to us from a statistical point of view and we are now getting permission from the Secretary of Commerce to enable us to examine some of the actual bills to see whether we can identify that item in our imports, and we are also thinking of contacting the trade.

Capt. Collins: The examination we made of that in connection with our bids indicated that there were available supplies of quartz crystal which may be used for strategic purposes in this country. Some in New York but that they were trinket type and not the type of quartz that we have to have for use in any sounding equipment.

HM, Jr: But we are pursuing that further?

Dr. White: This report on quartz crystal is in no sense complete. It's going on.

One other item, industrial diamonds -- the report is very preliminary -- produced chiefly in Brazil and South Africa, but apparently we have a good deal to do with the preparation of the material.

- 10 -

Mr. Purvis: Information comes to me that the nub of the problem is re-export from New York.

Dr. White: That's why, as I say, most of that is done in New York and we are pursuing that information as well, but on those two items we do not have a report beyond that very brief preliminary.

Mr. Purvis: I was able to get a little further on industrial diamonds because prior to the thing coming up here the Counsel General had been asked from the other side to try to talk to the trade to see what could be done to control the re-export of industrial diamonds and what I would like to do is put on the record the minutes of a meeting which he held with the trade on the 22nd of December which climaxed these preliminary discussions. Now, I have come across this by accident and the Counsel General, Mr. Haggerty, has promised to send me the background of these minutes which are not complete in themselves.

HM,Jr: Thank you very much.

Dr. White: We do produce a very little quantity in Arkansas.

Mr. Purvis: I think it comes down to export of cut diamonds from New York.

Dr. White: Probably a highly technical operation.

Mr. Purvis: I think there is the makings of a possible control there but it looks to me, with an article which can so easily be secreted, that nothing short of an export licensing system or some system that would enable one to have control, that would make it an offense to export it, would really put the necessary foundations under that situation. It is very important.

HM,Jr: Of course we have no such facilities.

Mr. Purvis: And it would be very difficult to put such facilities?

HM,Jr: Impossible.

Mr. Purvis: There is no other way?

- 11 -

Mr. Purvis: I wonder whether there would be any other way if the trade, represented by a few big people, of their having a chance to be influenced in any way?

HM, Jr: Well, I'll tell you, you make a note -- I have an idea which I may be able to give you later -- if I can find out who are the firms. If you can, tell me.

Dr. White: Would you like us to find out?

HM, Jr: Yes.

Mr. Purvis: I think the minutes will give you at least key information.

HM, Jr: If we can find out who the firms are -- possibility of our Customs working with your Customs and notifying them in advance. You see?

Mr. Purvis: That might be very good.

HM, Jr: If you knew they were in transit.

Mr. Purvis: That would be splendid. It's excellent as one of the possibilities. I will undertake to get from Haggerty the information on these firms and send it on to you.

Dr. White: What is your thought on this, Mr. Purvis, that something might be done with respect to their selling those industrial diamonds to somebody else?

Mr. Purvis: The minutes of these meetings visualize the voluntary imposition in the trade similar to what the nickel company does with nickel.

Dr. White: Does it seem possible?

Mr. Purvis: Apparently so. The only difficulty you might get into would be with the smaller man. But the Secretary's suggestion of possible customs.....

Dr. White: That would merely give you information in regard to the movements, but would it enable you in any way to control?

- 12 -

Mr. Purvis: It might help us. It might be the best way.

My next one on the list is copper. I reported the other day we had a record that the United States producers may have recently sold 60,000 tons to Russia; then had a further report after that Russia was becoming possibly a little alarmed about the extension of the moral embargo and it might be shipping to Mexico to Mazanillo and it is suggested two steamers, the Guyaquil and Gausdal may have cargoes.

Dr. White: The first one has and I think has already been loaded. Second one also. I have both names. I think they have left and had copper on them. Whether they have left or whether they are in the process of loading new shipments we will soon find out.

HM, Jr: But nothing we can do about it.

Mr. Purvis: Copper is a difficult one, as we said originally. Moral embargo could not go to that?

HM, Jr: I am afraid it would become immoral if you stretch it too far.

Mr. Purvis: Perfectly good answer.

HM, Jr: We are making it work overtime right now.

Dr. White: Of course the names of the ships on which these shipments are made are available to us.

Mr. Purvis: Would it be agreeable -- we would appreciate it if we could get information on the names of the ships.

HM, Jr: Let me think.

Mr. Purvis: One or two general questions, Mr. Secretary. Our people in the Commission -- its purchasing mission -- have pointed out that there are two or three specific problems that arise in connection with the Neutrality Act on which they would like to get State Department's rulings. I immediately said you give those to me. My channel of information is to you and I wondered whether we -- I didn't want our people to proceed with any other medium even though it is merely a question, in this case, of interpretation.

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One of them is the product called toleune. It is ordinarily piped on to a tanker and paid for on delivery to the tanker -- the exact point at which the title has passed and certificate passed is when the toleune gets into the middle of the pipe in the ship and that makes a disturbance of the existing channels of trade. What is our position? That is merely an illustration of three different kinds of points.

HM, Jr.: I'll tell you what I'll do. When we are through here I will ask you to talk for a few minutes with Huntington Cairns who passes on such things for us and he will advise you whether you should go directly to the State Department or whether we in the Treasury pass directly on it.

Mr. Purvis: But I am correct, am I not, in bringing up something of that kind here first?

HM, Jr.: This is all right. I don't know where the British mission begins and the British Embassy. I just don't know, but let me ask Huntington Cairns. I don't know whether that ought to go through your Embassy to the State Department. I don't know. It may be purely a Treasury matter. If it is, it's all right for you to bring it to us but if it is something that has to go through the State Department, my curb-stone opinion is it ought to go through the Embassy to State.

Mr. Purvis: I think so. In that case I would go to the Embassy and ask them to take it up with State.

I feel almost ashamed about the length of this list. When we were here before you were good enough to say on the Consolidated Aircraft situation you might be willing to let us know the terms of your arrangement with them.

HM, Jr.: Look to your right.

Capt. Collins: I have done nothing with it, sir.

HM, Jr.: That is for you.

Capt. Collins: Yes, sir.

HM, Jr.: If you ask Captain Collins maybe he will make an appointment to see you. That's definitely in Collin's hands.

- 14 -

Mr. Purvis: There was one thing we were talking of with Captain Collins this morning that I thought we could bring up in a very general way. We are troubled naturally by quite a number of individuals who claim to be acting for the French or British. One firm which appears to be getting into a rather large-scale operation, rather carefully thought out -- United States Engineering and Sales Company. We are preparing a memorandum which we were wondering if there is any way in which real misrepresentation -- whether there is any channel we should go to or you could think of.

HM, Jr: They are misrepresenting?

Mr. Purvis: I think we will be able to have a clear case of misrepresentation.

HM, Jr: I think that's the Justice Department.

Capt. Collins: They are using the mails.

HM, Jr: Justice.

Capt. Collins: Justice would investigate it first, I think.

HM, Jr: What I would suggest again is, to make it easy, when you are ready we will -- if you will send it here I will see what is the proper department to advise you. I think it is the Department of Justice. To save you time -- I imagine that they go back to the United States Attorney in New York, Mr. Cahill, but I will find out.

Mr. Purvis: Thank you. Because where they use the mail there is a chance that something might be done?

HM, Jr: Oh, definitely.

Mr. Purvis: The only other thing I have to say is Captain Collins has been helping us on aluminum and we are gradually getting him information in enabling him to do it. That is enormously important and we will soon be at a stage where we will be able to move. It takes us some time to get our information together.

HM, Jr: We are meeting tomorrow on planes. Are you in on that?

- 15 -

Mr. Purvis: I have seen -- with Mr. Plevan and Col. Greenley we saw Sloan on Sunday. The situation which has developed was -- of course I have known him for a long time -- on Tuesday he very guardedly said, "I have had the preliminary contacts you have authorized me to have with the two people who could help and my belief is that despite the magnitude of the thing" -- as I told you it was a terribly difficult thing to do -- but by Thursday we will be able to move as a unit, the three of us, in presenting to you means by which it can be done. I telephoned that to Captain Collins. He said, "I am much more hopeful than I expected to be as to the possibilities of solving the actual production because I think on the subcontracting basis we can do that."

HM, Jr: You said that?

Mr. Purvis: Sloan of the General Motors. They come in as the Allison engine.

HM, Jr: Where is Gordon Rentschler in this picture?

Mr. Bloch-Laine: He's National City. I did go to see Leroy-Beaulieu. I understand Sloan told Gordon Rentschler of his talk and the man in charge of the other.

Mr. Purvis: I have not known Gordon Rentschler in the matter and what Sloan said was, "I have been in contact with the two other possibilities and I think by Thursday we will be in a position to put/before the people.
it

Of course the people who saw him were Plevan, Greenley and myself and he has heard the production problem, the question of the production problem.

Mr. Bloch-Laine: As I understand, Gordon Rentschler asked for an appointment with Leroy-Beaulieu. On the contrary Rentschler knew the whole story.

Mr. Purvis: Rentschler is the one Sloan knows best in Pratt-Whitney.

HM, Jr: I think he has one brother in Pratt-Whitney and one brother in some other tool company.

Capt. Collins: Niles, Bement and Pond.

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Mr. Purvis: That might account for it because I understand the machine tool question was very much in Sloan's mind.

HM, Jr: He spoke to me yesterday and said he was doing everything he could in the machine tool business and seemed to know what Sloan was doing.

Mr. Purvis: Sloan said, "With whom may I talk?" And we said with the two concerns most interested.

HM, Jr: He might have used Rentschler because of his connection with the two companies and the tool industries.

Mr. Purvis: We impressed upon Mr. Sloan the importance, from the British and French viewpoint, the matter of secrecy.

HM, Jr: You saw it in the papers that you are here for 10,000 planes. It was all in the papers. The New York Times had a very interesting article by their correspondent in Germany talking about the trouble you are having getting your airplanes here.

Mr. Purvis: Isn't that amazing! Of course, there is only one advantage comes from breaks of that kind, that after a time they are no longer news.

HM, Jr: That's right. Does that cover your list?

Mr. Purvis: I have question number one. I won't return to it.

HM, Jr: Have you anything you would like to ask?

Mr. Bloch-Laine: No, thank you, Mr. Secretary.

HM, Jr: We will get Huntington Cairns in here.

Mr. Purvis: Thank you very much. It would perhaps be fairer to him if I handed a copy of this memorandum to him with the three main queries here.

HM, Jr: He follows this whole Neutrality thing for me and he's the contact man with Berle or the Maritime Commission and he can say this is a Treasury matter or it ought to go either here or there. I don't know, but he may be the man who is holding it up. I don't know and then if you don't mind, go back to his office.

- 17 -

Mr. Purvis: Thank you very much.

HM, Jr: Are you buying the foodstuffs too? Is your Commission buying.....

Mr. Purvis: We are not.

Mr. Bloch-Laine: We bought a few beans and got a cable the other day -- it was a sort of circular calling back all the missions that had been sent to buy foodstuffs, which would seem to indicate they had given up the plans.

(Mr. Huntington Cairns comes in.)

HM, Jr: If you will take them back to your office -- it's a question where oil leaves our ships and goes on their ships and get a certificate. What I was saying to Mr. Purvis -- head of the Allies Purchasing Mission -- on a matter like that if it is Treasury we will handle it. If it is some other department, you will indicate it. If it is State, that would have to go through the Embassy.

Mr. Huntington Cairns: It may be Commerce.

HM, Jr: But you tell them before they leave who is the person.

- ooOoo -

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris

NO.: 45

DATE: January 10, 1940

STRICTLY CONFIDENTIAL FOR THE SECRETARY
AND THE SECRETARY OF THE TREASURY

Reference is made to your telegram no. 1574 of December 29, 1939, noon.

From personal sources in London I have been hearing during the last week that the British Government has been requested by the United States Treasury Department to indicate the approximate proportion in which the British Government will use gold and securities in making payments in the United States; also that it has been intimated to the British Government by the United States Treasury Department that it would be preferred by the United States Government that the British Government use gold to as small an extent as possible in making such payments and that payments be made by realizing on securities so far as possible.

I have also heard from my sources in London that at first it had been the British Government's inclination to answer that payments in the United States would be made in the approximate proportion of 40 percent

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in dollars realized on securities and 60 percent in gold. However, it was decided, after consultation with French authorities, that the British Government would reply that its policy had not yet been determined and that it would point out that it was likely that the value of gold would quickly disappear if the position should be taken by the United States Government at this time that it did not wish to acquire gold.

I paid no attention to these reports until last evening when they were repeated to me by Paul Reynaud. Reynaud went on to say that in his opinion the United States Government would be very foolish if it appeared at the present time unwilling to accept gold. The future of gold would be disastrously affected if there were the slightest indication that in a time of emergency the United States Government did not wish to receive gold. The maintenance of gold as the means for settling international balances was clearly in our interest since we held so much gold.

It was added by Reynaud that before the close of the present war France and England's gold stocks would be completely exhausted if it should prove impossible for the United States Government to work out some exceptional plan for taking care of the situation. In such an event, the

-3-

the setting-up of a monetary bloc by the British and French completely detached from gold would be advocated by many persons. He said it was his personal opinion that gold serves better than any other metal for the settlement of international balances. He therefore thought that in the long run gold would again be used to settle international balances even though it might be temporarily eclipsed on account of its concentration in the hands of the United States Government.

Reynaud inquired as to whether or not I had any information concerning the questions which had been put to the British Government by the United States Treasury Department. My answer was that I had no official information of any kind regarding the matter. The personal reports which I had received from London (but which had not come from the United States Embassy there) were in conformity with the information which had been given me by him. I added that since I had no information or instructions from my Government, I wondered whether the receiving of unwanted gold might not be causing less concern to the United States Treasury than the disorderly and too-rapid selling of securities in the American market.

Reynaud stated that he thought a message regarding
this

-4-

this question was being brought to me by Leroy-Beaulieu. However, the latter is not expected to arrive in Paris until the 17th at the earliest.

It was added by Reynaud that in the near future he would like to talk about this matter with me again. I shall therefore appreciate any information or instructions which you may care to send me.

(END OF MESSAGE)

BULLITT

ALL INFORMATION CONTAINED
HEREIN IS UNCLASSIFIED

DATE 11-15-80 BY SP-12

TO THE SECRETARY
DEPARTMENT OF STATE
WASHINGTON, D.C. 20520

EA:EB



DEPARTMENT OF STATE
WASHINGTON

January 11, 1940.

The Secretary of State presents his compliments to the Honorable the Secretary of the Treasury and encloses a copy of a strictly confidential telegram from the American Embassy at Paris, no. 45 of January 10, 1940, having reference to financial matters.

Enclosure:

From Paris, no. 45,
January 10, 1940
(paraphrase).

RECEIVED
TREASURY DEPARTMENT

1940 JAN 11 PM 12 15

OFFICE OF THE
TECHNICAL ASSISTANT
TO THE SECRETARY

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: January 10, 1940, 6 p.m.

NO.: 49

FROM MATTHEWS.

FOR THE TREASURY.

I visited Couve de Murville at the Ministry of Finance at noon. He said that matters were going along quite satisfactorily internally. For the month of December subscriptions to armament bonds reached a total of more than 6,000,000,000 francs. Subscriptions are expected to go as high as 9,000,000,000 francs for the month of January - though investments by banks represent a substantial proportion of this, subscriptions by private individuals and business have proved encouraging too. The Government has had more satisfactory tax returns, and the capital circuit is functioning very well.

Couve de Murville said that in the near future no long term loan is contemplated. He agreed that to resort to one now would be "foolish".

So far the last statement of operations of the Treasury which has been published was for the month of August - reference telegram No. 2912 of December 6 from the Embassy, and despatch No. 5443 of December 14. I asked my friend whether they would publish later Treasury statements - I had been told by Norman Young that he did not think this would be done. Couve said that they had not yet reached

a decision on this but that in any event they have not yet gotten ready the figures for September.

He said with regard to payments in the United States that around \$45,000,000 would be the actual outgo for the month of January, and that recently not so many new orders had been placed requiring early payment, so that for the next two or three months he anticipated some little slackening from the earlier heavier figures. After that time it would be difficult, he said, to anticipate at what rate it would go up, as a great deal depended on the rhythm and form of the war, and so on.

Couve de Murville volunteered the information that word had come to him that the United States and Great Britain had had "a little friction" over "the sudden cessation in December of British sales of American securities", and the question of the respective proportion of allied payments to be made through gold or through sales of securities by Great Britain. As far as France is concerned, he said, it is their plan to make payments in gold, for at the present time they have not thought of requisitioning private holdings of foreign securities. He said that the Government is loath to take any steps along this line. He said that they are still continuing to get dribbles of repatriated capital, including dollars, even though the volume is small; the French Government has no wish to end this capital repatriation.

- 3 -

References: telegrams from the Embassy, Nos. 2765 of November 15 and 2912 of December 6: Through the declarations required for January 15 and February 1 for those mobilized, France is just on the point of taking "inventory" of such holdings. Therefore the Government would not want to make any move in this direction which might create any sudden fears or disturb the favorable financial atmosphere prevailing just now.

We asked Couve de Murville how the financial accord between Great Britain and France is functioning. Like Norman Young - reference: telegram No. 18 of January 5 from the Embassy - he indicated that as yet it was too early to form any seasoned opinion as to its operation. He could not make any guess as to whether in the long run British franc requirements would be less than French sterling needs - reference: telegram No. 23 of January 8 from the Embassy; please compare Rist's view given therein - the British were spending more in francs than the French in sterling at the present moment. It would be very difficult to formulate any estimates for the long run, as he said so much depended on the nature and duration of the war, consumption of stocks existing now, and completely unknown factors, of which price levels is an important one.

The

- 4 -

The weak point of the financial accord between Great Britain and France, he reiterated, was this question of price levels. He said France is anxious to get down to realities about it with the British. I made the remark that it seemed this point was touched on yesterday by Chamberlain even though it had been in a somewhat timid way; he said that was so, but that the British fear their trade unions too much, although they could cite the example of the French syndicates which without complaint has accepted the ceiling on wages. To date he agreed the French have had remarkable success in keeping prices down. However, he said it was inevitable that prices would rise, and the rate and timing would depend on how much had to be purchased abroad; they were living on pre-war stocks to a great extent just now - this is a view similar to Pennachio's, reference: telegram No. 3056 of December 29 from the Embassy.

Couve de Murville seemed to be quite satisfied with the results of recent trade and clearing negotiations. He said, like Rist, that the French had been successful in "resisting" the tendency of all the neutrals wanting to export in dollars. Negotiations with the Greek Government were for the most part for a clearing agreement, he said, and did not have primary rank. In February France will

- 5 -

undertake negotiations with Italy, and Couve said that the French would not give dollars to Italy; he quite frankly stated - as I have emphasized in telegrams sent previously - that at least as far as the French are concerned, the main purpose of the financial accord between Great Britain and France was to preserve the maximum quantity of dollars and gold for purchases of only such American goods as are vital to carry on the war and which cannot be feasibly purchased in other countries.

END SECTIONS ONE TO SIX, INCLUSIVE.

BULLITT.

MM

GRAY

Paris

Dated January 10, 1940

Rec'd. 5:42pm.

Secretary of State

Washington, D.C.

49, January 10, 6pm. (SECTION SEVEN).

Instructions were published in today's JOURNAL OFFICIEL setting forth the conditions of application of the decree published in the JOURNAL OFFICIEL of November 17, 1939 (telegram No. 2779, November 17, 7pm) relating to the collection of the special national salaries tax the general rate of which is 5% with 15% for men between 18 and 49 not serving with the armed forces. Detailed information relating to the latter is given in the form of an annex to the instructions. Exemptions notably include those who have served their time in the army and navy, physical inaptitude, fathers of 6 children, war veterans, et cetera. Foreigners to be relieved of the 15% tax rate must fulfill the following conditions:

BULLITT

BK
HPL

JT

GRAY

PARIS

Dated January 10, 1940

Rec'd 6:05 p.m.

Secretary of State,
Washington.

49, January 10, 6 p.m. (SECTION EIGHT)

"(A) Be in receipt of pay for active service in the French Army or in an allied army.

(B) Be of an age where Frenchmen are not yet subject to military obligations or have been relieved therefrom.

(C) Be in receipt of a military disability pension or of a pension as civil victim of the war, in virtue of French laws or the laws of an allied or ex-allied country.

(D) Be former volunteers or have voluntarily reenlisted in the French Army or an ex-allied army.

(E) Be the father of six children.

(F) Be of an age at which Frenchman liable to mobilization are returned to their homes because of demobilization of their class or because of family charges.

(G) Be possessors of veterans cards of an allied or ex-allied country".

All the foregoing except the last are worded similarly to the exemptions provided for Frenchman.

BULLITT

BK:NPL

MM

GRAY

Paris

Dated January 10, 1940

Rec'd. 5:10pm.

Secretary of State

Washington, D.C.

49, January 10, 6pm. (SECTION NINE).

The local press has recently been reporting occasional arrests of dealers on the "black bourse" in Paris and 21 are stated to have been taken in yesterday. Reportedly the largest "haul" yet made was one of 1,500,000 francs of foreign currencies. The existence of such dealers in view of the small volume of their transactions as I previously reported have not as yet aroused any anxiety.

Further selling took place on the securities market today and losses were general. It was influenced largely by a 10 franc drop in the quotation of the 1937 dollar exchange guaranty rents issue. Apparently speculators found that the coupon rate is below that which the market had anticipated. Other rents issues were only fractionally lower.

(END OF MESSAGE).

BULLITT

BK
NPL
 600 AM 11 22
 RECEIVED
 FOREIGN
 OFFICE



GENERAL COUNSEL
TREASURY DEPARTMENT
WASHINGTON

183

January 10, 1940

MEMORANDUM FOR THE SECRETARY:

Mr. Purvis raised three questions under the Neutrality Act. The first related to an extension of credit and belongs in the State Department. The second involved the transfer of title to goods and belongs in the Treasury. The third involved registration under the Munitions Control Act and belongs in the State Department.

Mr. Purvis did not have possession of sufficient facts to discuss the second problem with us, and he is sending one of his assistants down to explore the matter further. It is possible that the first problem may be eliminated with the ironing out of the difficulties under the second question. Mr. Purvis will, therefore, not discuss the first problem with the State Department until his assistant has discussed the second problem with us. I arranged for him to see Mr. Green in the State Department with respect to the third question.

Huntington Cairns

January 10, 1940

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(Signed) Huntington Cairns

HC/ep

CHUNGKING via N. R.

Dated January 10, 1940

Rec'd 3:20 a.m.

Secretary of State,

Washington.

19, January 10, 11 a.m.

Following from Yunnanfu.

"January 9, 10 a.m. French officials here state that the Lace Bridge at kilometre 83 was hit during the January 7 bombing rendering the bridge impassible for trains. Two uprights to one section of the bridge were twisted and the foundations badly shaken. Eighty meters of rails were torn out.

The sources also state that while all freight and direct passenger traffic with Yunnanfu is interrupted the transfer of passengers and small baggage across the two major breaks can still be effected. Perkins".

Repeated to Peiping, Shanghai, Hong Kong. Shanghai please repeat to Tokyo.

PECK

RR

C A B L E

From: Treasury Attache Nicholson
Shanghai, China.

Date: January 10, 1940

For Secretary of the Treasury:

Current situation for week ending January 10, 1940. Exchange market fluctuated good deal during week with net result a slight rise. 7000 tons wheat were ordered abroad during week but exchange therefore has been settled previously. Cotton imports continued a predominant factor. Stock exchange maintained previous high volume with still further increases in price level particularly for rubber shares. All daily records for both volume and price were broken on Monday, January 8. Real Estate turnover in Shanghai in 1939 was yuan \$56,000,000 or largest since 1931, December being slightly the largest month of year. Local currency values in most districts are still low in comparison with 1937 in spite of subsequent inflation. One large apartment house recently sold for the equivalent of less in U.S. dollars than the imported fittings cost when it was built six years ago. Trade of Japan in 1939 compared with 1938 shows imports up 10%, exports up 35% and total trade up 22% with a favorable balance of 762,000,000 yen. This result however is due entirely to business within the yen blok as trade with other areas shows in unfavorable balance of 416,000,000 yen. Bank of Japan loans outstanding at end of 1939 were about 1,000,000 yen embodying in increase of about 100% during the year. Public bond issues during year aggregated 5,250,000,000 yen. Note circulation of local Hun Shing Bank increased from about \$4,000,000 at end of November to about \$5,000,000 at end of December. During year service on most loans was defaulted.

NICHOLSON

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Chungking, China.

DATE: January 10, 1940, 1 p.m.

NO.: 20

The following information is confidential:

Yesterday I was told by the British Ambassador that the Chinese, through him, are seeking financial credits from the British Government. The Chinese have informed the Ambassador that they are sanguine of obtaining additional credits from the United States to the amount of 75,000,000 dollars before the end of January, exports of tin and tungsten being the security.

I was asked whether I knew anything of the above, and I replied that the Embassy here had not received any information about negotiations in the United States for further credits or assistance in any other form. However, I said the American Government adhered to its position, announced in times past, on the general attitude toward the hostilities in China. When I told him the foregoing the British Ambassador expressed such relief and pleasure that I inferred he was somewhat anxious as to the British Government's own position; the Ambassador himself is very sympathetic toward the cause of China, as the Department knows.

PECK.

EA:LWW

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2211 THIRTIETH STREET
WASHINGTON, D. C.

Jan 10, 1940
12.01 P.M.

Finland I believe the
reason Hull does not want
anything done is because
he fears that Finland loan
might hold up his xx
trade treaties as both will
have to go thru Ways + Means.
Of course this is my
surmise.

I will see Houghton myself
and see where matter stands.

Prepared by: Mr. Murphy
Mr. Lindow
Mr. Tickton
Mr. Haas

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TREASURY DEPARTMENT

CONFIDENTIAL

INTER OFFICE COMMUNICATION

DATE January 10, 1940

TO Secretary Morgenthau
 FROM Mr. Haas *HA*
 Subject: Developments in the High-Grade Security Markets

SUMMARY

- (1) At the close on Tuesday, January 9, the prices of all long-term high-grade domestic bonds were at new highs (low yields as measured by the averages) for the recovery period (Charts I and II). The prices of long-term municipal bonds were not only at a recovery high, as measured by the Dow-Jones average of yields, but were also at an all-time high. Municipals have done better than Treasury's on the recovery movement and the spread between the average yields of these bonds has narrowed (Chart II).
- (2) Treasury bills have been undergoing important shifts in ownership principally because of a demand for tax purposes, investors other than banks having acquired about \$130 millions since December 6 (Chart III). During the same period, New York City banks have disposed of \$271 millions of bills, on net balance (Chart IV). Banks in Chicago, on the other hand, increased their bill holdings by \$172 millions.
- (3) During the last three weeks the Treasury has sold \$10 millions of securities held by Government accounts, and the Federal Reserve banks have sold \$19 millions of the Governments held in their open-market account. With the exception of a few weeks during last August the Reserve portfolio is now at its lowest level since the first part of 1937 (Chart V).
- (4) As a result of recent financing operations, the composition by maturity classes of direct and guaranteed public debt has been altered significantly. At the year-end, the greater part of the open-market debt was fairly equally divided between the 1-5 year, 5-10 year, and 10-15 year maturity classes (Charts VI and VII). The amount of obligations maturing within five years has declined by more than \$2 billions since the middle of 1934.
- (5) British 2-1/2 percent consols have been rising since Wednesday, January 3 (Chart VIII). The closing price on Tuesday, January 9, was the highest since December 1938.

Secretary Morgenthau - 2

I. High-Grade Bonds at Post-Crisis Highs

At the close on Tuesday, January 9, the prices of all long-term high-grade domestic bonds were at new highs (low yields as measured by the averages used in Charts I and II), for the recovery period. The average yield of all long-term Treasury bonds stood at 2.28 percent at the close -- down 51 basis points from the September high yield. This yield compares with the all-time record low yield of 2.07 percent reached on June 5, 1939, and with the yield of 2.19 percent reached on August 19, just prior to the outbreak-of-war crisis.

The prices of municipal bonds are not only at a recovery high, as measured by the Dow-Jones average yield of twenty 20-year municipal bonds, but are also at an all-time high. At the close on Saturday, January 6, the last date for which the average has been calculated, the yield stood at 2.52 percent -- down 73 basis points from the September high. Long-term municipals, it is apparent, have done somewhat better than Treasury's on the recovery movement, and, accordingly, the spread between the average yields of these bonds has narrowed (Chart II). This better performance has been due, in part, to the rather restricted supply of new municipals available in the market. The volume of new offerings has been relatively low during recent weeks, and the schedule ahead, at least for the remainder of January, shows no important issues ready for the market.

The prices of high-grade corporate bonds, as shown by our average of the yields of these issues (Chart I) are still slightly lower (yields higher) than their record level reached last summer shortly before the crisis developed. At the close on Tuesday, January 9, our average of the yield of high-grade corporate bonds stood at 2.80 percent. This compares with the summer record reached August 3 of 2.72 percent. Many high-grade corporate bonds -- those included in Moody's Aaa average for example -- have done better in relation to their previous highs than those included in our average, however. Thus, Moody's index broke through its summer high on Thursday, January 5. This different behavior can be explained, however, by the fact that Moody's average did not reflect the full extent of the rise last summer. This was because it was heavily weighted by bonds which were selling well above their call prices, and were consequently unable to rise as much as those not so fettered. These bonds are still in Moody's average, but the market is evidently giving somewhat less weight to the possibility of their call than at that time.

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The corporate market took in its stride the public offering on Monday, January 8, of \$30 millions of American Gas and Electric Company debentures. The new issues were taken up quickly, and went to premiums of two points over the offering prices in early over-the-counter trading. The flotation consisted of three issues of debentures maturing in ten, twenty, and thirty years, and priced to yield 2.47 percent, 3.26 percent, and 3.56 percent, respectively. In addition to the debentures, the company brought \$35 millions of preferred stock to the market. It was offered to holders of the outstanding preferred stock under an exchange arrangement.

II. Treasury Bills

The last two issues of Treasury bills have been sold at prices in excess of par, which means a negative rate of interest. The principal explanation for this phenomenon is that taxpayers have been getting ready for approaching property tax dates in certain States. Inasmuch as United States securities are exempt from such taxes, it is cheaper to pay a small premium for Treasury bills than pay the tax on taxable assets.

Primarily as a result of this tax stimulus, important shifts in the holdings of Treasury bills have been taking place in recent weeks. On December 6, when the last of the Federal Reserve bill holdings had run off, the outstanding supply of bills was equally divided between weekly reporting member banks and "all other" holders. Since then, "all others" have acquired about \$130 millions of the holdings of reporting banks (Chart III). Presumably, the purchasers have been corporations and individuals rather than non-reporting banks, inasmuch as such banks have in the past held only negligible amounts of Treasury bills.

Meanwhile, there have been large shifts among the banks included in the reporting group. New York City banks have disposed of \$271 millions of bills on net balance since December 6 (Chart IV). Banks outside of New York and Chicago have disposed of \$32 millions. Banks in Chicago, where the tax date is April 1, on the other hand, have increased their bill holdings by \$172 millions.

During the calendar year 1939, the privately held marketable supply of bills increased as follows:

	(Millions of dollars)
Increase in gross amount outstanding	149
Decrease in Federal Reserve holdings	<u>566</u>
Total	715
This amount was absorbed by holders as follows:	
Weekly reporting member banks	309
All others	<u>406</u>
Total	715

The bill holdings of "all others", as shown in Chart III, are now as high as on June 30, 1937, the highest previous level shown in the Chart. The privately held marketable supply of bills, however, is \$225 millions smaller now than at that time.

III. Official Operations in the Market

During the market rise of the last three weeks, the Treasury has sold \$10 millions of securities held by Government accounts and the Federal Reserve banks have sold \$19 millions of securities held in their open-market account. With the exception of a few weeks during last August immediately preceding the outbreak-of-war crisis, this brings the Federal Reserve portfolio to its lowest level since the first part of 1937 (Chart V). Fifty-four percent of the portfolio as now constituted consists of bonds and the remainder consists of notes. The shortest maturity now held is the note issue due June 15, 1940, of which the account holds \$137 millions. No Treasury bills have been held in the account since the first week in December.

IV. Composition of the Public Debt by Maturity Classes

The refunding of the March notes removed the largest single maturity of a United States Government obligation until 1945. As a result of this operation, and other financing operations conducted in the months of November and December, the composition by maturity classes of the direct and guaranteed interest-bearing public debt has been altered significantly. These alterations

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are brought out in Charts VI and VII, which classify the securities making up the public debt according to the number of years to maturity. The left-hand grid of each chart is based on data for the end of each fiscal year from 1930 to 1939. The right-hand grid is based on data for the end of each month from June 30, 1936 to December 31, 1939. The classification is entirely according to final maturity, irrespective of first call date.

On December 31, 1939, the greater part of the open-market direct and guaranteed debt was fairly equally divided between the 1-5 year, 5-10 year, and 10-15 year maturity classes. These classes accounted for 23 percent, 25 percent, and 26 percent, respectively, of the total outstanding obligations, as shown in Chart VII. This chart is constructed on the same basis as Chart VI, but for purposes of analysis, only open-market issues have been included.

Changes in the composition of the debt by maturity classes are brought about not only by the maturity of outstanding issues and the addition of new issues, but also by the mere passage of time. All of the debt now outstanding will, of course, eventually move into the under-one-year class.

One of the more striking developments brought out by the two charts is the decline in recent years in the amount of direct and guaranteed Government securities maturing within five years. From June 30, 1934 to June 30, 1939, the privately held marketable supply of direct and guaranteed obligations increased by about \$11 billions. The amount of obligations maturing within five years, however, declined by more than \$2 billions in this period.

V. Foreign Security Markets

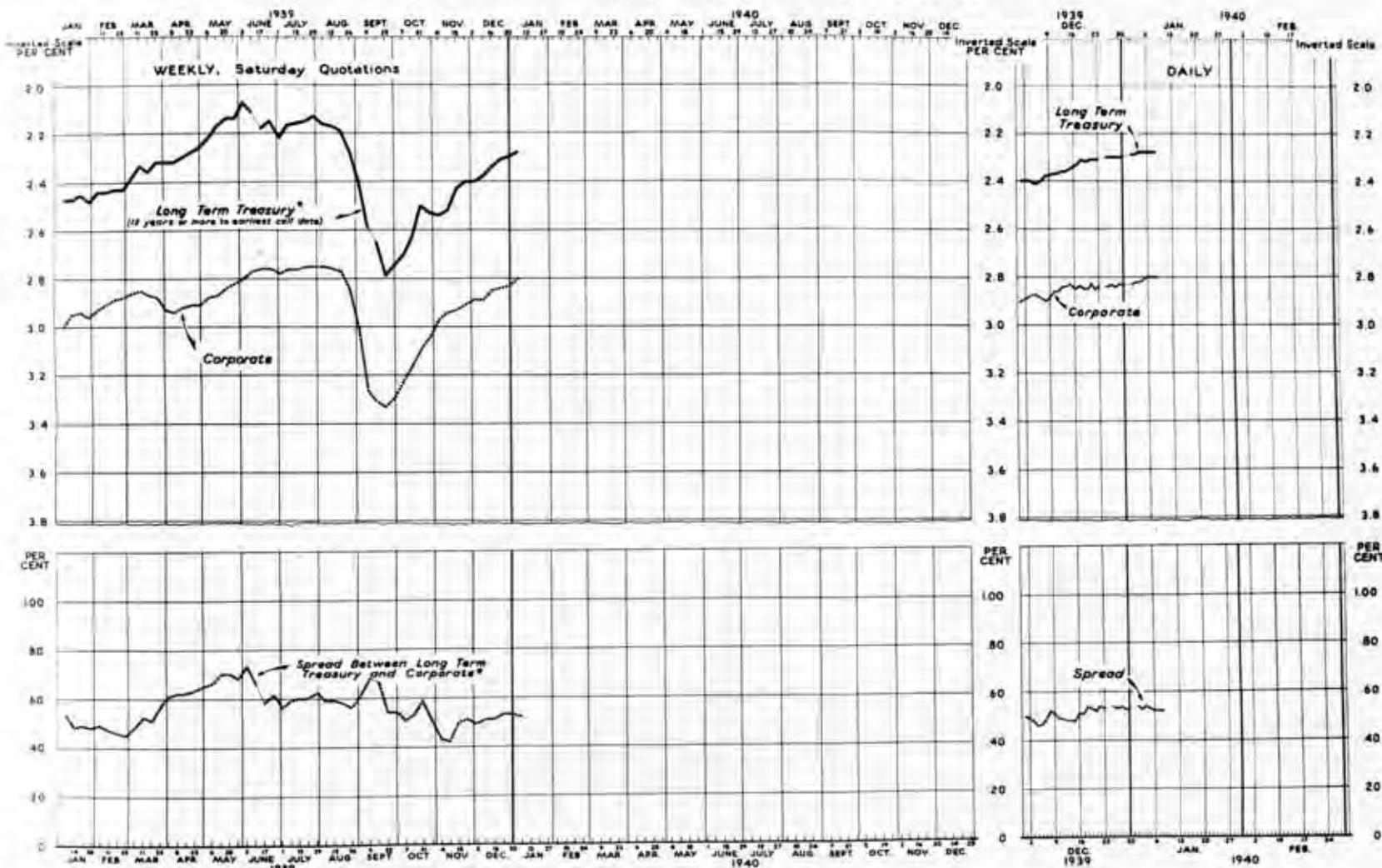
British 2-1/2 percent consols, after having remained quiet for several weeks, started to rise on Wednesday, January 3. The rally continued over the week-end, and at the close on Tuesday, January 9, consols were up nearly 3 points over their price a week before. The closing price of 71-1/4 (yield 3.52 percent) on Tuesday was the highest since December 1938 (Chart VIII).

French 3 percent rentes reached a recovery high of 77.10 on Wednesday, January 3. They closed at 75.90 on Tuesday, January 9, to yield 3.95 percent.

Attachments

Chart I

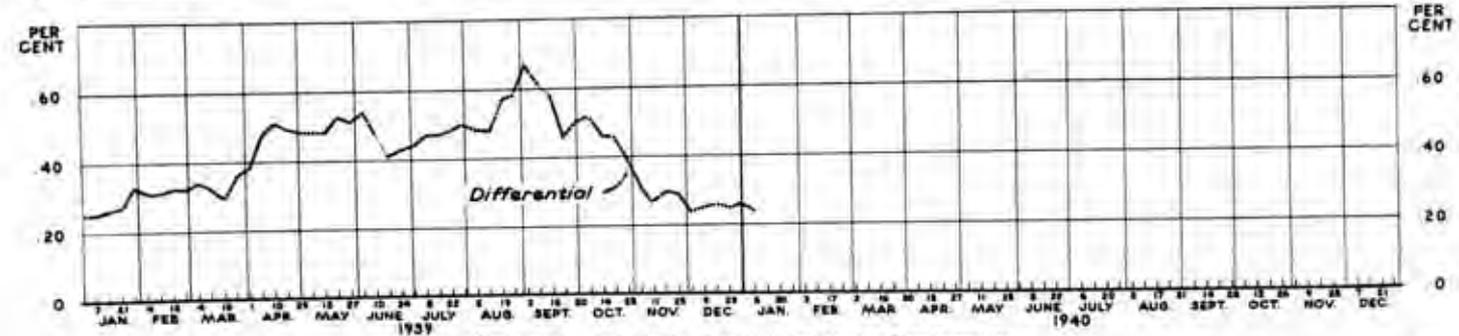
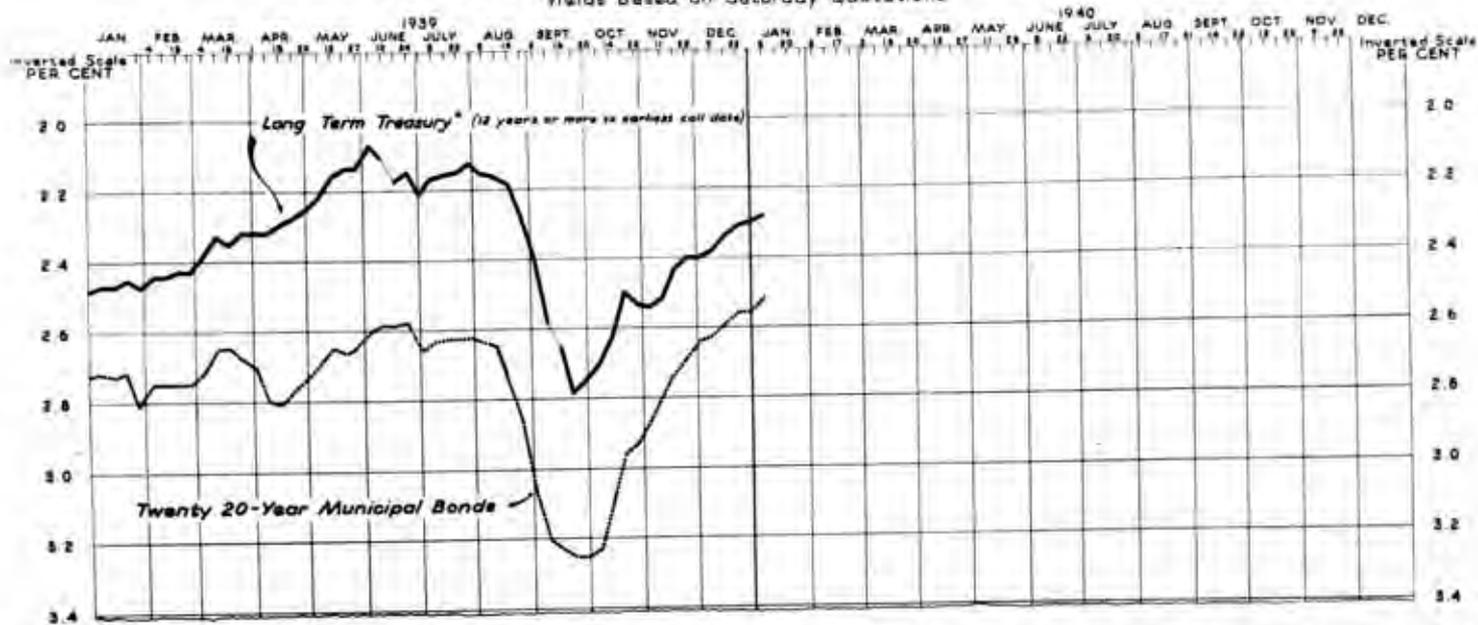
COMPARATIVE YIELDS OF AVERAGE OF ALL LONG TERM U S TREASURY AND AVERAGE OF HIGH GRADE CORPORATE BONDS



Source: U.S. Department of the Treasury, Bureau of Economic Warfare and Finance

COMPARATIVE YIELDS OF AVERAGE OF ALL LONG TERM U S TREASURY AND DOW-JONES AVERAGE OF MUNICIPAL BONDS

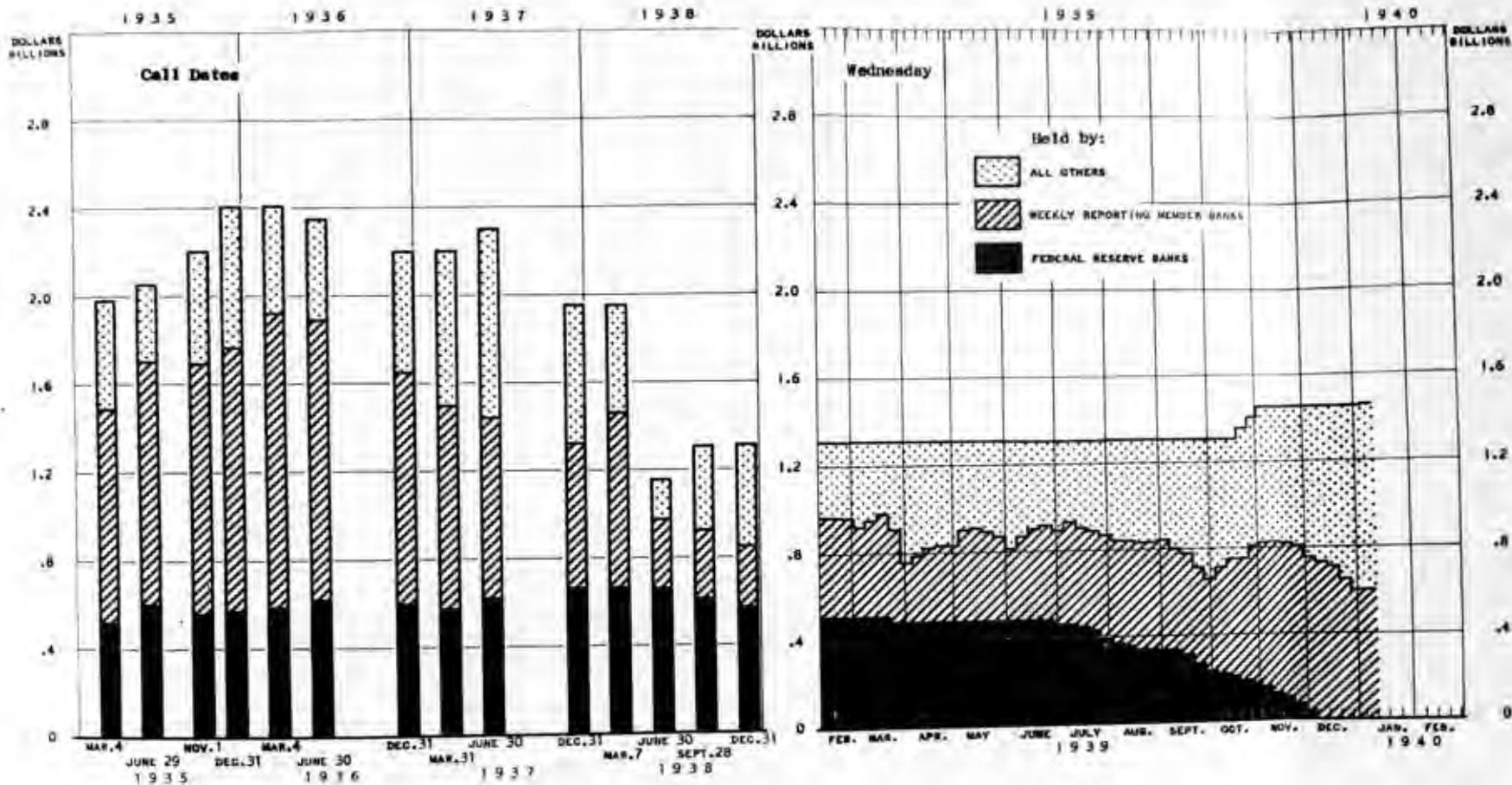
Yields Based on Saturday Quotations



*Break in line indicates change in composition of Long Term Treasury average.

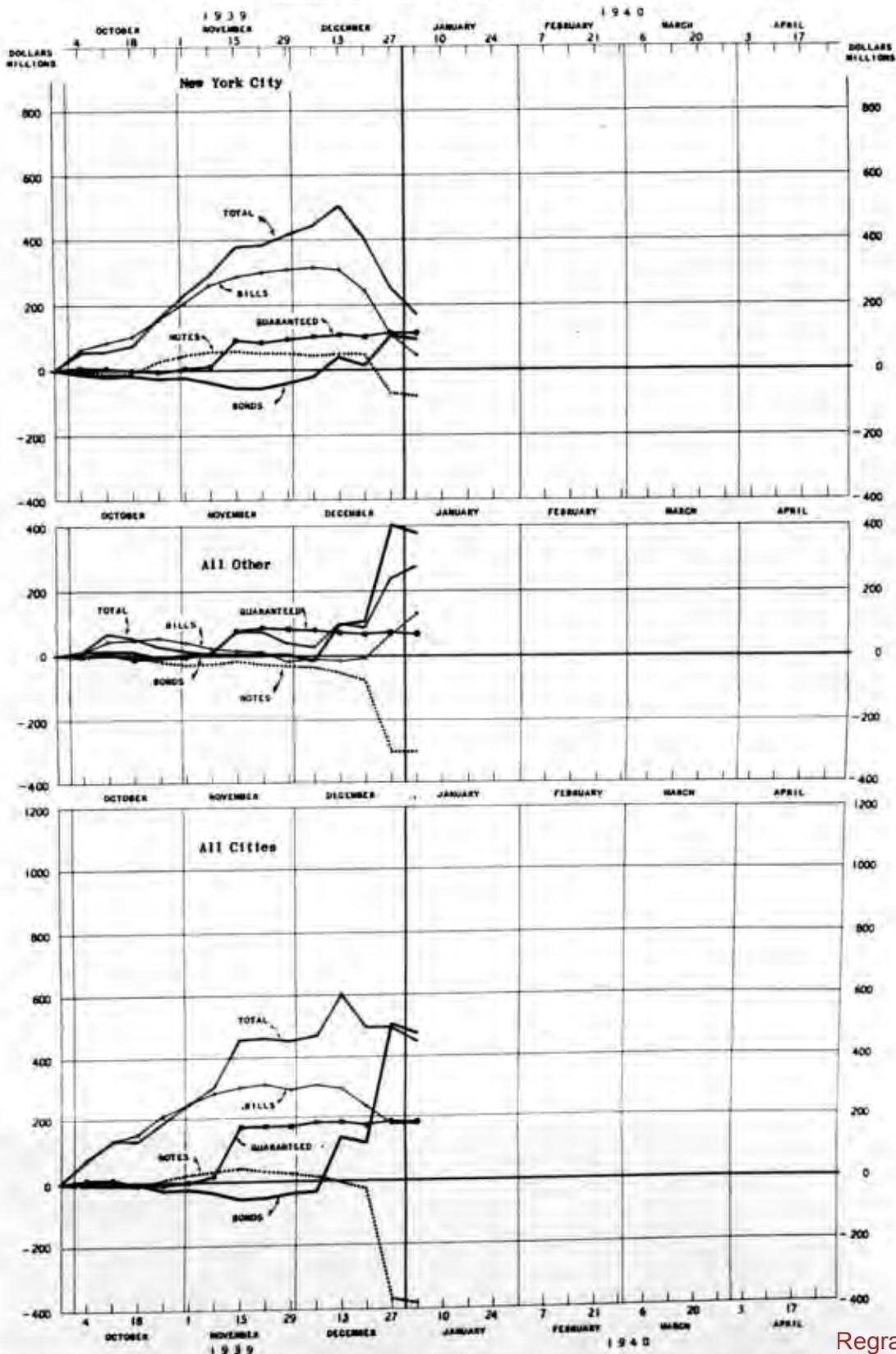
Chart III

DISTRIBUTION OF OWNERSHIP OF TREASURY BILLS

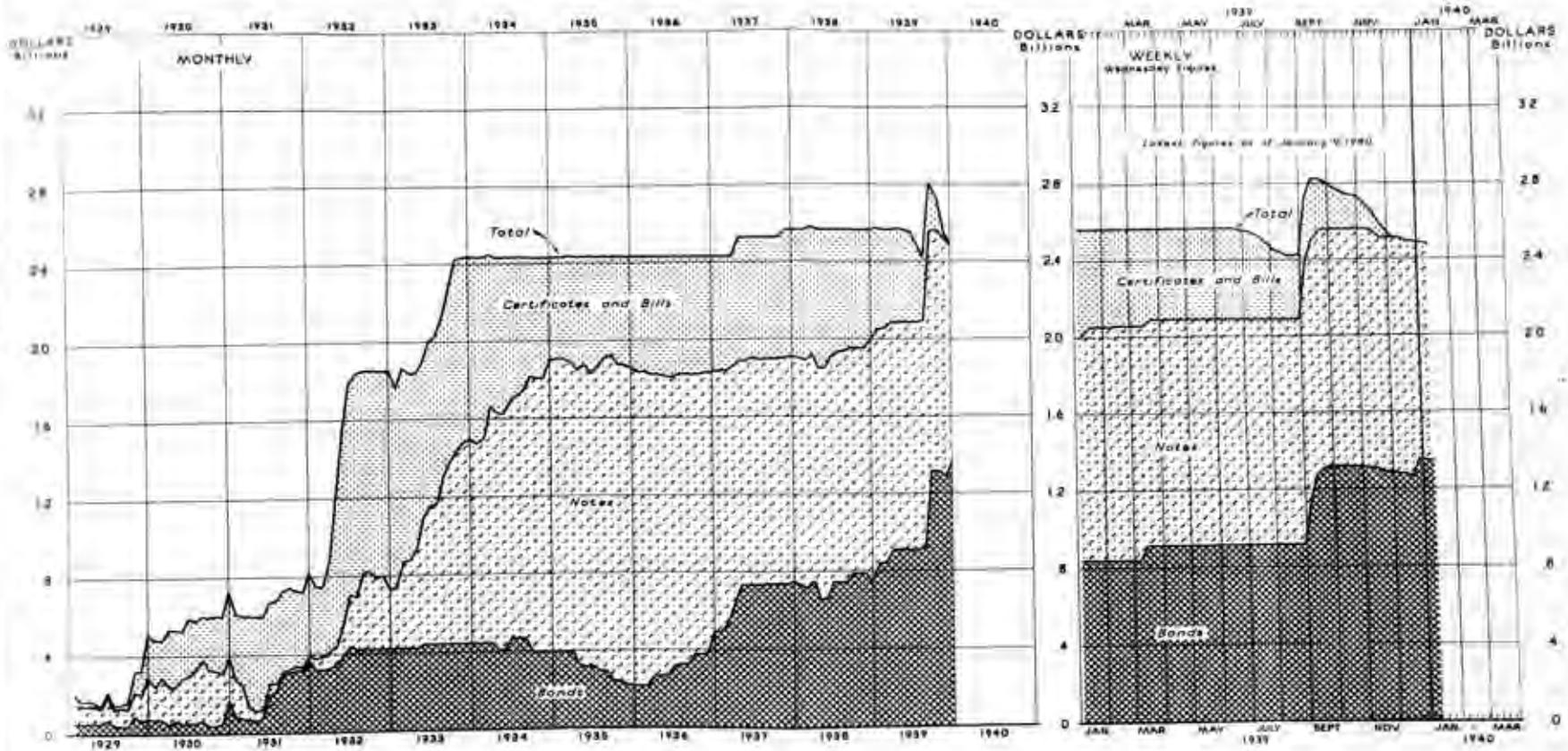


Office of the Secretary of the Treasury
Division of Research and Statistics

U. S. GOVERNMENT SECURITY HOLDINGS. WEEKLY REPORTING MEMBER BANKS
 Cumulative Net Change from September 27, 1939

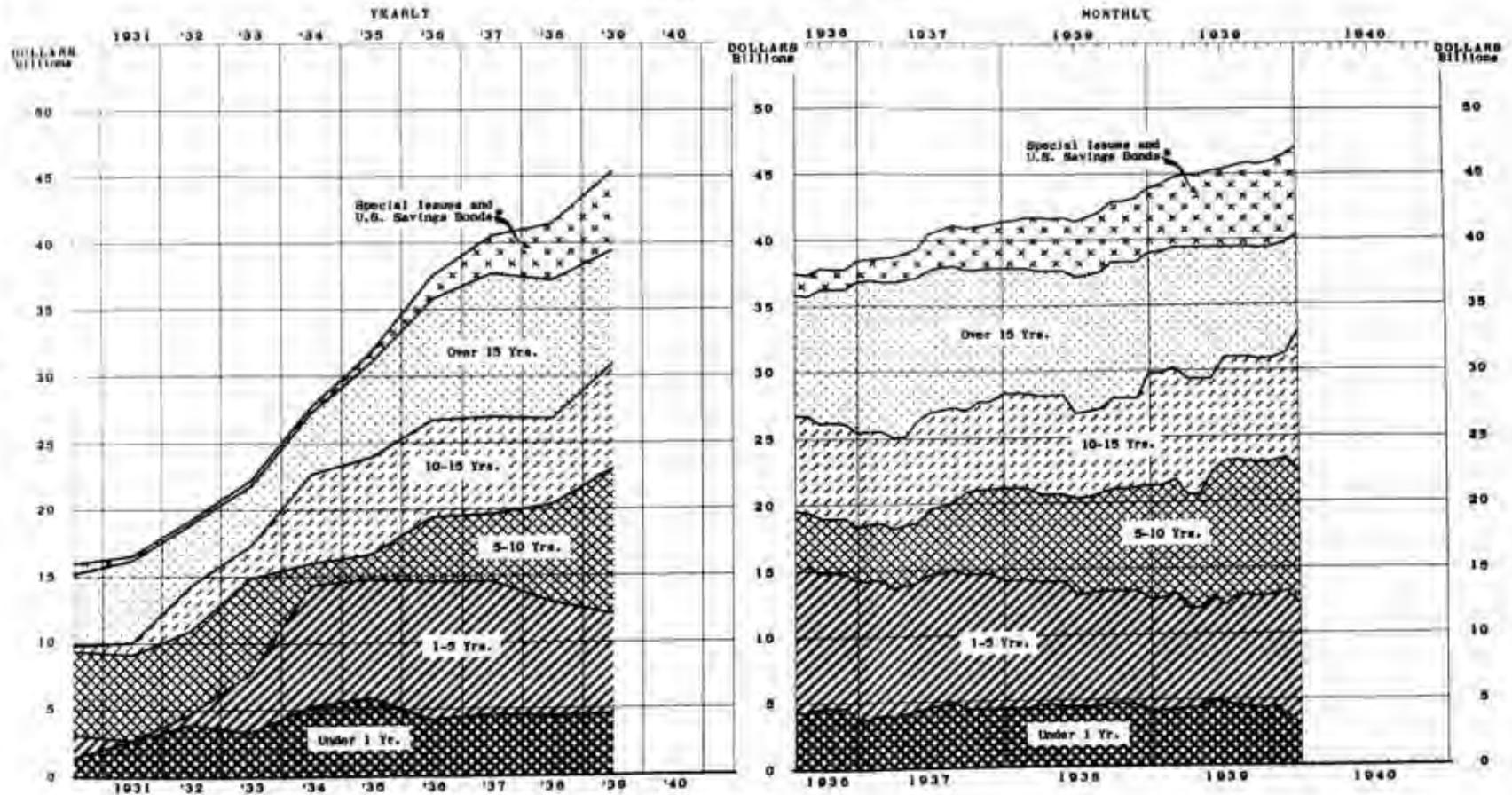


FEDERAL RESERVE BANK HOLDINGS OF U.S. SECURITIES



U.S. GOVERNMENT PRINTING OFFICE: 1939

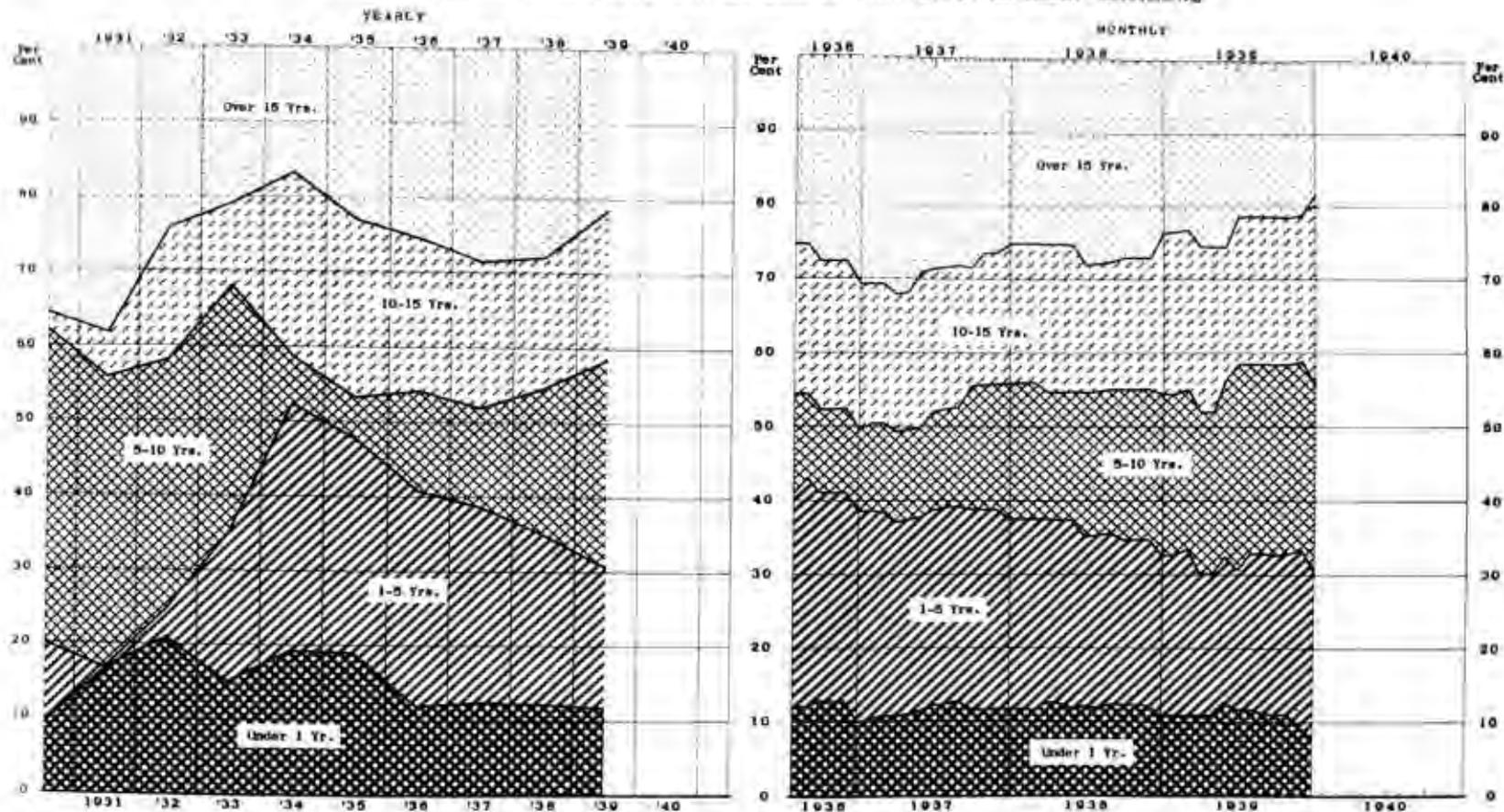
INTEREST-BEARING DIRECT AND GUARANTEED PUBLIC DEBT
Classified by Number of Years to Maturity



*Including Adjusted Service Bonds.

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INTEREST-BEARING DIRECT AND GUARANTEED PUBLIC DEBT
 Classified by Number of Years to Maturity and Shown as Percentages of the Amount^a Outstanding



^aExclusive of U.S. Savings Bonds, Adjusted Service Bonds and Special Issues.

Chart VIII

COMPARATIVE YIELDS OF AVERAGE OF ALL LONG TERM U.S. TREASURY BONDS AND U.K. 2½% CONSOLS

