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TREASURY DEPARTMENT
Washington

FOR RELEASE, MORNING NEWSPAPERS,
Tuesday, October 21, 1941
10/20/41

Press Service
No. 28-12

The Secretary of the Treasury announced last evening that the tenders for \$150,000,000, or thereabouts, of 91-day Treasury bills, to be dated October 22, 1941, and to mature January 21, 1942, which were offered on October 17, were opened at the Federal Reserve Banks on October 20.

The details of this issue are as follows:

Total applied for - \$303,852,000
Total accepted - 150,185,000

Range of accepted bids:

High - 100.
Low - 99.989 Equivalent rate approximately 0.044 percent
Average price 99.994 " " " 0.024 "

(71 percent of the amount bid for at the low price was accepted)

October 21, 1941
9:30 a.m.

GROUP MEETING

Present: Mr. Haas
Mr. Thompson
Mr. Blough
Mr. Foley
Mr. Morris
Mr. Bell
Mr. Kuhn
Mr. Schwarz
Mr. Gaston
Mr. Barnard
Mrs. Klotz
Mr. White

H.M.Jr: I am going to rush you people a little bit this morning. Eccles is coming in at ten because I have just got to get on this financing.

(The Secretary held a telephone conversation with Mr. Sproul and Mr. Rouse.)

H.M.Jr: Whose job would it be to find out whether the Navy have notified their various people that Mr. Knox is going on the air tonight?

Kuhn: I can do that. You mean the people at sea and so on?

H.M.Jr: Well, particularly in the schools. They think they should be notified.

Kuhn: Oh! All right.

H.M.Jr: There are forty thousand boys in schools, and they think they should be excused tonight to listen to Mr. Knox. At sea and at school.

Kuhn: I will do it right after this meeting.

Gaston: We are in the Navy now. (Laughter)

Kuhn: Roy just asked if the Navy had taken over the Treasury Hour, and I said, "I wished they had." (Laughter)

Klotz: It would make life simpler for you.

H.M.Jr: Incidentally, you might tell Vincent Callahan to tell Mr. and Mrs. - whatever their names are.

Kuhn: Hummert?

H.M.Jr: Yes. That when they go to the trouble to put on a song by an American composer, they might mention his name. They didn't mention his name last night. Would you pass that on? Did you listen?

Kuhn: No.

H.M.Jr: Well, I did. They didn't mention his name. "We will now hear a song by a young American composer in the Army," and then they play it and don't say what he is doing in the Army or his name.

Bell: It is probably against the rules of the Intelligence Service. The...

H.M.Jr: ...

THOMAS: ...

H.M.Jr: Dan?

Bell: You sent me this cable of October 16 from Fox and asked for a reply today. That cable came in last Thursday when we were preparing a cable to Fox, and we read it over and it said in that cable: "We have just received your 4-20. We are nevertheless sending you this cable to clarify the situation."

Now there are more cables in last night from Fox which we haven't gotten yet, and this doesn't really need answering at this point. We have set it out in the cable that went out last Thursday.

H.M.Jr: Well, can I forget about it?

Bell: Yes, sir.

H.M.Jr: Are you and White in agreement?

Bell: I think we are. I think all of us are in agreement. Probably tomorrow or Thursday we will have another conference on China when the new cables come in.

H.M.Jr: O.K.?

Bell: Yes, sir.

H.M.Jr: Got anything else?

Bell: I have an amendment to the Treasury regulations on tax notes which will enable parent companies to subscribe for subsidiaries. Our balance Saturday got down to a low of five hundred million.

H.M.Jr:

Yes

(Mr. Bell handed tax anticipation note pamphlet to the Secretary.)

- H.M.Jr: When it is printed, it won't come through like that, will it?
- Bell: Yes, sir, that is the printed document.
- H.M.Jr: Will it show through? What do you call that, offset?
- Gaston: That is offset on the press. That is not offset printing. It is an offset on the press.
- H.M.Jr: On the press?
- Gaston: Yes.
- H.M.Jr: That is what I meant.
- Bell: I take it it was the grade of paper they had to use.
- Gaston: It doesn't come through, but it is from the draw sheet - it picks up the previous impression.
- H.M.Jr: I wish you would tell the Government Printing Office it is very unsatisfactory. Just hold that in your hand.
- Who contacts them?
- Bell: I don't know who did it, but we will find out.
- H.M.Jr: Well, would somebody pass the word before they print them all? You can't read that.
- Gaston: Of course, that is a thing they will only run for one or two impressions. That is something that picks up - where the type is run

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through without the sheet, and then they try to scrub it off, and it picks up for two or three sheets after that.

H.M.Jr: Get me another copy, will you.

Bell: Yes.

H.M.Jr: This is terrible. Get me another copy.

Bell: Yes.

That is all I have.

H.M.Jr: Harry?

White: I have nothing.

H.M.Jr: Wonderful.

Schwarz: I have nothing.

H.M.Jr: Have you got any follow-ups?

Klotz: I am looking for them.

H.M.Jr: George, at ten o'clock, Eccles and you and Henry Murphy, please.

Haas: All right.

H.M.Jr: How about that cost of living stuff for Mrs. Roosevelt?

Haas: Here it is. Last night I had this run off (handing report to Secretary), which gives the September thirtieth. The latest we had was August. It didn't change it much.

H.M. Jr: All right?

Haas: Yes.

Kuhn: Major Namm and his Retailers' Group will be meeting here in the Treasury on Thursday. Harold Graves is very anxious to have you just say "Hello" to them downstairs sometime Thursday. Could you manage it?

H.M. Jr: Sure. Remind me Thursday.

Kuhn: Thursday morning?

H.M. Jr: Yes.

What is the name of the fellow that used to be comptroller of Macy's?

Barnard: Beardsley Ruml.

H.M. Jr: Is he still there?

Barnard: Yes, still treasurer.

Kuhn: I have the time of the various items tonight. I will send it in to you in the form of a memo.

H.M. Jr: What time? Will you get it in to Mrs. Klotz's hands, actually get it in to her hands? Then I will get it. Please. What time does Noel Coward come on?

Kuhn: Eight twenty-three something.

H.M. Jr: I have...

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Kuhn: I have all the information about that man. I didn't know what you wanted it for.

H.M.Jr: Well, the other man, this fellow Streit is --

Kuhn: Oh, yes, Etheridge is a different kind of fellow. He is a political writer.

H.M.Jr: Well, Streit?

Kuhn: Streit will be down in Washington tomorrow if we want him.

H.M.Jr: Last week on October 25 or thereabouts we got a letter from the Pittsburgh United Electric and Machine Workers, and I wanted to send a letter.

Kuhn: I believe it was answered on Saturday.

H.M.Jr: Would you tell Mrs. Klotz about it sometime?

Kuhn: Yes.

H.M.Jr: All right, Ferdie?

Kuhn: Yes.

H.V.Jr: Hoy?

Blough: The British-Canadian income tax comparisons you asked for will be ready before lunch today.

H.V.Jr: Wonderful. With an explanation so I can understand it?

Blough: With some explanation which we will be glad to elaborate as much as you wish.

H.V.Jr: You see what I want with this Canadian thing; I'll also to say the various things that come in a way there; the withholding tax.

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and this tax and that tax, and they have to make -- I know they have to make a tax for the war -- I mean, I think it is a hospital tax. They have got all kinds of taxes.

- Blough: You want a description of these taxes plus the effect of the whole business as a burden?
- H.M.Jr: Yes. And then how it affects the fellow - I would give it in various jumps, you see, from one thousand to two thousand, twenty-five hundred and up, you see.
- Blough: The tables are already ready.
- H.M.Jr: You take the workman in Canada has to pay four or five different taxes.
- Blough: That is correct.
- H.M.Jr: And you have them all?
- Blough: We have them all, but it may take a little bit longer to write, so it may be the middle of the afternoon before it is ready.
- H.M.Jr: That is all right.
- Morris: I have a letter from Allen Sproul. I am not quite sure whether you saw it or what I am supposed to do with it. It says he is working on trying to get some data on capital issues.
- H.M.Jr: That is just for your information, that is all.
- Morris: And has Sullivan seen you about a report on yesterday afternoon or do you want one?
- H.M.Jr: No. Last night he went home with me, and I talked with him at eight this morning, so I am up on that. You might acknowledge that letter from Sproul.

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Morris: All right.

H.M.Jr: Will you be here at ten?

Morris: Yes.

H.M.Jr: Ed?

Foley: We got a telegram from Irving Wright, the chief examiner on the West Coast, to the effect that the Yokohama Specie branch in San Francisco, there were very large withdrawals yesterday, and it may be necessary to close that branch, and I have contacted Dean Acheson. He has got his people over here this morning, and they are phoning the facts to us at twelve o'clock, our time.

H.M.Jr: Yokohama Specie where?

Foley: In San Francisco. They don't know whether these licensed Japanese nationals are taking it out and putting it under the mattress or putting it in another bank. They are getting those facts for us, too. Insofar as liquidity is concerned, the bank is under water. It may be necessary to revoke the license.

H.M.Jr: Let me know.

Foley: Insofar as retaliation is concerned, only the National City has one branch. The other two branches are closed in Japan.

I talked to Francis Biddle yesterday and he doesn't want to give us those names. He says he is going to make an investigation himself unless he was given a hundred thousand by Congress to make the investigations. After

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Hoover. I will talk to Hoover again, however, but he thinks that that is --

H.M.Jr: Well now, Gaston is taking up their whole thing. This is these fifty-six so-called communists in the Treasury. Why am I not entitled to know? If he won't give them, Mr. Dies will give them to me.

Foley: I said that he said he thought that would be better. He didn't think it would look right for him to give them to us.

H.M.Jr: Oh, nuts. I am just sick and tired of the way Francis Biddle is behaving. My God, he is the worst yet.

White: Absolutely.

Gaston: Yes.

H.M.Jr: This is in the room.

White: He is worse than that.

H.M.Jr: He is the worst one yet (laughter). I thought, gee whiz --

White: Popular, isn't he?

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Gaston: Did you read the New Yorker's story on Bridges having fun with the FBI? It may soothe you a little bit if you read that.

H.M.Jr: Send it in to me.

Well, Herbert and this man (Thompson) know about my contact on this, investigating under orders from the President on OPM. Have you (Gaston) got it up now?

Gaston: Yes, I have.

H.M.Jr: Talk about it and if Francis Biddle won't give it to me, see --

Foley: He doesn't want to.

H.M.Jr: Well, if he doesn't give it to me --

Foley: I told him I would mention it to you.

H.M.Jr: All right, we will ask Mr. Dies for it because I am not going to sit here for months while J. Edgar Hoover investigates the Treasury.

Foley: Well, we can pick it up from Mr. Dies. I don't think we will have any trouble getting it from him at all, but I think Francis is right. I think it would be better for us to get it from that source rather than for him to give it to us because it would look like a whitewash if he turned around and gave it to us, particularly when he has been given a hundred thousand dollars by Congress to make this investigation.

White: Now look, Ed, if there are any Communists in groups, it seems to me the quicker we know it and the quicker we get them out, the better. There is some awfully confidential material floating around here.

Foley: That is perfectly true, Harry, and he says that the people that he and I know on the list are people that obviously Dies has taken from some mailing list somewhere and they are no more Communists than we are.

Thompson: I suspect we have already investigated them.

H.M.Jr: You missed it. I got off a good one. Ed Foley says they are no more Communists, Harry, than you and I are, and I said, "How much is that worth?"

Foley: That is what Biddle says to me, "than we are."

H.M.Jr: Well, I still say, ever since Ed has seen there is a ten thousand dollar fellow on that, he has been a little worried. Well, anyway, if this fellow --

Foley: Do you want me to ask Larry to pick it up from the Dies Committee?

H.M.Jr: Yes.

Foley: Well, that will be all right with Francis.

Thompson: Then we ought to check that list with the investigations we have made. We have probably covered them all.

Foley: I think that is right. There is one fellow on there I am sure of too, Dan.

H.M.Jr: All right. Now what else?

Foley: Congressman Luther Johnson, who is on the Foreign Affairs Committee --

H.M.Jr: I had better call up Elmer Irey first and see if it is all right with him because I don't want to

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get Elmer Irey angry at me. (Facetiously)

Klotz: You couldn't.

H.M.Jr: But that is what happened over there when they went over to see them. Francis Biddle says, "I don't know whether I can do this. This may make Mr. Hoover very angry." Isn't that what he said?

Thompson: He didn't mention Hoover's name, but that is what he said.

Gaston: He is too big to mention him by name. He just says, "he, and "him."

White: Capital "he"? (Laughter)

Gaston: He didn't mention Hoover by name. That would be sacriligious.

H.M.Jr: Are you all through, Ed?

Foley: Yes. (Laughter) I am discouraged.

Gaston: In view of the turn that this Honolulu thing is taking, we are sending Fred Gaertner, the Supervising Customs Agent on the Pacific Coast and one of his brightest men out by Clipper from Honolulu Thursday. They are going to get there Saturday--

H.M.Jr: Well, I think on that--

Gaston: to see if they can give any help, because it has turned into a proposition where the Army isn't taking the stand of wanting to see that justice is done. It is a straight out battle against the Customs. They want to destroy this man.

H.M.Jr: Well, I want Ed Foley, then, to send one of his men too.

Gaston: Well, you see, he can't act as a lawyer out there.

H.M.Jr: He can tell me, though, what is going on.

Gaston: This man Fisher, one of the two Customs men who is going out, is a lawyer.

H.M.Jr: I still say, if it is this kind - I would like Ed to send a man out.

Gaston: All right.

H.M.Jr: It is a straight legal matter and it is now between Stimson and myself and I want to be advised on the law on that.

Gaston: I don't think, just privately, that Stimson is strong enough to buck that Army machine.

H.M.Jr: No, I think Stimson is a great fellow. Don't forget what he did on the Spanish thing, and so forth. I think you underestimate him. On a moral issue, there isn't a finer man in this country than Henry Stimson. He is strong enough to buck anybody on a moral issue. I have got great respect for him. But I think if we are sending people out - talk it over.

Gaston: I will do that.

Foley: I think we ought to have somebody there who can make an investigation of the facts and let us know.

H.M.Jr: Well, you talk it over. My inclination is, I think it ought to be a lawyer.

Foley: All right.

H.M.Jr: And a trained one.

Anything else? All right?

Gaston: All right. Oh, I wanted to tell you, I don't know whether Carl Shoup sent to others in the Treasury a copy of his study on the necessary taxation to stop inflation. If he didn't, I have a copy of it. It is quite interesting.

H.M.Jr: Well, I got a letter about it and he is to be here Thursday morning, but if you have it, if you would give it to --

Haas: He sent several around.

White: He sent several around. It is worth reading, particularly the first few pages.

H.M.Jr: I would like to have one.

Gaston: Seventeen percent supplementary additional taxation on net income.

H.M.Jr: I would like to have one.

October 21, 1941
9:30 a.m.

HMJr: Hello.

Allan
Sproul: Good morning, Mr. Secretary.

Robert
Rouse: Good morning, sir.

HMJr: Good morning, gentlemen. Look, if you don't know now, could I call you back a little later? I'd like to have you tell me what you think we ought to do on this refunding.

S: Well, I can tell you what I think right now.

HMJr: Go ahead.

S: I think we ought to - that you ought to open up the bunch of '43's, and give a fifty per cent exchange to the maturing RFC's and CCC's and do the rest for cash in the same issue.

HMJr: Uh huh.

S: I think that fits in best to the general program of financing we've been talking about, that is, long term obligations for the permanent investors and as short as possible including bills for the banks.

HMJr: Uh huh.

S: And it's impossible to do this all with bills and to retain any rights values, which I think is desirable temporarily, and therefore the next best thing, it seems to me, is that short note in which only a small amount is outstanding and in which price - pricing it at par to exchange holders gives about the right premium on a 50% exchange.

HMJr: Yeah. That's the way you feel.

S: Yeah.

HMJr: Well, we're pretty far apart.

S: What?

HMJr: We're pretty far apart.

S: We are? (Laughs)

HMJr: Yeah. But I'll call you back a little later.
Mr. Eccles is coming in at ten.

S: I see.

HMJr: And I'll call you back after he leaves.

S: All right, fine.

HMJr: Thank you.

Treasury Department 19
Division of Monetary Research

Date 10/21/41 19

To: Miss Chauncey

The Secretary might well read
the first Chapter (which is a summary).

However, if he doesn't have
time, I am having a one page summary
made of the memorandum which will be
done in ample time for him to read
before the three o'clock meeting.

H.D.W.

MR. WHITE
Branch 2058 - Room 214 $\frac{1}{2}$

TREASURY DEPARTMENT

20

INTER OFFICE COMMUNICATION

DATE October 21, 1941

TO Mr. White

FROM Mr. Shandro

Subject: Summary of Report "Amount of Taxes Needed in June 1942 to Avert Inflation"

It is estimated that in June 1942, defense spending will be at an annual rate of \$12 billion higher than in June 1941. As production in June 1942 will probably be at a rate of \$12 billion higher than in June 1941, the output of civilian goods (probably for private investment) will be restricted by \$2 billion.

This program of increased defense spending cannot be achieved without a rise in prices unless purchasing power at the annual rate of \$12 billion -- the increase in defense spending minus voluntary reduction in private capital formation -- is withdrawn from the public. Increased Federal revenues will absorb \$6 billion of this sum. Of the remaining \$6 billions, \$1 billion will be absorbed by the increased sale of defense bonds.

This leaves \$5 billion still to be mopped up.

If inflation is to be averted, further withdrawals at the annual rate of at least \$5 billion must be taken from consumer incomes by June 1942. It is even possible that the withdrawal of as much as \$8 billion may be necessary. This can be achieved by compulsory saving or increased taxation. It is probably easier to collect higher taxes now than in the post-war period.

The best form of taxation (according to the report) is a supplementary tax on incomes, collected currently at the sources to avoid the lag, to facilitate the taxation of low incomes, and to make rate changes easier. A supplementary income tax, to take effect in January 1942, at the rate of 13 percent rising to a maximum of 17 percent in later months on income in excess of \$2,000 (single, \$1,000 married, \$500 single, \$300 per dependent) would raise revenue at the rate of \$5 billion annually; a 24 percent rate would raise \$7 billion; and a 31 percent rate would raise \$9 billion.

The report points that even such a program has the following limitations:

1. Cannot stop certain types of price rises.
2. Taxation may not prevent a rise in the cost of living in view of the large stock of goods.
3. ...
4. ...

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Columbia University
in the City of New York

SCHOOL OF BUSINESS

October 17, 1941

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

Dear Mr. Secretary:

I am enclosing a copy of a research report that analyzes the need for taxation to prevent inflation. I trust that this study may be of some value to the Treasury in the light of the current pressing problems of finance.

Sincerely yours,

Carl Shoup

Carl Shoup

CS:RA

enclosure

AMOUNT OF TAXES NEEDED IN JUNE 1942 TO AVERT INFLATION

A Preliminary Report Submitted to a Joint Committee
of the Carnegie Corporation and the
Institute of Public Administration

CARL SHOUP

MILTON FRIEDMAN

RUTH P. MACK

October 15, 1941

AMOUNT OF TAXES NEEDED IN JUNE 1942 TO AVERT INFLATION

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October 15, 1941

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SUMMARY OF PRELIMINARY REPORT ON AMOUNT OF TAXATION NEEDED
IN JUNE, 1942, TO AVERT INFLATION

The cost of living in the United States has been rising during the past few months almost as fast as it did during the first world war. In no year in the period 1915-1920 did the index rise at an average monthly rate for the year greater than 1.7 per cent. The rise from March to April, 1941, was 1.0 per cent; from April to May, 0.7 per cent; from May to June, 1.7 per cent; from June to July, 0.6 per cent; from July to August, 0.8 per cent. Moreover, the Federal Government is planning to increase greatly its defense spending. Is there, then, a real danger of substantial inflation (that is, a substantial rise in the cost of living) over the next year or two? If the danger exists, can it be largely eliminated by increased taxation? How much taxation is needed for that purpose, and when?

Let us compare the situation as it stood during last June with the prospects for June, 1942, under a favorable set of assumptions. In June, 1941, defense expenditures were more than \$200 million, or at a rate of about \$10 billion a year. In June, 1942, they are expected to reach an annual rate of \$24 billion, or about \$14 billion more than in June, 1941. Production for the country as a whole can probably increase at most by about \$12 billion in the same period. Hence civilian output must decline by \$2 billion at June, 1941, prices. If consumer spending did not rise above the June, 1941, level, it seems likely that private capital formation would decline by between \$1 billion and \$2 billion. If the larger of these declines occurs, the increase in expenditures by government minus the decrease in the spending by producers of private capital goods can be matched by an increase in physical output. But the fact that \$12 billion more is being spent means that consumers will be getting about \$12

billion more income (actually nearer \$11 billion because of retention of profits by corporations; but to avoid dealing in fractions of billions in the computations that follow in this summary, the \$12 billion figure is used). Federal tax revenue will be at an annual rate about \$6 billion higher next June than last, as a result of both the larger flow of income and the higher rates enacted in the Revenue Act of 1941. The \$12 billion increase in consumers' income will therefore mean only a \$6 billion increase in purchasing power. But the consumers will have no greater physical amount of consumer goods and services on which to spend this added \$6 billion, for they will have received this extra income by producing, not consumer goods, but armaments, which they cannot buy. Last June, consumers were buying at an annual rate of about \$70 billion. Next June, government and producers of private capital goods will together, net, be adding to consumer purchasing power some \$6 billion a year more than last June. The recipients of this added purchasing power will be spending part of it on consumption -- probably some \$4 billion a year more than last June, the remainder being absorbed by personal or corporate saving. Those who benefit by the increase of \$4 billion a year in consumption expenditures will in turn be spending more than in the previous year. Just what the total increase in consumers' spending will be is difficult to estimate, but it would probably be at least \$8 billion a year.

By next June, then, consumers would be spending at an annual rate of at least \$78 billion, with only \$70 billion of goods and services to spend it on, at last June's prices. The extra \$8 billion of consumers' outlay would be almost entirely reflected in a price rise, of about 10 per cent. With so sharp a rise in consumer spending and consequently in prices, the expenditures on private capital goods would probably not decline by \$2 billion (assumed above) but might instead actually rise. More than that, the government's own spending would presumably increase, since it would have to pay higher prices for the

goods it purchased (its tax revenue would increase too, but probably not so much). The rise in the cost of living would strengthen existing tendencies toward wage increases, thus raising costs, and therefore prices, still higher. Hence the cost of living would probably have risen by much more than 10 per cent next June. To prevent this widespread rise in prices by direct price control would require universal rationing and merciless policing.

Such price rises, based on an excess of consumer purchasing power, can be stopped by preventing consumers from getting the \$6 billion excess purchasing power, or by inducing them to spend less of it than they normally would. The Defense Savings Bond campaign will help somewhat here. Suppose that consumers are buying Defense Bonds, next June, at an annual rate about \$4 billion greater than last June. Part of this will reflect merely a shifting of assets -- a drawing down of savings deposits, return of hoarded currency, and so on. Part of the rest will come from normal savings, the kind of savings that are already allowed for in the calculations above. Only the remainder -- probably not more than \$500 million a year -- will come out of money that would otherwise have been spent on consumption. This reduction in consumer outlay because of Defense Bond purchases will offset an equivalent amount of spending by the recipients of the excess purchasing power that the government is distributing through its defense program. Taking into account indirect effects on the income and spending of others, total spending by all consumers would be about \$7 billion a year above June, 1941, instead of \$8 billion, thanks to the Defense Savings Bonds campaign. This decline of \$1 billion in extra spending would help, but obviously it would not be enough to stop the upward spiral of prices outlined above.

To stop the price rise, consumers must be prevented from getting the excess purchasing power not offset by the Defense Bonds that are bought by cutting

consumption. The surest way, and in fact the only practicable way, to prevent them from getting it is to extract an additional \$5 billion or so from their incomes, either by additional taxes or by compulsory savings. That is, by June, 1942, the government must be collecting, currently, \$5 billion more out of consumer incomes than will be coming in under the present revenue system, if it wants to prevent a substantial rise in prices by then and forestall an even more serious one in the latter part of calendar 1942.

The extra receipts needed by June, 1942, to prevent a price rise may prove to be much higher than \$5 billion, possibly as high as \$9 billion (annual rate). The \$5 billion estimate is based on a combination of optimistic assumptions about possible increase in output, and decline in expenditures by producers of private capital goods.

One way to increase government receipts out of consumer income is through forced savings brought about by compulsory payments to the government in return for securities not redeemable until after the emergency. But while this method has the advantage that it promises a future payment for present sacrifice, it would mean as great a sacrifice in terms of the individual's present consumption, and would further intensify the post-war problem posed by a large public debt. There is little reason to believe that the taxes which would repay the debt -- or even pay the interest on it -- would be any more progressive than those which can be levied now. The time to collect the tax is now, when the government is adding large sums to the income stream through the defense program.

A tax on income is the most direct method of absorbing the excess purchasing power. But an increase in the ordinary income tax will not do. A Revenue Act of 1942, even if passed early in the year, would not drain purchasing power until 1943. The added tax must be collected currently from 1942 incomes. The best way to do this is to utilize collection at the source so far as possible --

to have the payor deduct the tax from the wage, salary, interest, or dividend payment before it reaches the worker or investor. Collection at the source is necessary anyway, for two other reasons. First, even the most careful forecast of the amount of taxes needed to prevent a price rise will prove somewhat in error. The amounts involved are so large that an error could have serious consequences unless it were subject to prompt correction by changes in the rate of the new tax as often as every three months or so. Second, the amount of new taxes needed is so large that it will almost surely force a lowering of the personal exemptions still further (say, to \$1,000 for a married couple and \$500 for a single taxpayer). Taxpayers near these levels can be reached satisfactorily only by collection at source. Moreover, since they spend about as quickly as they receive, they might not have the cash on hand to pay the tax unless they were asked to pay at least once a month; and they could scarcely be expected to file twelve returns a year. But they could file one return a year, which would allow them to claim refunds, if personal exemptions, etc., had not been correctly taken into account in deducting at source. Similarly, it will be difficult to collect increased taxes from taxpayers somewhat higher on the income tax scale unless a convenient method of installment payment is provided for the additional tax burden. Partners and proprietors (including farmers), and landlords could be required to submit quarterly returns, paying on their estimated current incomes, subject to an annual correction.

To raise the \$5 billion, this supplementary source-collected income tax would have to be imposed at a rate of about 17 per cent on that part of the income in excess of exemptions of \$1,000 (married) and \$500 (single) and a \$300 credit for each dependent.

If \$9 billion had to be raised, a 31 per cent rate for the supplementary income tax would be needed. It would be better, then, to put the exemptions

substantially below \$1,000, \$500, and \$300, and possibly modify the revenue requirements to allow a price rise of, say, 5 per cent a year, thus permitting the use of a much lower tax rate.

If \$7 billion had to be raised, a 24 per cent tax rate would be needed, under the \$1,000, \$500, and \$300 exemptions.

If we had to make a decision at this moment, we should recommend a tax on the lowest basis, that is, at 17 per cent, subject to upward change if a further check of our technique and data indicated still a range of \$5 billion to \$9 billion. If it did, we should then recommend lowering the exemptions to about \$900, \$450, and \$250, and also allowing the cost of living to rise very moderately, thus permitting the tax rate to be set at perhaps 20 per cent.

To avoid more than 100 per cent taxation in combination with the 1941 Revenue Act, the 17 per cent tax could be levied on the income minus the regular income tax on 1942 incomes paid under the 1941 Revenue Act. This adjustment would be carried through in the annual return, filed in 1943, not in the withholding.

To avoid a steady upward rise in prices before next June, the supplementary income tax needs to be in operation, at a somewhat lower rate, as early as January, 1942. The rate should, for this purpose, be at least 13 per cent for the first quarter of 1942, and 17 per cent for the second quarter (April-June). Even then, a price rise from the June, 1941, level would not have been entirely avoided; some has already occurred, and more may occur by January, 1942. To this extent our computations in this preliminary report do not take full account of the actual situation.

If the supplementary tax were thought to be somewhat too light on the well-to-do, the rate schedule of the regular income tax could be adjusted accordingly.

A supplementary income tax of 17 per cent on that part of an individual's net income above \$1,000 (\$500 single) is a severe burden, but not so severe as the evidently inevitable rise in the cost of living that will result unless some tax measure of this magnitude starts draining purchasing power by January and is in full operation by next June.

Some limitations to the scope of the present report must be emphasized. In the first place, some kinds of price rise cannot be stopped by taxation -- for example, the recent increases in the prices of cotton and wheat so far as they have been caused by the government's loan program. The present report offers no suggestions on direct prevention of such price increases. In the second place, the amount of money that should be raised by taxation may be greater than the amount needed merely to prevent a rise in the cost of living. The long term possibilities of an unduly heavy interest charge on the budget and a dangerously large stock of money are relevant here; but limitations of time and resources have made it impossible for the present report to analyze these matters. The amounts of taxation that we now recommend are therefore minimum quantities. They would by no means balance the budget; in fact, they imply the continuance of a large annual deficit.

In the third place, our analysis of anti-inflationary taxation has not given full consideration to the problem of special taxes on business income. A simple rise in the corporate income tax rate does not seem very suitable; the answer may lie in some form of taxing undistributed corporate profits -- a complex matter than cannot be adequately treated in this report.

In the fourth place, the figures that we have used in our computations can surely be refined by further research and will surely have to be changed as new conditions develop. At the least, a monthly recomputation is called for, even though it would be better not to shift the tax rate, in practice, until the re-

AMOUNT OF TAXES NEEDED IN JUNE 1942
TO AVERT INFLATION¹

How much taxation is needed if a substantial rise in the retail price level ("inflation") is to be averted? To this question the present report addresses itself, and to collateral questions also: How soon are the tax measures needed? What kinds of taxes will be suitable for this purpose?

The present report is preliminary; it will be followed, within a month or two, by a final report that will include, among other items, statements of sources utilized in deriving the data that, for brevity, are presented here without much explanation.

This preliminary report first discusses, in the light of recent changes and the general prospect for the next year or so, the advisability and possibility of keeping the cost of living from rising sharply. Then follows a description of what has proved to be the major task of the present study, that is, the computation of the approximate amount of added tax revenue that will be needed if a substantial rise in the cost of living is to be avoided. The technique used in this computation is described first in general terms and then step by step. The added revenue needed is given as of June, 1942. Computations for a number of earlier months -- even for months before January, 1942, if there is any real prospect of enacting new tax

1. The present study was made possible through a grant of funds to the Institute of Public Administration by the Carnegie Corporation, and has been carried on under the auspices of a joint committee representing the Corporation and the Institute. The members of the committee and the two institutions bear no responsibility for the contents of this preliminary report. The work was started in June, 1941; it is expected that a final report will be submitted toward the close of the year. The authors acknowledge the valuable assistance of Harlan Bramble and George Lent in research, and Dorothy Harmon, secretarial assistant. We cannot express adequately here our indebtedness to the many individuals who have assisted us so generously.

measures before then -- can be made by the same technique. Lack of time and resources is the only reason they have not been given here. The final section discusses the kinds of tax that would be suitable to raise the revenue needed to avert inflation, and offers some recommendations on this score. An appendix describes briefly the work done by others in the field covered by this report; another appendix presents an algebraic formulation of our technique.

The Growing Divergence of Money Income and Real Income

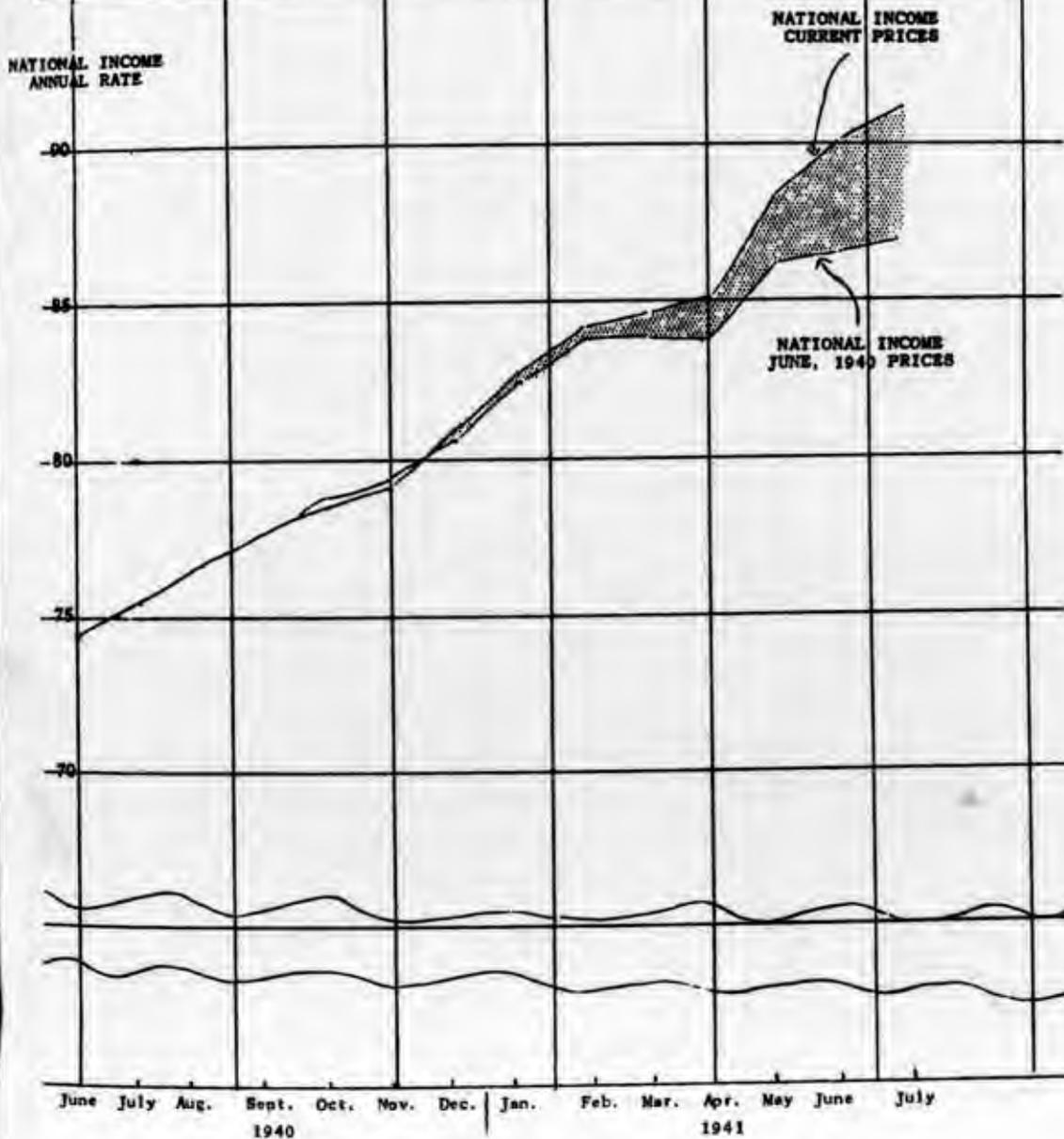
Three major aspects of the events of the past year need to be kept in mind in formulating a fiscal policy for the coming year.

In the first place, during June, 1940, real national income was being generated at the rate of \$74 billion a year. One year later the flow had increased to \$86 billion in June, 1940, prices.

In the second place, this increase of \$12 billion was spread throughout the economy. Although the largest part, perhaps over one-half, had taken the form of increased defense, there had also been a marked increase in both the flow of consumer goods and services and additions to privately owned business plants not included in the defense expenditures.

In the third place, the increased physical output was accompanied by a price increase of over 4 per cent as recorded by the somewhat lethargic Bureau of Labor Statistics cost of living index, which tends to understate the actual rise. But this increase for the year as a whole was by no means evenly distributed throughout the year. The accompanying chart shows for each quarter what part of the increase in money incomes went into a price rise rather than into a rise in real output. From the third to the fourth quarter of 1940, none of the increase in income was absorbed by the increase in prices -- physical output rose as rapidly as money income. From the fourth quarter of 1940 to the first quarter of 1941, only 10 per cent of the increase in money income was absorbed

**THE GROWING DIVERGENCE
BETWEEN REAL AND MONEY INCOME**



by price rises. But from the first to the second quarter of 1941, about half (51 per cent) of the rise in income went into increased prices rather than an augmented flow of goods. This tendency for rising prices to absorb a growing proportion of the increases in money income is apparently continuing -- from June to July, about 55 per cent of the increased income was so absorbed.

Defense Requirements and Output Limitations

If we look now towards the future rather than the past, the dominating fact is the magnitude of the defense program. We have estimated that it will increase from an annual rate of \$10 billion in June, 1941, to \$24 billion in June, 1942. These figures are based primarily on the October 5, 1941, estimate of the Director of the Bureau of the Budget.

In the past it has been possible to increase both output for defense and for civilian consumption. Can this continue?

The \$12 billion increase in the annual rate of output at constant prices from June, 1940, to June, 1941, is one of the largest, if not the largest, ever attained in this country during any twelve-month period. It was accomplished by increasing civil non-agricultural employment by some $3\frac{1}{2}$ million and average hours per week in manufacturing industries by about 10 per cent. The labor reserve is apparently sufficient to permit a further increase in employment and hours of about the same magnitude by June, 1942, though such an increase would come close to absorbing all but an irreducible minimum of the unemployed, unless it drew heavily on that part of the reserve that is not counted as unemployed. The smaller number of unemployed and the very much higher rate at which the economy is now operating makes the problem of absorbing such an increase far more difficult than it was a year ago. Moreover, the same increase in man-hours would probably yield a smaller increase in output. The additional man-hours would be worked primarily by the less skilled, since they are the ones who are

now unemployed or are working short hours; scarcity of materials and plant limitations are appearing at an increasing number of points; diminishing returns are setting in with increasing intensity; the need to use substitutes will increase the real cost of output, etc. These considerations suggest that we shall probably not exceed during the next year the record set during the 12 months prior to June, 1941, and may even fail to equal it. This view is supported by the slackening rate at which the Federal Reserve Board index of production has changed in June, July, and August.

If this conclusion is valid an extremely important inference follows: The real flow of goods to the private sectors of the economy cannot increase, during fiscal 1942, over the annual rate prevailing in June, 1941. In fact, it will have to decrease by at least \$2 billion (at June, 1941, prices). This fact, rooted in physical problems of production, is independent of fiscal policy at the same time that it sets the problem which fiscal policy must solve: How to maximize the real flow of goods for defense first and for consumption second, at the same time that the cost of defense is equitably distributed?

Relation of Public Finance Policy to Rising Prices

It is generally conceded that a rapid rise in the price level is one of the least equitable methods of distributing the cost of a war. It increases the cost of defense, it lays a burden of maladjustment on the future, it taxes the poor more heavily than the rich and wage earners more heavily than recipients of profit, and recipients of fixed incomes most heavily of all. To be sure, the recipients of fixed incomes must in any case sacrifice something, after the maximum aggregate of civilian consumption has been reached; an increasing part of the aggregate must be offered to defense workers thereafter drawn from other trades and from the unemployed. But the amount and distribution of the sacrifice of the fixed income groups can be determined to some extent by a careful

constructed fiscal policy, giving results preferable to those arising under the confusion of inflation. The prevention of a substantial increase in the cost of living is, therefore, a prerequisite to any equitable distribution of the defense burden; it is the major objective of fiscal policy today, although it is important to remember that it is by no means the only objective. This report does not deal with these other objectives but addresses itself exclusively to the problem of the prevention of price rises that serve no productive purpose and hence affect merely the distribution of the cost of defense.

In part, price change lies outside the jurisdiction of fiscal policy. Some part, for example, of the price increases during the past year were related to increases in the price of imported goods. Some part also resulted from rises in the price of agricultural products induced by guaranteed minimums deemed necessary to protect the farmer and encourage crop expansion. Although it would be possible for fiscal policy to counteract price increases of these sorts by inducing offsetting price decreases in other sectors of the economy, the resulting discouragement to production and hardships for various groups would make such a forced maintenance of a stable average level of prices scarcely worth while.

Fiscal control of prices is called for when, because of a general superfluity of money in the hands of would-be buyers relative to goods on the shelves of would-be sellers -- a situation well described by the term a "seller's market" -- there is a tendency for most prices to rise. The problem of preventing such a rise, should it be desirable to do so, is in large measure a Treasury problem. Such a situation exists today and is responsible for a very considerable part of the increase in prices over the past few months.

The question whether the moment has come to put a stop to it depends upon an analysis of the functions served by the price rise. It might make possible, by enlisting the efforts of marginal producers, an otherwise unattainable

increase in total national output. It might also facilitate the transfer of resources from private to public sectors of the economy and from one corner of the private sector to another.

The fact that total output of consumer's goods has in the past increased contemporaneously with prices suggests though it by no means proves that the price rises may have been responsible for part of the increase in physical output; the fact that increases in output are growing meagre compared with the price rise associated with them raises questions concerning the desirability of permitting price rises to continue. We are about at the point when the social cost of increases in output purchased by drastic price rise starts to exceed the social gain derived from the increased output. This is at best a very general judgment based on necessarily hazy evaluation of such factors as the extent to which the price rise is actually responsible for the increased output; the disorganization related to changes in price relationships; the extent to which the cost of defense will be increased; the tendency for price changes to spiral on the basis of labor demands and consumer reactions.

Price changes related to the second type of function -- facilitating transfers -- may well have a function to perform that is as yet unfulfilled. For this reason it may be well to set as the objectives of fiscal policy the prevention of significant price changes -- say a rise of 5 per cent or more a year -- rather than the maintenance of a stationary price level. As a first approximation, however, we have used an unchanging price level as our objective -- unchanged at least from January, 1942, if not from June, 1941, in view of the increase that will already be a fact by the earliest practicable time action can be taken on a new tax bill.

The Treasury can attack the problem of controlling price change by controlling redundant money incomes, computed net after taxes, when redundancy is

defined in terms of the relation between the dollar demand for goods of various sorts and the dollar equivalent of available goods at a stable or nearly stable price level. It could also conceivably attack the same problem by attempting to influence, by appropriate tax or other measures, not so much the amount of income after taxes as the proportion of the income that consumers and producers would be willing to spend. Although the latter approach might be very important when the pressing problem is how to increase spending, it is perhaps less well suited to the present problem, the restriction of spending. The former method of achieving a constant price level -- the draining off of redundant purchasing power -- is an efficient control device which is in part alternative and in part supplementary to direct techniques for price and production control.

Its efficiency lies in the very significant fact that it operates within the framework of accepted government function and form. It therefore does not have to overcome the inertia and resistance inevitably associated with new measures. It also does not endanger in ways difficult to anticipate the operation of an important economic equilibrating mechanism such as the price system. In the second place, it achieves its purpose through a minimum of restriction and policing -- certainly there is less onerous restriction of individual freedom involved in the payment of a higher tax than there is in the prescription and enforcement of the price which millions of sellers may ask and millions of buyers offer at thousands of individual transactions. The importance today of this sort of efficiency in government technique is hard to overstress. We are engaged in an undeclared war against autocracy. It would be as tragically foolish to emerge from that war with the weight of compulsion fogging American faces as it would to find there the fear of impotent dollars. Mechanically efficient techniques of control are the only assurance that we shall see neither.

However, draining off purchasing power seems a more efficient method of controlling prices of consumer goods than prices of producer goods. Its power lies in the extent to which income is the major determinant of spending over relatively short periods of time. This relation is fairly stable for consumers. But there are many factors other than current income that determine the willingness of producers to purchase plant and equipment -- prospective income, prospective and current rate of operation, technological change, the ability to borrow the necessary funds rather than finance capital purchases out of income. These factors cause the relation of spending to income to be highly variable over short periods of time. This means that the relationship that exists between the amount of producer current income and current additions to durable goods is both unclear and unpredictable in quantitative terms. If it were considered desirable to reduce the purchase of plant and equipment by private industry, the appropriate technique is not a general income or excess profits tax but a specific penalty tax on equipment purchases, priorities, licensing provisions and other instruments more accurately sharpened for their task of selective amputation.

The problem that we set ourselves, then, is the maintenance of an approximately constant price level through removing redundant consumer purchasing power, either by taxation or compulsory saving.

Method of Estimating the Amount of Taxes Required

Consumers receive income primarily in return for their contributions (or the contribution of their property) to the production of goods and services. These goods and services are of three major types: (1) those purchased by the Federal Government, including armaments; (2) consumer goods and services, including those secured through State and local governments; (3) additions to the nation's stock of capital not included in (1). While consumers receive income for the production of all three types of goods and services, they can spend this

income only on (2), consumer goods and services. The rest of their income is either drained off by taxes, or absorbed by personal saving. If the amount consumers want to spend on consumption exceeds the aggregate value of consumer goods and services at the prices for which they were made to sell, a change in one or both of these aggregates must occur to bring them to equality in the completed sale. Consumers may decide to save more than they had previously planned, or they may be forced to save more by their inability to induce producers to sell to them; producers may sell more by drawing down inventories, or they may sell the same amount of goods at a higher price, or they may sell the same amount of goods at the same price and turn away the customers whose wants they cannot satisfy. Ordinarily the way in which producers select between these alternatives, the effect of the nature of that selection on their future production plans, the effect of changes in production on consumer income, and, to close the circle, the effect of changed consumer income on effective consumer demand presents a very complicated chain of cause and effect which must be analyzed if the dynamics of changing national income is to be understood. We have developed a technique for an analysis of this sort on a monthly basis which will be presented in the final report.

But today, because consumer demand is not the dominant limiting factor in production, the current problem presents a special case which is for two reasons more readily analyzed than the usual situation: In the first place, the fact that the economic machine is straining at its job of turning out butter and bombs means that the wages, salaries, dividends, etc., distributed to consumers in the course of making the butter and bombs are far greater than the cost of the butter alone, even after consumers put aside some portion of their income for a rainy day. Moreover, because of the ceiling placed on the increase in that output by limitations of physical production and because of the urgency of

the demands for bombs, there is no chance for butter production to catch up with the amount that consumers would want to spend if they were permitted to keep all of their increased income. In the second place, the options that producers can exercise in the face of redundant purchasing power are materially limited by their inability to increase the physical quantity of goods offered for sale (temporarily by decreasing inventories and eventually by increasing production). This means that a rise in price is virtually the only way aggregate dollar demand can be absorbed; the chief practicable alternative is refusal to sell to some of their actual or potential customers.

The Approach

To estimate the volume of taxes or compulsory saving needed by any specified date to prevent rising prices three questions must be answered: What total amount of civilian production will our productive facilities and armament needs permit by that date? How will this total be distributed between groups (2) and (3), i.e. between consumer goods and services and private capital formation? What income after taxes in the hands of consumers will make them want to spend on consumer goods and services an amount equal to the value at present prices of the attainable output of such goods and services? The difference between the answer to this last question and the total income paid out by business and government in the course of producing armaments, consumer goods, and capital items is the total amount of taxes or compulsory saving that must be imposed if rising prices are to be avoided.

This statement of the problem purposely oversimplifies. The three basic questions are closely related to one another; in addition, the answers to them depend on the very result they are designed to yield, namely, the amount and kind of taxes needed. For example, what amount of consumption expenditures will be associated with any particular amount of income after taxes depends on the kinds

of taxes levied; consumption expenditures will be less if the taxes are paid primarily by very low income groups than if they are paid by high income groups, and so on. The interrelation of the three questions is exemplified by the dependence of the amount producers will want to add to their capital equipment on the way the increased armament output is obtained. This is discussed in more detail below, where the problem of diversion is considered. The manner in which these interrelations are taken into account is indicated in the following sections, which describe how we give quantitative answers to the questions posed. This description is in two parts -- first, in summary form, and then step by step.

General Description

As was noted above, the Federal Government will by next June be spending \$14 billion per year more on armaments than in June 1941. About \$6 billion of this \$14 billion increase will be drained off by the anticipated increase in tax receipts as a result both of the higher rates levied in the Revenue Act of 1941 and the higher level of business activity. There remains a flow of \$8 billion of purchasing power that will be exercising pressure on the price system. As we have seen, none of this can be matched by an increased flow of goods for civilian use. Indeed, even if the total flow of goods increases by as much as seems at all possible, namely, \$12 billion at June, 1941, prices (annual rate), the flow of goods for civilian use will have to decrease by \$2 billion if armament needs are to be satisfied. And if we can increase output by only \$9 billion, a not unlikely possibility, the flow of goods for civilian use will have to decrease by \$5 billion. If prices are not to rise, the streams of purchasing power which are now buying these quantities of goods must be sterilized.

To some extent the upward pressure on prices will be counteracted by forced reductions in consumption and private capital formation through the imposition of priorities; increased saving both by individuals, induced by the Treasury's savings bond campaign, and by corporations, out of the income received from government business; a somewhat lower level of capital formation because consumption will cease to rise; and a number of other less important factors. On the other hand, pressure in the opposite direction will be exerted by factors such as the need for new housing because of changes in the location of the population and for new types of capital because of changes in the composition of consumption, and the increased proportion of total income flowing to wage earners and other recipients of small incomes who ordinarily spend a large part of their income on consumption.

The net effect of these factors depends in considerable measure on the extent to which the armament needs can be satisfied by employing currently idle resources rather than diverting resources that are already being used for other purposes. If a relatively large amount of diversion is needed, the restrictive effect of priorities and unavailability of goods will be correspondingly severe, less capital formation will be required in view of the smaller change in the location of the population, but more because of changes in the composition of consumption. In this case, if there were no change in prices and consumer disposable income (i.e., income after taxes or compulsory saving achieved by obligatory purchase of government securities not redeemable until after the crisis), private capital formation would, by June, 1942, probably be running at an annual rate about \$1.8 billion below that of this June and consumption at an annual rate about \$400 million below this June. If diversion is relatively small, on the other hand, capital formation would probably decline by less than a billion dollars and consumption would rise by almost a billion. In both cases, something like a billion dollars of the increased government expenditures might be retained by corporations in the form of cash or investments and never paid to consumers.

The total upward pressure on prices will be least if there is relatively large diversion and, at the same time, the total flow of goods can be increased by \$12 billion, at June, 1941, prices. In this case, the \$2 billion necessary reduction in civilian output would come about automatically if prices and consumer disposable income were kept unchanged from the June, 1941, level. The \$8 billion excess purchasing power being distributed by the government would be offset by the reduction of something over \$2 billion in purchasing power distributed by others and by the \$1 billion increase in corporate retained income, leaving some \$5 billion as the net excess purchasing power. This is the annual

rate at which, by June, 1942, the government would have to be absorbing excess purchasing power through additional taxes or compulsory saving to keep prices from rising.

The greatest upward pressure will be exerted on prices if there is relatively little diversion and the total flow of goods can be increased by only \$9 billion at June, 1941, prices. In this case, if prices and consumer disposable income were kept constant, the decline in capital formation would about offset the rise in consumption. Consequently, no part of the \$5 billion reduction in civilian output will occur automatically and there will be no offset to the \$8 billion excess purchasing power being distributed to consumers other than the increased corporate retained income. In order to keep prices constant, the government will have to drain off not only the remaining \$7 billion excess purchasing power but also enough additional purchasing power to reduce expenditures by consumers and the producers of private capital goods by \$5 billion. In order to accomplish this end, about \$2 billion additional purchasing power would have to be drained off. No more than this would be necessary because, if the individuals from whom this money were withdrawn spent less, others would have smaller incomes and would in turn spend less, and with the decline in consumption, producers of private capital goods would add their mite by reducing their expenditures by more than has already been allowed for. In all, then, under the less favorable circumstances postulated, government receipts by June, 1942, will have to be at an annual rate \$9 billion higher than will be attained without additional measures, if the price rise is to be averted.

If no measures are taken to increase government receipts by the suggested amounts, a very substantial price rise is in prospect by June, 1942. Under the most favorable circumstances, the Federal Government and producers of private capital goods will be distributing some \$6 billion more in purchasing power

than they were this June. About \$2 billion of this \$5 billion might be absorbed by personal and corporate saving. The rest would be spent on consumer goods and services, thereby increasing the incomes of others who would in turn spend more than previously. Just what the total increase in consumers' spending would be it is difficult to specify, but it would almost surely be at least \$8 billion a year.

Last June, consumers were spending at an annual rate of about \$70 billion; next June, with no greater physical amount of goods and services available for purchase, they would be spending at an annual rate of at least \$78 billion. The result is that prices would be driven up about 10 per cent. In the face of so sharp a rise in consumer spending and hence in prices, expenditures on private capital goods would probably not decline by \$2 billion, but might instead actually rise. More than that, the government's own spending would presumably increase, since it would have to pay higher prices for the goods it purchased (its tax revenue would increase too, but probably not so much). The rise in the cost of living would strengthen existing tendencies toward wage increases, thus raising costs, and therefore prices, still higher. Hence, the cost of living would, in fact, have risen by much more than 10 per cent next June. To prevent this widespread rise in prices by direct price control alone would require a degree of rationing and price fixing that could be enforced only by policing on a totalitarian scale.

Our estimates of the amounts that the government must withdraw from consumer income to prevent such a price rise by fiscal measures are necessarily rough and rest heavily on personal judgment and none too well informed guesses. We have tried to keep these to a minimum and to express them in the form of a range rather than a single figure; but there is no escaping the intermixture of fact and judgment in any estimate for the future. Additional data that were

either not available to us, or that time-limitations made it impossible for us fully to exploit would enable the margin of error in our estimates to be somewhat reduced. Of even more importance, the estimates should be continually revised in the light of changing events so as to provide an up-to-date basis for policy decisions. Any forecast is bound to be in error, and the amounts involved are so large that errors could have serious consequences unless subject to fairly prompt correction.

Step by Step Analysis

The role that personal judgment plays in our estimates, and their susceptibility to periodic revision can perhaps best be indicated by supplementing the summary statement given above by a brief step by step description of our method. All money figures given in the course of this description are expressed as annual rates in billions of dollars. "Private capital formation" includes throughout state and local construction and capital goods ultimately destined for defense use but privately financed (that is, their cost does not appear directly, as such, in the official estimates of defense expenditures) as well as plant and equipment for private business use, inventory change, residential construction, and the net export balance.

1. Dates were selected as the beginning and terminal points for which estimates are to be obtained. We have used June, 1941, and June, 1942, in our detailed analysis. As soon as possible, similar estimates should be made for other intermediate dates.

2. Certain basic assumptions were made:

a. The progress of the war and America's relation to it will not have changed sufficiently by June, 1942, to alter fundamentally the size of the defense program, the state of public morale and the general international setting for domestic problems.

b. General price increases in consumer goods should be prevented, although adjustment in the price of specific commodities to facilitate transfer of resources may occur to some extent.

3. Probable increase in the physical output of the economy was estimated in accordance with the reasoning described on page 10. A range of 9 to 12 billion dollars in June, 1941, prices was selected as a reasonable one.

4. The probable increase in defense spending was set at \$14 billion on the basis of the October 5 Bureau of the Budget estimate that defense spending would be at an annual rate of \$24 billion in June, 1942, and Treasury figures indicating that defense spending in June, 1941, was at an annual rate of \$10 billion. Non-defense spending by the Federal Government was assumed to be the same in June, 1942, as in June, 1941. On these assumptions, the Federal Government will be adding \$14 billion more to the income stream in June, 1942, than it was in June, 1941. (In principle, some allowance should be made for expenditures on existing assets, since at least some part of these do not add to the income stream. However, this allowance is of no quantitative importance and can be neglected.)

5. An increase in defense expenditures of \$14 billion can only be achieved if both new and already employed resources are utilized in the defense program. The estimate of the extent to which resources currently employed elsewhere will be diverted to defense work must be based on very crude judgments involving criteria such as achievements during the past year, Bureau of Labor Statistics' estimates of the extent to which increased labor needed in defense industries will come from unemployed or new rather than now employed workers, the expansibility of the supply of certain crucial raw materials such as steel and aluminum and other non-ferrous metals, the plant bottlenecks in the machine tool and other machinery industries, the amount of priorities unemployment and the extent

to which the administration is willing to force the utilization of plants affected by it. Obviously, these judgments ought to be refined on the basis of an industry by industry analysis.

In view of the importance of the estimate of diversion and the crudeness of the information on which it must be based, we have expressed our estimate in the form of a range. This range, like all others that we use, is not made so wide as to include all possible values; rather, it is intended to be wide enough to include all the likely cases (something like the range between the first and third quartiles of a frequency distribution). As a minimum, we assume that diversion will amount to \$5.5 billion. This implies that there are \$8.5 billion of resources now idle but available and suitable for defense work. As a maximum, we assume that diversion will amount to \$9 billion, implying that the use of resources now idle will account for \$5 billion of the \$14 billion increase in defense output. On the basis of even slighter evidence than that on which this range is based, we have assumed that two-thirds of the diversion will come from the consumer goods industries and one-third from producer goods industries.

5. The diversion of resources to government use and the other changes in the economic picture that are clearly foreshadowed would lead to changes by June, 1942, in the expenditure patterns of both consumers and producers of private capital goods. These changes might either counteract or intensify the upward pressure on prices exerted by the increased government spending. In order to isolate these changes in expenditure patterns from the effect of increased government spending, we assume that consumer outlay is the same in June, 1942, as in June, 1941, in estimating the probable change in expenditures by the producers of private capital goods; and that consumer disposable income (income after taxes or forced saving) is the same, in estimating changes in consumer outlay. To the extent that these assumptions turn out to be incorrect, the estimates must be modified at a later stage.

7. Starting, then, with our preliminary assumption that consumer purchases at a steady price level will remain constant, we need to determine the probable change in private capital formation. The major variables taken into account are the disappearance of the increase in consumer outlay; changes in the relative importance of the production of different sorts of consumer goods; changes in the geographic location of industry and consumers; changes in the amount of privately financed plant expansion for defense (more precisely, whatever defense plant expansion is not included in the estimate in step 4 above); changes in the export balance; the incidence of diversion through priorities, allocation, or the bidding away of resources. Estimates were made of the impact of each of these variables on residential construction, inventory change, plant and equipment purchases, construction by state and local governments, and export balance. These estimates were sometimes in the form of a single figure, at other times, of a range. In all cases, separate estimates were made for the minimum and maximum diversion assumptions (step 5). For example, the estimates of the change in inventories that would be caused by shifts in the composition of consumption were made somewhat as follows: Inventories were increasing at a rate of about 3.0 billion dollars per year in June, 1941. Of this total perhaps a half, or \$1.5 billion, was in the consumer goods industries (a somewhat smaller proportion of inventories than of production, since government expenditures and capital formation increased faster and required, on the average, heavier inventories than the consumer goods fields). A change in the composition of consumption will imply a shift to fields in which inventories are relatively small -- services, perishable and semi-durable goods. The shift will be smaller under the minimum transfer assumption than under the maximum. In the light of our estimates of the amount of diversion, we evaluated the probable change in inventories of consumer's goods that would be caused by shifts in the composition of consumption

as .4 billion dollars under the minimum and .7 billion dollars under the maximum diversion assumption; i.e., the annual rate of increase would be smaller by these amounts in June, 1942, than in June, 1941.

Since many of the individual estimates are in the form of ranges, the aggregate of the estimates for all component items yields one range for the minimum diversion assumption and another range for the maximum diversion assumption. We have used the central points of these ranges as our final estimates. (Computing the final range by combining the minimum under one diversion assumption with the maximum under the other would clearly yield too wide a range since it would require the coincidence of extreme figures for all component items.) These estimates are that under the minimum diversion assumption, private capital formation would be \$.8 billion less in June, 1942, than in June, 1941, and under the maximum diversion assumption, \$1.8 billion less.

B. The estimates of probable change in consumer outlay if prices and consumer disposable income remain the same, like the estimates of probable change in capital formation, were made by evaluating the separate influence of the major factors affecting consumer spending. The factors taken into account are: change in cash anticipatory buying; change in installment purchases; increasing unavailability of goods because of diversion; the defense savings bond campaign and similar patriotic appeals to reduce consumption; a lead or lag in the adjustment of cash spending to changing incomes; changed distribution of consumer disposable income.

The effect of the last factor listed -- changed distribution of income -- depends greatly on the means taken to keep consumer disposable income constant in the face of expanded government spending. We have assumed that this will be done by means of taxes that will fall more heavily on the higher income groups (viz., those with incomes of more than \$1,500) than on the lower. Since a large

part of government expenditures takes the form of wages and salaries, this means that we anticipate substantially greater equality of consumer income after taxes in June, 1942, than in June, 1941. Further, it means that many individuals in the higher income groups will have smaller incomes after taxes next year than this. There may well be a tendency for some of these individuals to adjust their spending and saving pattern, in part at least, to their income before rather than after taxes. We have tried to take account of this tendency in our estimates.

In estimating the influence of unavailability of goods because of diversion of resources to the defense program, we have differentiated between installment and cash purchases, since it so happens that the kinds of goods that will be made unavailable are very largely purchased on installment. We assume that a reduction in installment purchases will involve little additional spending on other goods, but that, on the other hand, the bulk of the reduction in cash purchases will be reflected in increased spending on other goods.

According to our estimates, minimum diversion of resources to defense would mean an increase of \$0.8 billion in consumer outlay by June, 1942, if prices and consumer income after taxes or forced saving remain constant. Maximum diversion would mean a decline of \$0.4 billion.

9. The combined effect of the changes in capital formation and consumption estimated in the two preceding steps would be to leave total private spending unchanged under the minimum diversion assumption, since the decrease in capital formation (\$0.8 billion) would be matched by the increase in consumer outlay (\$0.8 billion), and to reduce total private spending by \$2.2 billion under the maximum diversion assumption (\$1.8 billion decrease in capital formation plus \$0.4 billion decrease in consumer outlay). In view of the small changes in consumer outlay we have not tried to take account of their repercussions on capital formation (see step 6).

10. Comparison of the maximum probable increase in physical output of \$12 billion (step 3) with estimated expansion in defense spending of \$14 billion (step 4) indicates that civilian output must be reduced by \$2 billion. With maximum diversion, slightly more than this decrease -- \$2.2 billion -- would be forthcoming without a reduction in consumer disposable income. In this case, a price rise would be forestalled if the amount of additional taxes (or forced saving) were sufficient to keep consumer disposable income constant. The amount of taxes needed for this purpose is estimated in step 11. With minimum diversion, none of the needed decrease in civilian output would be forthcoming without reducing consumer income after taxes. In this case, prevention of a price rise requires a reduction of consumer income after taxes by an amount sufficient to reduce private spending by \$2 billion. The amount of taxes needed for this purpose is estimated in step 12. Step 13 gives corresponding estimates for the smaller increase in total output of \$9 billion (step 5).

11. To keep consumer income after taxes constant, the whole \$14 billion increase in government spending must be offset by reduction in private spending, increased retention of profits by corporations, or increased taxes and compulsory saving. We saw in step 9 that \$2.2 billion would be offset by the reduction in private spending. Some part also would probably be offset by increased retention of profits by corporations. Although the heavy taxes in the Revenue Act of 1941 might tend to decrease business retained income, the accelerated tempo of business activity, in conjunction with the lag in dividend distributions and the tendency to set up high tax and other reserves, ought to increase it. Accordingly, we may, more for purposes of illustration than because we have any great confidence in the guess, assume that it remains the same on old business and is about 10% on new business, thus increasing by 10% of \$12 billion or, roughly, about \$1 billion. (The same estimate is used in the steps

that follow.) There remains about \$10.8 billion [$14 - (2.2 + 1)$] to be offset by increased taxes or forced saving. About \$5 billion of this will be forthcoming from existing taxes - this increase in the annual rate of tax receipts between June, 1941, and June, 1942, reflects both the higher level of business activity and the higher tax rates enacted in the Revenue Act of 1941. The rest - \$4.8 billion - is the amount of additional taxes or forced saving needed by June, 1942, to avert inflation if total output increases by \$12 billion and diversion of resources currently employed accounts for \$9 billion of the \$14 billion increase in defense spending.

12. If output increases by \$12 billion but there is only \$5.5 billion of diversion, private spending would remain the same if consumer disposable income remained the same. To keep consumer income the same would call for \$13 billion additional taxes or compulsory saving, since the only offset to the \$14 billion increase in government spending would be the increase in retained corporate profits. But this would not be enough to keep prices from rising. Enough additional taxes are needed to reduce private spending by \$2 billion.

To estimate how much more taxes would accomplish this end is a difficult problem. Increased taxes will reduce the spending of those who pay the tax; this will reduce the incomes of others who in turn will reduce their spending, and so on. Moreover, these reductions in consumer spending may lead producers of private capital goods to reduce their spending more than we have already allowed for. We have here the familiar multiplier process at work whereby successive withdrawals of income generate a larger total reduction of income than the initial reduction or successive respending of income generate a larger total addition to income than the initial addition. This process is, of course, at work at all times and with respect to all parts of the income stream. But we have heretofore been able to ignore it because we have been concerned with

keeping total income constant. As a very rough approximation of the multiplier relation we can assume that the government must withdraw from (or add to) the income stream about $1/2$ or $1/3$ of the desired decrease (or increase) in spending. The figure of $1/2$ would be precise if consumers reduced consumption by $2/3$ of any reduction in income (this is the proportion for 1941 levels of income suggested by Appendix C, Consumer Expenditures in the United States, National Resources Committee, 1939), if all indirect effects were encompassed, and if producers of capital goods did not change their spending in response to the reduction in consumer spending. Of course, not all indirect effects are encompassed since additional taxes would have been in effect only a fairly short time by June, 1942. However, this would probably be more than counterbalanced by the reduction in private capital formation. The figure of $1/3$ implies a sharper reaction on the part of the producers of private capital goods. If a sizable reduction in private spending were called for, the use of such a mechanical figure would be too crude to be acceptable. It would be preferable to try to estimate the reflex influence of the decline in consumption on capital formation directly -- somewhat along the lines of our analysis in step 7. Similarly, a more detailed analysis of consumer reaction would be needed. However, our problem is to reduce private spending by only \$2 billion; the possible error made by using the crude multiplier relation is too small to justify much additional effort. Applying the $1/2$ to $1/3$ range gives $\$2/3$ to \$1 billion as the additional taxes or compulsory saving needed to reduce private spending by \$2 billion. Total additional taxes or compulsory saving needed are therefore about \$14 billion, and taxes over and above the 1941 Revenue Act, \$8 billion.

13. If total output increases by only \$9 billion (instead of \$12 billion) by June, 1942, civilian output must decline by \$5 billion (instead of \$2 billion). The estimates of tax requirements in steps 11 and 12 must accordingly be

increased by enough to bring about an additional decline of \$3 billion in private spending. We may make the adjustment by the method used in the preceding paragraph -- namely, by using the crude multiplier relation -- though if the desired decrease in private spending were any larger, the related change in capital formation ought certainly to be estimated. Applying the $1/3$ to $1/2$ range used here gives 1 to $1\frac{1}{2}$ billion dollars as the additional taxes or compulsory saving needed to reduce private spending by an additional \$3 billion. The total amount needed over and above the Revenue Act of 1941 is about \$6 billion under the maximum diversion assumption and about \$9 billion under the minimum diversion assumption.

The accompanying table summarizes our estimates of the amount of taxes or compulsory saving over and above the Revenue Act of 1941 needed under alternative combinations of assumptions. The estimates in the tables are given to the nearest tenth of a billion, though in the text we have rounded them to billions.

Increase in Total Output at June, 1941, Prices	Amount of additional revenue needed with Diversion of	
	\$5.5 billion	\$9.0 billion
\$12 billion	4.8	8.0
9 billion	6.0	9.2

Selection of Appropriate Tax Measures

What measures of taxation or compulsory saving are available to take money from consumers in a quantity sufficient to avert inflation? How much choice is there in fact between taxation and compulsory saving or among various kinds of taxes?

Compulsory saving -- the obligatory purchase of government securities not redeemable until after the emergency -- has two advantages over taxation: first, it promises a future payment for present sacrifice and thereby enables a greater inducement to be offered to attract individuals to defense work; second, it can provide an automatic mechanism for distributing purchasing power when the driving force of the armament program ceases. Neither advantage seems sufficient to justify at this time the imposition of compulsory saving rather than taxation. Compulsory saving would mean as great present sacrifice of goods and services, and would further intensify the post-war problem of a large public debt. There is little reason to believe that the taxes which would repay the debt -- or even pay the interest on it -- would be any more progressive than those which can be levied now. Moreover, we are far from the point when a future reward will be the only inducement we can offer to secure greater exertion. As our previous analysis has shown, the defense program does not require a drastic restriction of consumption for the time being; it merely requires that consumption be kept slightly below the level of June, 1941 -- a level somewhat higher than any achieved during the preceding decade. At so high a level of consumption there is considerable room for offering greater inducements to some at the expense of the consumption of others. The second advantage of compulsory saving -- the automatic distribution of purchasing power after the crisis -- can be attained equally well by remitting certain types of taxes at that time. And both methods are probably inferior to others that could be adopted, since neither

Restrictions on consumption on the basis of need.

The time to collect the tax is now, when the government is adding large sums to the income stream through the defense program. The choice among various taxes probably narrows to three: some form of individual income taxation, a retail sales tax, and a sales tax on manufacturers of finished goods, i.e., goods ready for consumption.

A tax on "value added" by manufacturers, and possibly also wholesalers and retailers, is perhaps a fourth possibility, but the exemption of particular commodities like food would be impracticable under such a tax. An exemption of food would be necessary if it were desired to avoid a severe burden on those with very low incomes -- say, less than \$500 a year.

A tax on the sales of all products, including semi-finished and raw products, would favor the vertically integrated firm where the product passes from raw to finished state with no sales, and it would also favor some kinds of finished products, commonly produced with less processing and less marketing, over the rest.

A series of heavy excises -- production taxes or sales taxes on specific products -- could raise the necessary money only if (1) so many products were covered that the result was more nearly a general sales tax with exemptions, or (2) the rates on a few products were very high, resulting in widespread distress among the employees and investors of those few industries.

Direct property taxation is for all practical purposes forbidden the Federal Government under the constitutional clause that requires apportionment of such taxes among the states on the basis of population.

The taxation of corporate profits has some tendency to check inflation by removing one source of demands for increases in wages, although it also tends to lessen the employer's resistance to whatever demands are made. It does not check consumer spending enough to be of major significance for present purposes

since its only direct action is in decreasing the amount of dividends (but presumably not of interest) paid out. Also, a mere flat-rate addition to the corporate income tax is sure to weigh heavily on many small-income stockholders who are probably overburdened even by the current rate; hence the advantage from the viewpoint of equity would be at least doubtful. The undistributed profits of corporations present a pressing problem, but one too complex to be explored in this report. Taxation of the purchase of capital goods by business firms might be useful in lessening excess civilian drain on scarce materials, etc., that had slipped through S.P.A.B.'s allocation net, but the quantitative aspects of this problem seem unpredictable, at least in the present study. Hence, although we have by no means entirely ignored the possibility of utilizing further business taxation in an anti-inflation program, a variety of considerations has induced us to concentrate on the taxation of consumers as the overwhelming, if not the sole, element in such a program.

The Supplementary Personal Income Tax

Even individual income taxation would not be reasonably effective in checking the threatened inflation if it took the form simply of an addition to the rates of the existing individual income tax. This tax is collected only after a lag of about a year; income received in January-December, 1942 would result in tax payments only in March, June, September, and December, 1943 (with some exceptions). Unless a very heavy tax on 1941 incomes, additional to that imposed by the Revenue Act of 1941, were enacted, the \$5 billion to \$9 billion extra revenue that will be required by next June (annual rate) could not be obtained under traditional income tax methods. Two devices suggest themselves: quarterly prepayment on the estimated income of the current year; and collection at source. These techniques would not need to apply to the income tax as it stands in the Revenue Act of 1941 (hereafter called the "regular" income tax); they

would be necessary only for the supplementary tax designed to raise (as of June, 1942) \$5 billion to \$9 billion a year.

The quarterly prepayment method is the only one applicable to partnership and proprietorship income, including farm profits, and to rents and probably also royalties (so much rent is paid by a large number of small tenants). The Treasury would send each of these taxpayers a tax bill based on one-quarter of his preceding year's net income, and the taxpayer could, if he desired, pay instead on a return based on his actual income for the quarter. The regular annual return after the close of the year would allow adjustment for overpayments (refunds) or underpayments.

Perhaps neither this method nor collection at source would be successful in the case of domestic servants.

The choice between the two methods remains available, however, with respect to much the largest segment of the income stream -- wages and salaries in general, and interest and dividends.

Two considerations weight the balance heavily in favor of collection at the source: the probable necessity of changing the rate of the supplementary income tax before the calendar year 1942 is out, and the difficulty of inducing millions of small taxpayers to file quarterly returns on estimated quarterly 1942 income.

The rate would probably have to be changed because of the difficulty of forecasting the amount of taxation needed to check inflation. For example, it might be seen by September, 1942, that retail prices had risen by, say, 2 per cent or more a month in June, July, and August, despite the supplementary tax of 17 per cent suggested below; hence Congress might deem it imperative to step up the rate to 20 per cent or so for the October-December quarter. While such a changing of rates is no insuperable obstacle to the filing of quarterly returns

and quarterly prepayments on estimated 1942 income, it might result in considerable confusion and many errors in payment.

The task of inducing millions of small taxpayers to make quarterly prepayments is, however, self-evident and decisive. Even if they understood the requirements and were eager to fulfill them, they would in many cases find themselves without enough money to pay. Monthly prepayments or even weekly prepayments would be necessary, to get the money while the taxpayer still had it.

If personal exemptions and credit for dependents were to be granted under this supplementary tax, each taxpayer would have to file a return once a year, perhaps as part of his regular income tax return (in March, 1943, for example), to ascertain whether he was entitled to some refund because too much had been collected at source (during 1942). In some cases, too little might have been collected; the system can be set up, of course, either to result almost entirely in refunds, or almost entirely in supplementary payments, or in a mixture of both.

Those who had prepaid in 1942 on an estimated 1942 income would in any case have to file a correcting return in 1943. Moreover, if the quarterly rates had been changed during the year, the annual return could be made the occasion for applying to the whole year's income an average rate, granting refunds (or credits) against the regular tax for over-payments, with an additional tax for underpayments. This would avoid inequities due to taxing at different rates incomes arising in different parts of the year.

Some simplicity in administration and in compliance could be gained by eliminating deductions, personal exemptions and the credit for dependents. To raise the necessary \$5 billion or \$9 billion would require a rate of from 5 per cent to 10 per cent if no exemptions, credits and deductions whatsoever were allowed; and experience might soon show the need for a rate still higher. The

burden on those with very low incomes -- families with less than, say, \$800 or \$1,000 a year -- would be severe; and, for the purpose of checking inflation, not essential. The result would in our opinion be decidedly unfair, because the added tax burden would be so regressive. Moreover, entirely aside from the issue of unfairness, there is the productive power of the economy as a whole to consider. The restriction that would be forced in the consumption of the barest necessities would impair the productive powers of the working members of these lowest-income families and also increase demands on government and private sources for cash relief, free food, free medical service, and so on. Finally, it is not clear that there would be a net administrative advantage. The task of covering the millions of income recipients of less than \$500 a year would be huge. For these reasons, the present discussion assumes that personal exemptions and a credit for dependents would be allowed under the supplementary income tax.

How large might they be? Without committing ourselves finally on this point, we have made estimates of revenue on the basis of \$1,000 for married couples, \$500 for single persons, and \$300 for each dependent, chiefly because we happen to have available some data on tax base and number of taxpayers under these hypothetical provisions. These are the exemptions that will be assumed in the present discussion. If, however, much more than \$5 billions has to be raised by a supplementary income tax, exemptions of \$800 and \$400 (or thereabouts) and a credit of \$200 for each dependent might be considered.

The exemptions of the regular income tax, given the rate schedule of that tax under the Revenue Act of 1941, might or might not be reduced to the level of the supplementary tax. If they were, there would presumably be less need for actual refunds on the supplementary at-source and prepayment tax, since there would be a greater opportunity for subtracting from the regular income tax

otherwise due at the time of filing the annual return in March, 1943, inadvertent overpayments in 1942 on account of the supplementary tax. This device could in any case, of course, be used by those taxpayers who would pay something on the regular tax even if the exemptions and credit (for the regular tax) were left as high as they are in the Revenue Act of 1941. If the exemptions and credit were lowered for the regular tax, the revenue needed from the new tax would be somewhat less, but probably not enough to affect estimates to the nearest billion dollars. On the other hand, such a decrease in exemptions and credit would probably result in a somewhat less progressive rate structure for the income tax as a whole.

The allowance of deductions like interest paid, state and local taxes paid, professional or occupational expenses, and so on, to arrive at net income, under the source-collected and prepayment tax, would presumably be seriously needed for many types of taxpayer. Since it could not readily be taken into account in setting the amount to be deducted at the source, it would enhance the need for refunds, but only in those cases where the regular tax otherwise due was not large enough to absorb the overpayments that had been made on this account (plus the overpayments connected with the exemptions and credit). In the present discussion it is assumed that under the supplementary tax the same deductions are allowed as under the regular tax.

Could the rate of the supplementary tax be graduated? While it would not be impossible to do so, in view of the opportunity for correction in the annual return filed after the income year had ended, it would complicate matters somewhat. It would probably make advisable the deduction at source at varying rates. Not every employee, of course, would need to be accounted for at a different rate; indeed, if the rate-graduation brackets of income were fairly wide, most of an employer's deductions from payroll would be made at only two or three tax

rates. But the personal exemption minimum of \$500 itself introduces a factor of graduation.

In general, there is no urgent need for graduation in this supplementary part of the income tax. Indeed, in view of the high rate needed for this supplementary tax on the average -- say between 15 and 20 per cent -- its rate will have to become regressive at the high level of income if it, in combination with the regular income tax, is not to take more than 100 per cent of the taxpayer's income. Tentatively, we suggest introducing this feature by levying the supplementary rate, not on the net income (after exemptions and credits), but on that net income minus the regular tax payable on it. The withholding would be done at a flat uniform rate on income less pro-rated exemptions and dependent credit; the adjustment to place the tax on income less regular tax would be made in the annual return. If the result were deemed to be too regressive an addition to the tax structure, the rates of the regular income tax could be adjusted to counterbalance this regressivity.

Sales Taxes

How does a supplementary source-collected (and prepaid) income tax of this kind compare with a tax on the sale of finished manufactured goods, and a tax on retail sales? There are a considerable number of significant points on which these taxes are either bound to differ or might differ, but the points of chief importance are probably as follows:

1. The supplementary income tax would keep the retail price level lower than would the manufacturers sales tax. The income tax would keep a large part of the consumer's income from appearing on the retail market at all. The sales tax would not prevent it from appearing on the market (and hence pushing prices up higher than they would be under the supplementary income tax), but would absorb it after it had reached the manufacturer. The manufacturers sales tax

would, therefore, make the amount of income that the manufacturing firms will be able to pay out to stockholders, partners, and proprietors less than it would have been if no additional tax at all had been levied. Perhaps, indeed, some of these profits that would be present under a no-tax policy would cause increases in wages. In these respects the sales tax would keep the price level lower than it would be if no additional taxation of any sort were imposed. But the price level would still be higher than under a supplementary income tax. A more detailed analysis, to be submitted in the final report of the present study, will show further modifications to be made in this broad generalization, but the prospect as stated here is near enough to accuracy for the present purpose, i.e., for choosing among the major revenue possibilities.

2. The exemptions under the supplementary income tax make no allowance for differences in cost of living in various localities. A \$1,000 income means much less in a large metropolitan area than it does in a country town; generally, it means less in the northern United States, where fuel and clothing bills exceed those of the South. Some day it may be possible to vary the personal exemption and credit for dependents to allow for such differences; at the present, it is impracticable to do so. A manufacturers sales tax that exempts dwelling rental thereby automatically makes some allowance for regional differences in cost of living, for it is in dwelling rental that much of the difference is found. Over a period of decades the sales tax would raise the cost of dwelling accommodation unless building materials were exempted, but over the shorter period it would be virtually without direct effect.

3. Complete exemption of families and single persons with extremely low incomes is practicable under the supplementary income tax; but not under a manufacturers sales tax.

4. Millions of individuals would come into direct contact with the Federal Treasury through filing returns and claiming refunds or making additional payments under the supplementary income tax. This would create a mixture of civic consciousness and irritation. We estimate that under exemptions of \$1,000 and \$500, and with a \$300 credit for dependents (and with no earned income credit), the supplementary income tax would make at least 19,700,000 families and single individuals taxable; the total might well prove to be 10 per cent to 20 per cent higher. The sales tax would in general be paid by persons (business firms) who were already familiar with Federal taxation.

5. Many farmers escape the income tax because the cash personal exemption is set against an income that is in large part non-cash, and hence readily wipes out the remaining cash segment of the income. The sales tax, to be sure, fails to reach farm-produced, farm-consumed income, but its application to clothing and household supplies makes it at least somewhat effectual in places where the income tax is not.

6. To check consumption without allowing a rise in price, somewhat more tax revenue might be required under the supplementary income tax than under a sales tax if, as is commonly assumed, a larger proportion of the former would be paid out of savings than the latter. But both taxes, as here set up, are paid so largely by those with low incomes that it may be doubted that this difference is quantitatively important.

7. Administratively, there is probably not enough to choose between the two measures to influence the decision appreciably, in view of the far weightier issues involved. Both measures are practicable. It would probably be desirable to exempt manufacturers with less than, say, \$5,000 sales a year, in view of their large numbers and small total sales. Both measures would require new branches in the Internal Revenue Bureau. The income tax could not function well for low

incomes without a large number of local offices throughout the country where the puzzled taxpayer filling out his annual return could go for brief advice. The sales tax would necessitate a licensing system to prevent double taxation of a finished article sold to a wholesaler and resold to a manufacturer for sale by him, and, in general, would require either a great expansion of the division now handling manufacturers' excises, or a whole new division. An important point of definition, which influences the administrative task considerably, arises in the sales tax; are "finished goods" to include producers' goods, like machine tools? It is inconsistent to include them while excluding raw materials that enter into the finished product, but the inconsistency is found in virtually all tax laws here and abroad.

On most of these seven points a retail sales tax makes a considerably better showing than the manufacturers' sales tax, except that there would be more taxpayers to cover; exemption, either in law or in fact, would probably have to be granted to thousands of small retailers. The retail tax would be decidedly better if some plan could be devised for allowing complete exemption to all persons with incomes under, say, \$500, to all married couples with incomes under \$1,000, and to all dependents to the extent of \$300.¹ Such a plan has never been tried; but it might be workable if the taxpayer were given a book of coupons, up to the limit of his (or his family's) exemption, the coupons to be valid in payment of the tax by the retailer. We could not advocate such a device without far more study than we have been able to give to it, but it obviously deserves some consideration. If the retail tax were stated separately from the price, the price level as the consumer would view it might not furnish quite so much fuel for wage-increase demands as would a rise in prices under no tax or a manufacturers' sales tax (the comparison with the

1. We are indebted to Dr. Laszlo Eker-Racz for this suggestion.

supplementary income tax raises some complex questions). If rent were not taxed, the regional variations in cost of living would be taken somewhat into account. Farmers might be taxed somewhat more than under the income tax. On the other hand, use of retail sales tax by the Federal Government might meet with strong opposition from those states already using it for their own purposes. None of the state rates exceed 3 per cent. At least until the practicability of allowing personal exemptions and credits is thoroughly explored, and perhaps even then, our choice remains the supplementary income tax.

Rates Needed for the Supplementary Income Tax

How large a tax rate would be needed if the supplementary income tax alone were to be yielding, in June, 1942, from \$420 million to \$750 million, i.e., an annual rate of \$5 billion to \$9 billion? On the basis of a considerable amount of research that we were able to carry through in this field during the past two months, and which will be set forth in detail in our final report, we estimate that the taxable net income, after deductions and after personal exemptions and credit for dependents (but without any earned income credit) would amount to at least \$26.4 billion on calendar 1941 incomes. For 1942 incomes this figure could presumably be raised to about \$29 billion. No deduction needs to be made for evasion, unless the tax is administered less efficiently than the regular income tax has been, for the method of deriving the estimate allows, roughly, for whatever degree of underreporting (and non-reporting) has characterized the regular tax. Within the rough estimates used here, no allowance needs to be made for added cost of administration (the added cost, to set up local offices for advice to taxpayers, to handle refunds, and so on, would perhaps not exceed \$100 millions, or from about 1 per cent to 2 per cent of the added revenue).

Consequently, if new revenue at the rate of \$5 billion a year was needed, the rate would have to be $\frac{5}{29}$, or 17 per cent (only applicable, it will be

recalled, to the taxable income, that is, the part of the net income that is left after deductions and after the personal exemption and the credit for dependents.)

If \$9 billion were needed, the rate would have to be $\frac{9}{29}$, or 31 per cent of the taxable income. For general purposes we may use a central figure, \$7 billion, with the corresponding tax rate, on taxable income, of 24 per cent. Thus a married couple with no dependents and a net income (before exemptions and credit) of \$1,200 would pay (at the 24 per cent rate) \$48 in supplementary income tax. The husband, we may suppose for illustration, is receiving a monthly salary of \$110 and is paying out \$120 a year in interest and state and local taxes, and has no other deductions. He files with his employer a statement of family status, claiming \$1,000 a year exemption. This, divided by 12 months, gives \$83.33 a month to be applied as exemption against the \$110 salary, leaving \$26.67 to which the employer applies the 24 per cent rate in ascertaining how much to withhold and turn over to the government each month -- viz., \$6.40, or \$76.80 over the year. The following March, the couple file a return, showing \$1,320 income, less \$120 deductions, or \$1,200, minus a \$1,000 exemption, leaving \$200 taxable at 24 per cent, giving a tax of \$48. Against this is applied the \$76.80, showing an overpayment of \$28.80, which the government refunds (perhaps in defense stamps and savings bonds). If the exemption of the regular income tax has also been reduced to \$1,000 on 1942 incomes, while the rates have remained as in the Revenue Act of 1941, this married couple would deduct the \$28.80 overpayment from the regular tax otherwise due. This would be \$15.20, leaving a refund due of \$13.60. Under the device suggested above to avoid more than 100 per cent taxation in the higher ranges, the 24 per cent rate would, in the annual return submitted in March, 1943, be applied only to \$200 minus \$15.20 (regular tax), or \$184.80.

Not all the added \$5 billion to \$9 billion would have to come from the supplementary income tax. Some could be quite easily obtained by closing some of the existing loopholes in the income tax and the estate tax. Increases could be scattered around among the corporation taxes and customary excise taxes, though we doubt the wisdom of either of these. Special excises to help check consumption of materials and labor needed for defense may prove useful if priorities and allocation cannot for some reason or other do a comprehensive job on these points. Special taxes to recoup windfall profits of dealers in and producers of articles made scarce by priorities and allocation may prove advisable. But we are sure that all of them together would not eliminate the need for a new general tax like the supplementary individual income tax or a general sales tax, both because (i) the revenue requirements to prevent inflation, as we foresee them now, are so large and because (ii) the situation may change so rapidly, the errors of forecast may prove so considerable, and the necessity for correcting them promptly may be so great that there must be in operation by June, 1942, at the latest, (and preferably by January, 1942, as noted below) a powerful tax-raising instrument of a kind that will be capable of raising still more hundreds of millions a month by the quick action that a simple change in tax rate allows. Incidentally, it must be recalled that most of these other taxes would probably be less effective, per dollar of tax revenue, in checking consumption than would the supplementary income tax.

If \$5 billion to \$9 billion a year is needed by next June, something will surely be needed before then. Lack of time has prevented us from computing, for this preliminary report, data for a month earlier than June. We intend to submit a figure for January, and possibly other months, within a week or two. Meanwhile, we propose -- until something more precise is computed -- that the supplementary tax be imposed beginning with incomes of January, 1942; and that

the withholding rate for the first quarter be 13 per cent, and for the second quarter, 17 per cent.

In any case, the rates would be subject to change, not oftener than once a quarter, if either (a) continued research modified the forecast, (b) the rate was found in practice to be inadequate or too severe (as judged by the retail price index and other data).

Finally, it must be emphasized that the amounts of added tax revenue recommended in this report are minima, since considerations other than the checking of a substantial rise in the cost of living may suggest still more revenue, while it seems unlikely that there will be any other considerations that will suggest cutting down the revenue. An example of the former consideration is the danger that the country may find itself loaded with an unduly heavy interest charge for public debt after the emergency, or that the stock of money in the economy will be unduly large. The tax measures proposed in this report would not balance the budget: far from it. In June, 1942, the deficit would be running at least as high as in June, 1941, and probably higher.

APPENDIX A

RECENT RESEARCH BY OTHERS IN THE FIELD OF INFLATION AND FISCAL POLICY

The technique used in this report was developed only after a study of the work already done by others in the same field. It is to a considerable extent based on that work, since it must utilize much the same data and analysis. It differs, however, in that it pushes forward to a definite conclusion of "how much" and "when" and, in doing so, breaks the general problem down into a larger number of sub-problems that are analyzed separately.

With respect to the American scene, most of the work has gone on within various departments of the Federal Government and the results have not been published. Most of the products of this work have, however, been made available to the writers of the present report, on a confidential or semi-confidential basis. In a few instances the material was too confidential even for such a limited release; the chief instance is a "defense primer" composed by the Defense Economics Unit of the Office of Price Administration several months ago, containing, we understand, fairly specific suggestions on the amount of taxation that would be needed to avert inflation. But even if this report were to be made available now, it would probably not add much to the information we have gathered from other sources, and in any case the computations would need extensive revision.

The Finance Economics Unit of the Office of Price Administration developed, at about the same time, a suggestive technique for determining the amount of taxation needed, utilizing the device of successive approximations based on certain observed relations over the past few years between gross national product and "offsets to savings" (government deficit, private capital formation, and so on). It also utilizes certain other historical relations.

The Bureau of the Budget has developed recently a division of fiscal research which has been attacking the problem of refining and modifying the "inflationary gap" analysis utilized in the recent British White Paper Cmd. 6263 on sources of war finance. This analysis depends primarily on certain observed relations in recent years between increases in government deficit plus increases in new private investment, and increases in national income ("multiplier" analysis); but is so constructed as to permit account to be taken of modifications in these relations.

The "gap" and "multiplier" techniques have been analyzed carefully in two memoranda submitted a few weeks ago to the Defense Economics Unit of the Office of Price Administration by one of its consulting experts.

The Federal Reserve Board and the Treasury have, of course, been studying the general fiscal problem, but have not, so far as we are aware, produced memoranda along the particular lines described above.

Outside the Government, four studies have been made: the volume by Hart, Allen and others (Financing Defense), the article by Angell ("Taxation, Inflation, and the Defense Program," Review of Economic Statistics, Vol. XXIII, May, 1941, pp. 78-82), the volume by Seymour Harris (The Economics of American Defense) and the study by the National Bureau of Economic Research on the financing of defense. This last study will not be completed until some time in 1942, but mimeographed copies of the preliminary drafts of some of the chapters have been made available to the present writers. The Hart-Allen study develops a tax program in some detail, but the key point they make is that prediction on even the roughest basis should be eschewed, owing to its uncertainty, and the tax structure should be varied from time to time in accordance with what has happened to the cost-of-living index. Angell's analysis is limited to ascertaining the time by which a substantial rise in prices is likely to be under way, and .

does not offer a quantitatively specific taxing program. Harris' study covers the economics of defense in a comprehensive manner; the remarks on taxation, however, are not designed to formulate a particular program with specific timing. The National Bureau study has not yet progressed far enough to produce a particular technique of analysis for determining how much taxation is needed.

Abroad, the British White Paper referred to above, and comments on it by the London Economist, by Paish and by Kaldor are the chief examples known to the present writers of attempts to weigh the inflation problem in quantitative terms. Time and resources have not permitted an examination of the German and Italian literature. There seems to have been nothing significant in French.

Without exception, none of these studies (except possibly the "Defense Primer") has pushed its analysis far enough to give results definite enough for use by policy makers (legislators and top administrative officials). This reluctance or inability to carry through to a conclusion has existed partly because there has been no constant, inescapable pressure on any of these research groups to do so. In part, too, it reflects an uneasiness on the part of the research workers over the heavy dependence on historical relations between deficits and income, and so on, that their techniques necessitate. The times are so different now from 1935-39 that relations existing then may not exist at all today. The present project, while it has used these relations for purposes of checking its findings, has reached its conclusions chiefly by breaking the problem down into more manageable parts and studying each part in the light of current and prospective conditions.

APPENDIX B

ALGEBRAIC STATEMENT OF METHOD USED TO ESTIMATE TAXES NEEDED

- Let A = expected change in government spending between initial and terminal dates
- I = expected change in total output, at prices of the initial date
- $D = I - A$ = desired change in civilian output, i.e., in consumption plus private capital formation
- C = expected change in consumer outlay if prices and consumer disposable income (i.e., income after taxes and compulsory saving) remain the same
- F = expected change in private capital formation if prices remain the same and consumer outlay changes by C
- R = expected change in business retained profits and certain reserve accruals
- M = change in spending on consumption and private capital formation at terminal date associated with a change of \$1 in government deficit spending from the amount needed to keep consumer income the same
- T = change in receipts from taxes and forced savings needed to avert inflation
- t = expected change in receipts from taxes and forced savings under existing legislation
- $E = T - t$ = taxes needed in addition to those levied under existing legislation
- Then $(C + F)$ = change in government deficit spending that will keep consumer income the same (i.e., will be consistent with a change of $C + F$ in consumer outlay + private capital formation)
- $D - (C + F)$ = change in consumer outlay and private capital formation that must be brought about by changing consumer disposable income
- $$E = T - t = A - R + (C + F) - \frac{1}{M} [D - (C + F)] - t$$

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE October 21, 1941

TO Secretary Morgenthau
FROM Messrs. Sullivan and Morris
Subject: Calls "on the Hill" re "guaranteed issues", Monday afternoon, October 20.

Our first call was on Senator Barkley who was just a little concerned about the public's psychological reaction to the increase in the debt limit. He recognized the advantages of the saving in interest and a unified financing program but wished to think the matter over. He further said he would like to discuss this matter personally with Senators George (who he thought would be back by Wednesday, or Thursday, at the latest) Connally, and La Follette, and possibly one or two others.

At this point Senator McNary joined our discussion group. Senator McNary was entirely favorably disposed to the whole situation and said he would talk to Senator Taft.

Senator Barkley asked for a list of the outstanding obligations involved, and when they matured. It seemed to make considerable difference to him from a psychological point of view that the maturities were spread over a period of years and, therefore, that it was not a question of taking them all over in a lump sum right away. This list has been sent to Senator Barkley, as per Exhibit A, attached hereto.

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The next call was on House Speaker Rayburn. Representative McCormack was also present. Both of them seemed to think the proposal to take over the guaranteed issues was entirely logical and proper and that there would be no difficulty in justifying such action.

Speaker Rayburn and Representative McCormack then asked if there was any legislation so important that the Treasury felt the House should not recess between Thanksgiving and January 3rd. Mr. Sullivan said that in accordance with instructions from the Conference Committee, the Treasury was working on a bill covering the so-called administrative adjustments, most of which were purely of a technical and non-controversial matter, but that (also) in accordance with the Conference Committee's instructions, the bill would include such matters as the compulsory joint return of husband and wife. Speaker Rayburn said that it would take from three years to eternity (this last by implication) to pass any bill containing such a provision.

However, if these controversial features were left out and a bill containing only administrative adjustments were presented, it was then suggested that a sub-committee could probably be appointed to go over the matter and have a report ready by the beginning of 1942, and Mr. Sullivan was asked if he thought this would be satisfactory to the Treasury. In reply, Mr. Sullivan

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said he thought this would be quite a disappointment, even on the administrative matters, as the Treasury hoped to have all of these completely out of the way before the close of this year. He indicated that he would, of course, pass on to Secretary Morgenthau the opinions expressed on these matters by Messrs. Rayburn and McCormack.

D.A.M.
JRS

EXHIBIT A

My dear Senator Barkley:

The schedule you requested, covering the Governmental issues which Mr. Morris and I discussed with you yesterday afternoon, is enclosed herewith. You will note that the securities are listed chronologically, according to maturity or earliest call date, where one exists.

If there are any further data we can give you, please call on either of us, and we will be glad to supply it.

With many thanks for your help in this matter,
I am

Sincerely yours,

/s/ John L. Sullivan

John L. Sullivan,
Assistant Secretary.

Mr. Alben W. Barkley,
United States Senate.

Approximate Amounts Outstanding
as of October 20, 1941

(In millions of dollars)

Rate (%)	Dates to Call: (if any) and Maturity	RFC	HOLC	FFMC	CCC	USHA	Totals by Fiscal Periods
7/8	11/1/41)*	300					
1/4	11/1/41)					112	
1	11/15/41)				204		
7/8	1/15/42	310					
3	1/15/42-47			236			
2-3/4	3/1/42-47			103			
Current fiscal period ending June 30, 1942							1,265
1	7/1/42	276					
2-1/4	7/1/42-44		875				
7/8	10/15/42	320					
3/4	5/1/43				289		
Fiscal period July 1, 1942-June 30, 1943							1,760
1-1/8	7/15/43	324					
1-3/8	2/1/44					114	
3-1/4	3/15/44-64			95			
1	4/15/44	571					
3	5/1/44-52		779				
3	5/15/44-49			835			
Fiscal period July 1, 1943-June 30, 1944							2,718
1-1/8	2/15/45				412		
1-1/2	6/1/45-47		755				
Fiscal period July 1, 1944-June 30, 1945							1,167
Totals		2,101	2,409	1,269	905	226	6,910

* To follow normal procedure, refinancing plan should be announced not later than Thursday, October 23rd.

MEMORANDUM

October 21, 1941.

To: The Secretary
From: Mr. Sullivan

Upon receipt of your telephone call this morning, I phoned Mr. Doughton to inquire if I could drive him to the Capitol, thinking this would be a good opportunity for us to discuss the problem of covering the indirectly guaranteed Federal agency obligations into the National Debt. Mr. Doughton had left for the Hill so I immediately drove there. Enroute I saw Congressman William Boehne, and transferred to his car. Driving to the Capitol we discussed the problem and he was very much in favor of what you hope to do. Arriving on the Hill I interviewed Congressman Doughton who seemed to have some misgivings that the Republican Party would use this increase in the National Debt for political purposes in the coming campaign. I explained to him that by election time we would have taken over about a billion and a half of this amount. Eventually he concluded that he would be willing to "play along".

I then interviewed Congressman Treadway who said that he felt that on a matter of this kind he would have to be bound entirely by your recommendation. He said, "I can't agree that I will support any increase in the National Debt which may be proposed, but I can say to you that you will not be prejudiced in securing my vote for such an increase because of having covered these obligations over into the National Debt".

I then saw Congressman Jere Cooper who was very much in favor of your plan. My next visit was to Senator LaFollette who heartily endorsed your proposal. Senator Glass was not in and is not expected in today.

During my interview with Congressman Treadway, he stated that he thought Congressman Dan Reed would be opposed to covering these indirectly guaranteed Federal agency obligations into the National Debt. I decided not to see Mr. Reed because if I did there were many others on the Committee I would have to see.

JLS

October 21, 1941
10 a.m.

RF FINANCING

Present: Mr. Hadley
Mr. Sullivan
Mr. Piser
Mr. Morris
Mr. Haas
Mr. Murphy
Mr. Eccles
Mr. Bell

H.M.Jr: I have just talked with Sullivan, and he has been unable to reach the President. If I had a week it would be all right, but Bell says I have got to do it Thursday. Couldn't I wait until next Monday, Dan?

Bell: I just don't see how we have got time to print these things and get them out to the banks.

Eccles: Monday to Saturday. Saturday is the first, the due date, isn't it?

Bell: Yes, Saturday is the first. We would have to do all that work in a week. You see, you wouldn't get - you couldn't get it out before Tuesday. Monday afternoon you would send out word, and Tuesday you would open it.

Eccles: Send out word Saturday, and have them open Monday. You may have to.

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H.M.Jr: Yes, if we can't get it cleared. I am going to talk to Sullivan and I told John if he couldn't cover the Senate and the House today to let you (Bell) know and you would take care of the Senate side.

Bell: Has he made progress?

H.M.Jr: I don't know. He just called me up and asked me if I would call Barkley over at the White House and I said no, I wouldn't do that. Well, let's go on the assumption that I get the green light from the Hill. That is the purpose of the meeting this morning, you see, and that the President approves, you see. Then the question is, what are we going to do. Have you had time to consider it?

Eccles: Well, the only time I had was that Piser has been following this and he has written a memorandum on the thing which I had seen, but we have had no opportunity for any discussion of the thing at all, so that I can indicate here or he can indicate just what we have been thinking about, which is no doubt somewhat along the same lines you have been thinking about.

H.M.Jr: I wish you would.

Eccles: Do you want to do that, Piser? Go ahead.

Piser: Well, in regard to the type of issue, it seems to me that a long bond is out of the question, in view of the secondary distribution going on in the recent issue of two and a halves, and my own personal preference would be not to issue a short note, in view of the large maturities and the absence of open dates that you have up to about five years, so I should think it would be either a five year note or a intermediate bond, and

my personal preference would be for an intermediate bond, because I think even that type of issue would go about half to the banks, or say five hundred million to the banks.

(Mr. Hadley entered the conference).

If that five hundred million went to the banks it would leave them with approximately the same amount of issues as they have now, whereas I think --

H.M.Jr: Say that again, will you?

Piser: I figure that on an intermediate bond, say a '49 - '51, approximately five hundred million would go to commercial banks, which is about the amount that they hold in the three maturing guarantees. If it were a shorter issue, say a five year note, it seems to me that more would go to the banks, so it would be adding to the Government security holdings of banks.

H.M.Jr: We only figure a five hundred million dollar issue, total.

Piser: I thought you were going to raise cash in addition.

H.M.Jr: No.

Bell: Only in case we paid off part of the issue.

Piser: Oh, I didn't understand that.

H.M.Jr: It would be five hundred million the way it is now.

Bell: If you just refund, yes, five hundred million.

H.M.Jr: That is all I want to do now.

- Piser: I didn't understand it that way.
- H.M.Jr: Well, that is the purpose of these meetings. Five hundred.
- Bell: Well, what I told you was that what we would try to do, if we paid off half of it in cash, would be raise four hundred million dollars in cash. There is about three hundred sixty-seven million dollars to pay off in cash, which includes the hundred and twelve million of United States Housing Authority, and that is what I was trying to get the cash back for and reimburse us for that outgo.
- H.M.Jr: Well, I think I would keep it just as small as we can.
- Eccles: Are you thinking of giving rights? To what extent do you figure it? Is that what you want to discuss?
- H.M.Jr: Well, the way I feel is this: We checked up and we found that with the exception - that the only concern who is a large holder of those which have been sold is J.P.M. That was the only one.
- Eccles: Some of those fellows in Chicago - I happened to be over there on Wednesday, and I was over to the Fed and of course they knew I was - it was Thursday morning. I had been there Wednesday night, and had seen some of these bankers and they had tried to get me and I wouldn't talk to them. They were all up in the air about taking away rights. Sol Smith - you know Sol, Dan - what-is-his-name of the Harris Trust Company, and there was some other bank there had a lot of these and they were just about ready to have a fit, because they had understood - this

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feeler came out in the press that they were going to be paid off in cash.

- H.M.Jr: Well, my own feeling is, I haven't talked about it, that I don't see any particular reason to give these fellows a kick in the pants at this time. My inclination is to give them the right to convert. That is, the CCC and the RFC holders. The other fellows were on notice originally that there would be no rights.
- Eccles: Which is that?
- H.M.Jr: United States Housing.
- Eccles: Yes, you can't give them rights on that stuff. It is so terribly short.
- H.M.Jr: But on the CCC and the RFC - I mean, I have got to live with these fellows and I don't want to get them unnecessarily --
- Eccles: I think you have paved the way though, now, because I don't think they expect rights except for part of this.
- H.M.Jr: Well, as I say --
- Eccles: If you want to reduce the rights, I think you have got an excellent opportunity now.
- H.M.Jr: Well, they are down.
- Eccles: Clear down because --
- H.M.Jr: Well, they are down.
- Eccles: Nobody expects the full rights at this time.
- H.M.Jr: We can price the thing much closer, and that is

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why I want to keep it smaller and make it a small issue.

Eccles: There is this thought here. The RFC is going to need considerable cash between now and the end of the year, aren't they? About four hundred million, Dan.

Bell: Something like that, yes.

Eccles: Why not get that cash now for them? Here you have only got two months. I mean, November first, and they need it within sixty days. Why couldn't you at this time make this a billion issue, six hundred of it refunding and four hundred million cash? You wouldn't have a particle of trouble, if you want to put out a five year note or a short bond. I mean, it would be just as easy, I think, to put out your billion dollar --

H.M.Jr: It is awfully close.

Eccles: Yes, but it isn't close in that it is such an entirely different market.

H.M.Jr: But Marriner, for whatever it is worth, if I go out and raise nine hundred million dollars now, let's say for five years or ten years, I will get an awful panning.

Eccles: Why?

H.M.Jr: Oh, they will say we are going right back to the banks and the other thing is a failure.

Eccles: Well, six hundred million of it is refunding. I think if you said the six hundred is refunding and you are getting the four hundred million in anticipation of the RFC's requirements at the end of the year.

H.M.Jr:

Well, we had hoped to pick up some of that RFC money through bills.

Bell:

You see, we had in our original cash position six hundred fifty million dollars of short cash, five hundred for the RFC and a hundred and fifty million for United States Housing. Everybody expected that to go to the banks. That is one reason they argued against any short issue in your October financing because they said the banks will get all they want on the agency financing. You are taking over the agency financing and just have a refunding. When you do that, we are losing some money on our cash position. I think we will get by.

Eccles:

Well, I was thinking that your outlay is going to be so great that at any time in making a new issue you could get five hundred million, it tends to reduce the number of issues, and you certainly can use the cash. It did seem to me that a billion dollars would be just as easy here as six hundred million, and you have got a good reason for saying that you are getting the extra four now to take care of what will be the RFC requirements between now and the end of the year. Certainly either in a different year issue or in a short bond, the market is - would be very favorable, I think, in either one of those, and I don't believe you would find your banks taking - holding any more than they now hold when you got through with the thing.

You see, your banks hold practically all your six hundred million anyway, so you - when you finally got through with it, I would doubt if your banks would end up with any more than they have now got. If they did - this is what the banks may do. I know a lot of the banks

are still holding some of these long issues. I mean, there is just no place to go, and they have got some of those issues that they subscribe for. I think they would be more - they would be ready to shift from some of those into these if these were available.

- H.M.Jr: Could I just ask a question? How would you gentlemen price a March 15, '46, now how would you price that?
- Hadley: I would price it at one per cent.
- H.M.Jr: One?
- Hadley: A little over a half point premium. But I might be higher than the others.
- Eccles: Well, we had here - you had a September, '46. That is five years. It would make that October. One and a quarter coupon.
- H.M.Jr: I was thinking of March 15.
- Eccles: Oh. What have you got there, Piser? He has got it priced here for September.
- H.M.Jr: Well, our boys say one per cent.
- Eccles: Pretty thin, is it?
- Piser: I would say it ought to be one and an eighth. My yields are higher than the Treasury yields are on this.
- H.M.Jr: Our boys give it from eighteen to twenty-three thirty-seconds.
- Eccles: Maybe you fellows are figuring wrong, either one or the other of you.
- H.M.Jr: Go outside, Hadley, and call up Rouse and ask

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him how he would figure, will you, a March 15? Ask him how he would figure a March 15, please.

(Mr. Hadley left the conference).

Eccles: He is on his vacation.

H.M.Jr: No, he is there.

Eccles: Did he get back?

H.M.Jr: Yes.

Bell: He got back Monday.

Eccles: He was away last week, and I didn't know whether he got back or not.

H.M.Jr: Well, I will tell you. That is one of the reasons I want to get these darn RFC's and other things out of the way. I haven't caught my breath yet, and here I have got another issue.

Eccles: Well, it is going to be that way from here on.

H.M.Jr: Well, not if we can get this stuff out of the way. Then we oughtn't to have to do it more than six times a year. That is one of the things, to get this thing out of the way.

Eccles: You have RFC stuff next year, of course, coming in again.

H.M.Jr: Yes.

Eccles: Your HOLC and --

Bell: Well, HOLC is not until July, but you have got Federal Farm Mortgage of about forty million.

Eccles: Is it your idea, Henry, to cover HOLC as well as the Mortgage?

H.M.Jr: Well now, there is a legal question. Are they guaranteed?

Bell: Yes, sir. No legal question about it.

H.M.Jr: Oh, I was thinking of the Land Banks.

Bell: Federal Land Banks.

H.M.Jr: The answer to your question is "Yes".

Eccles: All of them, in other words?

H.M.Jr: The whole works.

Bell: Nothing in the market but Treasuries.

Eccles: Well, I think that certainly simplifies your problem. It ought to simplify the market problem tremendously.

H.M.Jr: Oh, sure.

Eccles: Well, if you just put out the six hundred --

H.M.Jr: It is only going to be five hundred.

Eccles: Yes. I see. You would pay in cash the United States Housing and give the rights for the RFC and the other. That would be a pleasant surprise to the market.

Bell: If you give them the rights?

Eccles: Yes.

Bell: It would now.

Eccles: They have --

- H.M.Jr: Nobody knows how I have thought. I have kept it very quiet because I didn't want to get it out and have them run the rights up on me, and then have them say - I would be right back where I was.
- Eccles: Well, of course you will be if you give them the rights.
- H.M.Jr: Well, not if we price this thing fairly close. They have had no warning. I can give them some warning next time. And New York says only give them the right to convert half. I think if you are going to do it, do it all or nothing. That is the way I feel. Half won't satisfy them.
- Morris: Well, if you give it all you can price it very close, and it comes out not too badly.
- H.M.Jr: That is right.
- Eccles: Well, you could give it all and price it closely or give half and not price it so closely.
- Haas: I am afraid pricing close will give you a thrill. It would give me one, pricing it close (laughter).
- Eccles: Well, a five year issue wouldn't. I wouldn't worry on a five year.
- Haas: Well, Marriner, take a look at what we are basing the price on.
- Bell: Did you see Murphy and George squirm in their seats?
- H.M.Jr: You squirm on one per cent, four and a half years?
- Murphy: It is apt to be close. I wouldn't have any

doubt about it going over but the top of our range of premium is twenty-three, and you couldn't go above that, and you have the result of it finally coming out better than their fondest expectations were a week ago.

Bell: Yes, originally.

H.M.Jr: How do you mean?

Murphy: Well, one, due in March 15, '46, we figure will sell at a range of eighteen to twenty-three. I think there is two thirds - all the chances are it will fall within that range. It might go up to twenty-six or seven. Now, the premium is only eighteen at the peak, when they expect a guarantee, so the result is that your rights crash to nothing, they come up part way, they dribble off, then they go way up, yet you shave that coupon to seven eighths and none of us would sleep.

H.M.Jr: Who is suggesting seven eighths?

Murphy: Well, no one, except that the one, you see - there is no --

H.M.Jr: You mean you will have a restless night at one? And at seven eighths you won't sleep at all?

Murphy: That is right.

Eccles: Well, no, as I get his point, it is that seven eighths is too close and one is too much of a premium.

Murphy: That is right.

H.M.Jr: Oh, one is too much?

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- Murphy: Yes, the chances are it will be too much. I wouldn't have any doubt about it going.
- Eccles: It would give you twenty-five thirty-seconds, he says, which is higher than they have ever been.
- Murphy: That is, it could be.
- H.M.Jr: Oh. How about June?
- Bell: Well, it wouldn't make a lot of difference, Mr. Secretary.
- H.M.Jr: How about June?
- Murphy: Well, I am a little disturbed on account of my friend Piser down here saying that we need a one and an eighth for March. Now, we go out to June with a one and I think it will go, that is what I think.
- H.M.Jr: It is a matter of mathematics.
- Haas: Well, it is judgment, Mr. Secretary.
- Bell: It is judgment and --

Eccles: You can't get it--

Bell: There is a hole in the market in that area. You see, we haven't got taxable notes out. We have only got these couple of issues out, and they are not very popular at that.

Haas: We are just guessing.

H.M.Jr: Piser thinks - how much leeway would there be on a March 15?

Piser: On a one percent?

H.M.Jr: Yes.

Piser: Well, I would price it about par.

H.M.Jr: Gee whiz!

Piser: I am out on a limb. Nobody agrees with me.

H.M.Jr: If you are right and I did it, we both would be. How about New York?

Piser: They agree more with Henry Murphy.

Bell: Mr. Secretary, I want to tell you that in March '46 there are four hundred eighty-nine million dollars of bonds, high coupon bonds, that are callable, and in June there are two issues, aggregating one billion eight hundred fifty million.

H.M.Jr: Well, but you didn't say that three - it is only four hundred eighty-nine million?

Bell: I said four eighty-nine, yes.

H.M.Jr: Oh, did he?

Bell: Yes.

Now, maybe--

H.M.Jr: That is another reason--

Bell: Another five hundred million on that would be nine hundred.

H.M.Jr: That is another reason for not making it any bigger. That wouldn't bother me, would it you?

Eccles: What is that?

H.M.Jr: That four hundred eighty-nine million could be called - there is a '46 - '56, three and three quarters, four hundred eighty-nine million, to be called on March 15.

Eccles: March 15, when?

Bell: '46.

Eccles: Oh, I wouldn't worry about that.

Bell: But you have got to assume that they will be called and therefore that is a maturity date.

Eccles: Yes, but I mean it is an option. You are not compelled to--

Bell: It is a high coupon.

H.M.Jr: Well, I wouldn't worry. You have drawn it to my attention. I won't be here.

Bell: You won't be here, I suppose that is the answer. (Laughter)

Eccles: You have got so many other problems in the meantime--

H.M.Jr: Let me just switch the conversation for one

minute, if I may. Supposing - this is what I want. Supposing Congress says to me, "Well, we don't want you to do it"?

- Eccles: Well, gosh, I am--
- H.M.Jr: Am I going to fly in the face of Congress?
- Bell: Not as long as you have taken it up with them.
- Eccles: What it would be, it would be Barkley and--
- H.M.Jr: I think George will be all right.
- Eccles: It would be those fellows that don't know anything about the problem, that is the trouble.
- H.M.Jr: Well, Walter George is the chairman. He isn't here, that is another thing. They are trying to get him on the phone.
- Eccles: Where is he?
- H.M.Jr: They are trying to call him on the phone.
- Eccles: You shouldn't have a bit of trouble with George, I wouldn't think.
- Listen, how does Jesse feel about this?
- H.M.Jr: Jesse is all right, because I told Jesse that I would charge him one percent for money that he gets as long as our rate stays at around two and a half, but as the public debt goes up, his rate will go up accordingly. You see?
- Eccles: That is one percent for five years. I mean, that is about the--

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- H.M.Jr: He first said, "Well, you can charge me whatever the five-year rate is," so I said, "No, I think what would be fair is if we charge you one percent and then have it key to the general public debt - if that goes up, we will up you a little bit." So he said, "That is entirely fair, and I will go along with you." See?
- Eccles: Well, I was thinking if Jesse feels all right about it--
- H.M.Jr: Isn't that what he said?
- Bell: Yes, that is what he said.
- H.M.Jr: Oh, yes, I called him first.
- Eccles: That you wouldn't have any trouble on the Hill. He could maybe help you on that. If, on the other hand, he didn't--
- H.M.Jr: Oh, no. Before I made my announcement, I talked to him, and the way he put it, he was in a very Jesse Jones-like manner. He said, "I will recommend to my boys that they accept it." (Laughter)
- (Mr. Hadley entered the conference.)
- Eccles: Did you laugh?
- H.M.Jr: Yes.
- Bell: What Jesse wants is the one percent. He doesn't care how he gets it.
- H.M.Jr: So I announced in my press conference that Mr. Jones was sympathetic to this, and he has been perfectly happy about it.
- Hadley: Mr. Rouse said that the yield on a March 15, '46, might run all the way from eighty up to

one hundred, and he would split the difference at ninety just as a rough guess, which would mean one percent at about par 14 or one and an eighth percent at 101.

H.M.Jr: Don't give me one and an eighth. What would be--

Hadley: About par 14. It might run higher.

H.M.Jr: But he puts it at a low of 14 and our boys put it at a low of 18.

Hadley: I have a low of 18.

H.M.Jr: Well--

Piser: You have a high, Murphy of--

Murphy: Twenty-three.

Eccles: And a low of what?

Murphy: Eighteen.

H.M.Jr: And Rouse is as low as forty?

Hadley: Yes. He says it might go much - the yield might go lower and the price might run up quite a bit, but that is a good guess right at the moment.

Murphy: Well, the top of his range, you say, is one percent, which is only par?

Hadley: Yes. Well, he says that is the two outside possibilities.

Murphy: Way outside.

H.M.Jr: Well, I think that when we get through here, these fellows ought to get together and get Rouse on the wire, don't you think so?

- Eccles: And kind of see where the difference is. It is judgment, I suppose. They have nothing to measure it with. Of course, they are trying to judge the market, aren't they, Piser?
- Haas: That is what makes it difficult to price it close and be sure after you have done it.
- H.M.Jr: Would you think a one percent, one and a half years is close?
- Haas: Well, sometimes, Mr. Secretary, we have points right on each side, and you have a great deal of confidence. You can say it will be within a few thirty-seconds. This one, there is too much judgment in it. Our bench marks are not certain.
- H.M.Jr: Well, how much off could I be as a low?
- Haas: Rouse says it might even go at par, but I don't think they will be that much off.
- Hadley: He says that is the statistical outside, but he says par fourteen would be a good figure.
- Eccles: I wouldn't personally worry at a one percent four and a half year issue.
- H.M.Jr: I wouldn't either.
- Haas: I wouldn't worry about it.
- H.M.Jr: Especially when it is all conversion.
- Haas: I wouldn't worry, but what if it turns out and they have quite a large premium? That is the worst that can happen.
- Eccles: Yes, but I mean that is giving them, of course,

more than they expect.

Mass: That is right, that is the worst they can have on that thing.

Eccles: But I think you have got to take that chance. I don't think you have got a possibility of dealing any more accurately - say par to eighteen-thirty seconds. How can you get any closer than that?

H.M.Jr: It is like the other day. We were talking, and I didn't have time to explain it to the President, and I just sent the thing over cold to him. We went out fifteen years beyond the last issue and the thing sold at a hundred and three. Well, it might just as well have sold at par. He said, "Well, how did it go to a hundred?" I said, "Well, Mr. President, I would a damn sight rather sit here and have it at a hundred and three than ninety-seven." We went out fifteen years. I mean, how can you guess it? You don't know. They sit here and tell you they are going to buy it and so forth and so on. If you had told me a year ago that these fellows would buy a thirty-one year two and a half percent bond, I wouldn't have believed it. They wouldn't have a year ago, either.

Eccles: No, they wouldn't have a year ago. But of course their accumulation of funds is such now that there is no other place to put them.

H.M.Jr: Say, this is a nice thing for bankers, four and a half year, one percent.

Eccles: Oh, the banks would be perfectly satisfied with it, because--

H.M.Jr: With no cash offer.

- Morris: Would it be stressing it too much to put it September 26?
- H.M.Jr: The way these fellows talk, yes, sir. I would keep it right at March.
- Bell: Mr. Secretary, if you announced today that you are going to allow exchange privileges and allow Bob Rouse to talk to the market on the basis of three to five years, tomorrow morning you can say what you ought to price it at.
- H.M.Jr: I can't do that, Dan. I can't say a word until I get word from the Hill. They will read it and they will say, "What is Morgenthau asking our advice for?"
- Bell: No, I mean you don't have to announce whether it will be a Treasury or a guaranteed issue.
- H.M.Jr: Oh!
- (The Secretary held an unrecorded telephone conversation with Mr. Sullivan.)
- Bell: So Doughton is playing along. What does that mean?
- Eccles: Making a concession. (Laughter)
- Bell: That sounds pretty good. You have got the House clear, and certainly there are a lot of people in the Senate that would like to see this. Byrd and--
- H.M.Jr: Dan, supposing I announce there are going to be rights. That doesn't help us any, does it?
- Haas: They would go up right away.

- H.M.Jr: Well, you would want that.
- Haas: Sure, that is all right.
- Eccles: That would give you an indication of how to price this, how it would go.
- H.M.Jr: But it wouldn't if they don't know whether they are going to convert into a Treasury issue or into a guaranteed issue.
- Eccles: Well, there is very little difference in a Treasury and a guaranteed.
- Hadley: There is quite a bit in that area. It would be quite a bit on the basis of rates.
- Eccles: How much?
- Hadley: Well, if they were going to get a five-year Treasury note or a five-year guaranteed issue, it would be more attractive on the basis of a Treasury note to some than it would be if it was a guaranteed issue. I think it would be better to get some indication of what rates they would put on an issue without giving them a leak on what you are going to do.
- Bell: The first question, of course, they are going to ask, Bob Rouse will say, "Well, are we going to get rights?"
- H.M.Jr: Well, I have kept my mouth shut. I think it is much better to be able to say, "Now, gentlemen, on Thursday we are going to give you the right to convert into a Treasury issue or into another guaranteed," give them a clean-cut statement. The market will adjust itself quickly.
- Eccles: You ought to get this thing cleared. If you

can get hold of George, then you will be able to get Barkley later.

- H.M.Jr: I will call Barkley myself.
- Eccles: If you get George and Barkley, I wouldn't care whether I got anybody else or not.
- Bell: Well, Vandenberg is already--
- H.M.Jr: Oh, Vandenberg is--
- Bell: He is enthusiastic about it.
- Eccles: He won't count so much.
- H.M.Jr: Well, he will when I come up to get the debt increased.
- Bell: He is on the Finance Committee.
- H.M.Jr: But he is for it.
- Eccles: But if you get Barkley - I wouldn't worry about going up before the Finance Committee to get the debt increased. There is nothing they can do. There is going to be no problem on that score. The main thing is, it would seem to me, to get leaders like Barkley and George so that they can't say that you did this without talking to the leaders, but if you can talk to Barkley and George, I would go ahead and announce it. I wouldn't wait to get anybody else unless you could get them with comparative ease. If you got those two, then why wait about seeing anybody else? You have got the chairman of the committee, and you have got the leader.
- H.M.Jr: Oh, if I have Barkley and George, I am not waiting for anybody else.

Eccles: You wouldn't get anybody else at all?

H.M.Jr: No, because I have got the Speaker and I have got McCormack and I have got Doughton.

Eccles: Well, don't you think you are going to be able to get those fellows before this afternoon?

H.M.Jr: Oh, yes.

Eccles: Well, then, you can announce it.

Bell: Then you could announce it. It would be a straight Treasury issue, and they would get rights, you could announce that.

H.M.Jr: And they would get rights, and it is going to be a note.

Bell: Then your problem is simplified, I think.

Eccles: Sure. Then tomorrow you can price it.

H.M.Jr: And you are all right about the four and a half or in that territory?

Eccles: I think a four-and-a-half year is all right. I wouldn't be afraid of the short bond, but if you were going to get more than the six hundred - for instance, if you were going to get four hundred million new money to finance the RFC to the end of the year, I would think that short bond would be a good thing to put out.

Bell: It may be tomorrow when we get this settled down in the markets, you can put out your one percent September.

Eccles: That is right.

- Bell: You will get ten or twelve thirty-seconds and it will be just right. It sells at par, doesn't it?
- Piser: Practically.
- Bell: It has been a little unpopular.
- Eccles: Keep the bills off the rest of the year, more or less indefinitely, another fifty million.
- Bell: The Secretary hasn't announced any policy on the bills, but assumed in our cash estimate that they will go right through the cycle of thirteen weeks.
- H.M.Jr: At least a hundred and fifty a week.
- Bell: To the end of the thirteen weeks. We will have to go there in order to get us our money back that we lose.
- Eccles: What I was asking was, that the fifty million bills, you would continue to put them out for how long, the thirteen-week period?
- H.M.Jr: Oh, yes, but I might increase them. I might go to two hundred.
- Bell: When we get to the end of November we may be short of cash and may have to increase it to two hundred.
- Eccles: You could do that very easily because you have got all the flexibility in the world in that bill market. You can pay them off if you find that you are financing into a long term field, depending upon what future developed in that field.
- H.M.Jr: That is the beauty of the thing. Unless you

fellows have some strong feeling, I would like to keep this to a straight refunding.

Eccles: I don't have any at all.

H.M.Jr: Piser?

Piser: No.

H.M.Jr: It makes it much simpler. For instance, supposing you added two hundred fifty million or two hundred million in cash. You would get the whole thing--

Eccles: I wouldn't do that. If I was going to get any cash on the thing, I would make this a billion dollar issue.

H.M.Jr: That I don't want.

Eccles: Six hundred million of it would - five hundred would be refunded, a hundred would be paid off and you would have four hundred cash which would finance your RFC to the end of the year. The only thought of the four hundred million cash plus the hundred million cash for refunding was to finance the RFC to the end of the year. I don't think there would be any question about being able to sell the issue, but I don't think it is important at all.

Piser: Mr. Secretary, what would you think of putting out an additional issue with the March 1943 notes?

H.M.Jr: That is what Sproul said in New York.

I can tell you the reason I don't do it. I would be glad to have you people know it. I think I have said it before, but I

am not sure. I would like very much not to sell any more issues under four or five years, and I will tell you why. Just as sure as I am sitting here, there will come a period in the next two or three years where we will be sitting and saying, "Do you think we can go as long as eighteen months?"

Now, therefore, I would like to get my issues out to four or five years and keep pushing them out so the inshore stuff will be free for the day when we get some bad news, which we will get, you see.

Eccles: Of course, you have got your bill market you would have--

H.M.Jr: See? We have had it before. We have talked, "Do you think we can go as long as eighteen months or two years?" That is why.

Eccles: Well, I don't believe you are right, but I think that under a war economy, if that is possible, then I think we have failed to completely control the money market to the extent that we can and should, to the extent that every other country is doing it. I mean, that is the way I feel.

H.M.Jr: Well, Marriner, I hope and pray I am wrong, but no one can criticize me for not selling any more issues that fall due in the next three or four years and keep that open against the day where we will have to use it. After all, you and I have been here going on our ninth years, and I think it has happened three or four times that we couldn't sell anything longer than a couple of years.

Eccles: Well, you have got a different situation. Now--

H.M.Jr: But it did happen, Marriner.

Eccles: It happened twice. It was in '34 when I was in Treasury here, September '34--

H.M.Jr: Well, you weren't here with me in November '33--

Eccles: No, that is right.

H.M.Jr: ... when I sold eleven months issues and that was as long as I could go. Wasn't it eleven months?

Bell: Yes. Eleven and thirteen months.

Eccles: The Federal was being pretty well handled by - I mean New York was handling the open market committee pretty largely. Now, you have got a very different situation.

H.M.Jr: True, but, Marriner, the worst that you or Piser can say is, "My God, Morgenthau is seeing things under the bed." Well, all right.

Bell: We may come to another scheme.

H.M.Jr: I wanted to explain to Piser exactly how I felt. I am not advertising it, that Morgenthau sees gloom ahead, but I just would like to keep - not place more than a three- or four-year period.

Eccles: I think we have got to think about this, too, in the planning of future financing, and that is that the Federal and the Treasury have got powers to control the situation, and if they haven't got them they had better get them. In the situation that you are going into you

just cannot leave yourself in the money thing any more than you can in your defense effort subject entirely to a private market interest. That is the way I look at it, and in studying what has happened everywhere else, the market is pretty well controlled.

- H.M.Jr: George is in Vienna, Georgia.
- Eccles: I thought he was from Atlanta. I never heard of Vienna. It must be a suburb out of Atlanta. Didn't he practice law - didn't he have a law office in Atlanta?
- Bell: I don't know.
- Eccles: I think so.
- H.M.Jr: Well, I feel this way. I will work on this all day, but I wish you people would think about it, see. Could I get you today?
- Eccles: Yes, I will be over there.
- H.M.Jr: Supposing I call up Sproul and Rouse now and talk to them.
- Eccles: Have you talked to Sproul or Rouse at all, Piser?
- Piser: No, I haven't.
- H.M.Jr: Let me talk to them while you are here.
- Piser: Rouse wasn't in.
- Eccles: In a market that is declining due to some adjustment you may favor, of course you can't sell and don't want to sell a long issue or even an intermediate issue. You want to use - if you have financing to do,

you want to do short financing and it is proper, of course, that you should during any period of adjustment, even though it may be an adjustment that you favor. People will not buy long issues or even intermediate issues in a market that is making some adjustment, even though it may be a pretty small adjustment. The long issues sell always, of course, and the intermediate issues, when a market is rising and is showing great strength, and we have been in that zone now for a long period.

H.M.Jr: That argument points up where?

Eccles: Well, it points up to the point that you made, that it is a good thing to have an opening for a short financing. I didn't want you to get - you might have gotten the impression from what I said here that we are going to have no period in which the bond market would do other than stay where it is or go up.

(Telephone conversation with Mr. Sproul and Mr. Rouse follows:)

(Telephone conversation with Senator George follows:)

October 21, 1941
10:47 a.m.

HMJr: You're on my loudspeaker, and besides my own people, Mr. Eccles and Mr. Piser are here.

Robert Rouse: Yeah.

HMJr: This is - we still haven't got the clearance from Congress to go ahead with this, you see, but I'm trying desperately to get it today.

R: That is to.....

HMJr: To sell Treasury issues.

R: To take the place of all guaranteed issues.

HMJr: That's right. But we have - we've cleared it with the House, but we've - Senator George is out of town and I'm trying to get him.

R: Yeah.

HMJr: This is the way I look at it, and I think - if Mr. Eccles could nod his head or not - I think he's perfectly happy about what I'm going to say. If not, he can get on the wire and talk to you himself.

We're thinking of a five hundred million Treasury four and a half year note - one per cent - and giving them, the present holders of RFC and Commodity Credit, full rights.

R: Yeah.

HMJr: That's the way I stand right now, and Mr. Eccles has a poker face, I don't know how he feels.

R: Any cash?

HMJr: No cash.

R: No cash at all.

HMJr: No.

R: Well, there's no question about your ability to do that. It would be a cinch. It will leave the market uncertain as to what is going to be the final policy on rights, of course, and I think it's desirable that that uncertainty be cleared up as soon as possible.

HMJr: Well, I don't know whether I can satisfy them right away.

R: No.

HMJr: But I certainly would within the next week or so when I really had time to - well, to go into it more fully.

R: Well, I'm - I was really talking in terms of the next week or so rather than today, if you were going to do this today.

HMJr: Well, we wouldn't do this now until Thursday morning.

R: No.

HMJr: You see? We'd announce this refunding Thursday morning.

R: Yeah.

HMJr: But as to the future policy - well, I want to talk to you people, I want to talk to the Board, I want to talk to my own people.

R: Yeah.

HMJr: And I just don't know.

R: Well, in the absence of any decision on rights, this issue looks good to me.

HMJr: It looks all right?

R: Yes.

HMJr: And I don't want - I've been very frank here.

I don't want to have these fellows say that - "Oh, why does Morgenthau have to do this to us? He could have given us a little notice," and so forth. And as far as money is concerned, out of pocket, the Treasury - I don't think the Treasury will be out of pocket a nickel; but I do think we might leave a couple of sore spots, and I just don't want to do that.

R: Well, in my discussions here, I got the impression that if you cut them off now, sharply, it certainly would leave some sore spots. If you gave them partial exchange privileges now and indication that they were going to be cut off in the future, they still wouldn't cheer about it, but they'd understand it and it would be a workable plan.

HMJr: Well, we think this over, if you give them half the rights, it's neither fish nor fowl.

R: Well, it's a form of notice which has some teeth in it, and allows them to readjust their position if that's necessary on the immediately maturing issues.

HMJr: Well, I could do that within a week or ten days.

R: Yes, you could.

HMJr: Now, I'm not - they can't say I'm wobbling, because I haven't said anything about rights.

R: No, you said you were studying the problem.

Operator: Hello.

HMJr: Yes.

Operator: I have a long-distance call.

HMJr: Tell them to wait. All right, go ahead.

Hello.

You'll have - I've got Walter George. Would you mind my talking to him a moment?

S: Not a bit.

October 21, 1941
10:53 a.m.

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Operator: Go ahead.

HMJr: Hello. Hello.

Operator: Hello, Senator George. Hello, Senator George.
Operator, put me.....

Operator #2: Disconnection.

Operator: Oh, I'm sorry. She says we were cut off.

HMJr: Oh.

Operator: Do you want to finish with the other conversation?

HMJr: Well no. I'll keep this open for Walter George.

Operator: All right.

HMJr: You'd better keep this open.

Operator: Right.

HMJr: I think I've finished on the other anyway.
Tell them I'll call them back a little later.

Operator: All right.

HMJr: Have you got Walter George?

Operator: I'll try again. I had him on there. We were out off right away.

Walter George: Yes.

HMJr: Walter George?

G: Yes.

HMJr: I hope I didn't disturb you.

G: Not at all, Henry. How are you?

HMJr: I'm fine. How are things down in that nice state of yours?

G: Well, it's rather quiet.

HMJr: Good.

G: Getting along very nicely.

HMJr: Walter, the reason for my calling you is this. Last week I sent up a sort of a trial balloon to see how the people would feel if from now on we only borrowed in the name of the Treasury and didn't borrow any more in the name of some of these other agencies like the RFC and Commodity Credit and Home Owner's Loan.

G: Yes.

HMJr: My trouble is this. The way it is now, for instance, I've got to borrow - do something seriously. I've got two issues coming due, and they keep coming due all the time; and with this tremendous financing I've got to do, I'd like to be in a position where I only borrow for the Treasury.

G: Yes.

HMJr: Now, if I only borrow for the Treasury, I can do it cheaper, and I'd only have to go to the market about every other month. Now, the disadvantage I want to point out to you is, that over a period of four or five years, I would increase the debt by about seven billion dollars of the Treasury.

G: Yes.

HMJr: And that would mean that I'd have to come up a little bit sooner to get the debt increased.

G: Yes.

HMJr: But with this war coming on, I'm trying to finance as well and as cheaply as I can; and everybody

in the Treasury and in the Federal Reserve, feels that we could do it better if we only were borrowing for the Treasury and for nobody else. Now, Jesse Jones is entirely satisfied to have me do his borrowing and lend it to him in time, you see.

G: Yes.

HMJr: Now, I've cleared it with the people in the House - everybody's - the Speaker and McCormack and Doughton - they're all satisfied to have me do this. But I didn't want to move without talking to you.

G: Well, Henry, it looks to me like it's a wise plan.

HMJr: Yes.

G: I saw your statement last week - I understood something about it.

HMJr: Yes.

G: And so far as I can see, it is a wise plan, and I'd be very glad to support you in it.

HMJr: Well, that would be very kind. Now, could I quote you to that extent to Senator Barkley?

G: Yes, you may.

HMJr: Well, thank you so much.

G: I'm coming on back tomorrow, anyway. I've got to get back up there because some of these things are coming up and I want to be there when they happen.

HMJr: Well, I was trying to get.....

G: How's that?

HMJr: I was trying to get a sort of a blessing today from you and Senator Barkley if I could, you see.

G: You can quote me to - just as I stated. It seems to me it's wise, and I'll be very happy to support you in that program.

HMJr: Well, thank you ever so much.

G: All right, Henry.

HMJr: Thank you.

G: All right, sir.

HMJr: Good-bye.

G: Good-bye.

- Eccles: There was no trouble there. He apparently was advised. He was familiar with it. He had read about it.
- Bell: He had read the statement.
- H.M.Jr: I don't know whether I was smart or dumb. I said it first in the paper, and then went to him, but I had a reason for doing it. I wanted to crack down on those damn rights when I did it.
- Eccles: Well, there is this thing. By going in the paper you found out what the market reaction was, and it seemed to me it is so favorable it made it easier for the Senators to approve.
- H.M.Jr: Morris, step outside and tell Dick Patterson I am going into another meeting at eleven, and I will step out and shake hands with him if he will be a little patient. He is chairman from New York of the Defense Savings Staff.
- Eccles: He used to be Assistant Secretary of Commerce.
- H.M.Jr: Excuse me.
- Eccles: You said you didn't know whether you were smart or dumb in announcing the thing first. I think it was the smart thing to do because it made it easier to get the approval of these people on the Hill when they found out that the market acted favorably than would have been the case if they hadn't known how the market would react.
- H.M.Jr: I did it a little differently. Usually I ask them first and then go to the press afterward.
- (Mr. Sullivan entered the conference.)

H.M.Jr: Come in. We are all waiting with our tongues hanging out. Are you all right with Doughton?

Sullivan: Yes. He had some reservations entirely political. He was afraid the other fellows would use that in the coming campaign as indicating the extent to which the national debt--

H.M.Jr: Who?

Sullivan: The Republicans would use it.

H.M.Jr: Who said this?

Sullivan: This is Doughton. I explained that we were taking them over as they matured and it would take five years for the full amount to mature, and that probably we would not have taken them much over a billion and a half by the time the next campaign rolled around, and he agreed to play along.

Treadway said that he felt that in a matter of this kind, in an emergency such as this, he would have to be bound entirely by your recommendation. He said, "I don't want you to interpret this as my agreeing to support any kind of an increase in the debt limit that may be proposed, but I can promise you that your proposal will not be prejudiced because of having done this."

I then saw Jere Cooper, who was very much in favor of it. On the way up to see Mr. Doughton I saw Congressman Boehne, also of House Ways and Means, driving by. I stopped him and got into his car and rode up with him, and he was in favor. Bob LaFollette didn't take a minute to make up his mind. He thought it was obviously the thing to do.

Senator Glass was not in and they called his home and he is not coming in today.

H.M.Jr: Well, I would forget about him.

Sullivan: Now, you recall that Speaker Rayburn and John McCormack were entirely in favor of it; so, too, was Senator McNary. Senator McNary was to talk with some of his men and report to Senator Barkley today. I was to hear from Senator Barkley after he had seen Senator George. Senator Barkley appeared to be in favor of it, but wanted time to talk it over with the others.

H.M.Jr: Well, why don't I leave a call for Barkley myself as long as I spoke to George?

Sullivan: I think that would be well, because I told him we had until Thursday, you see. I didn't know about this meeting today. For the record, Senator Vandenberg had already whole-heartedly indorsed this.

H.M.Jr: Well, Marriner, as soon as I get to Barkley, then I will get to the President.

Dan, give me a little memo along these lines for the President in case he questions me, how long it will take before this thing--

Bell: Sure.

H.M.Jr: Supposing he asks me the question, "Well, Henry, at this rate, how much sooner would you have to get the debt increased? Would you do it right away?"

Bell: Yes.

H.M.Jr: I think we are all right for the moment.

October 21, 1941
11:05 a.m.

Roswell
Magill: Henry?

HMJr: Yes.

M: How are you? This is Roswell Magill.

HMJr: I'm all right. How are you?

M: Oh, much the same. Did you get my letter?

HMJr: No.

M: Well, I talked to John Sullivan yesterday. He asked me to come down, as I take it you know, and I merely was calling on your behalf.

HMJr: Yes.

M: And I wrote you last night along these lines, that I can't very well come tomorrow because I've got classes here.

HMJr: Yes.

M: This eye business of mine is still persisting, so that I'm really greatly handicapped in my work.

HMJr: Oh.

M: I can't read during the day to amount to anything.

HMJr: Oh, I'm sorry.

M: Now, so that if it's - I wouldn't want to undertake to come down there and stay any length of time simply because it's - I'm having too much difficulty in carrying my ordinary work, if you follow me.

HMJr: Well, then, why not let it go over until next - next week. Would next week be any better?

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M: The - well, my class is here regularly Monday, Tuesday, and Wednesday. Now, what I would say is this. If I could come down and give you any help on a day or two, why I would be very glad to do it.

HMJr: No.

M: You know that. I'm anxious to do what I can.

HMJr: Well, a day or two right now wouldn't help much. It might a little later.

M: Yeah. Well, I don't think I ought to undertake much more than that, Henry.

HMJr: Well, why not give us a day or two?

M: That I'd be glad to do.

HMJr: What day could you come?

M: Well, most - whatever you say.

HMJr: Thursday?

M: I can come Thursday, if you'd like.

HMJr: Good.

M: Of this week.

HMJr: That'll be fine.

M: All right. Well, I'll be down there Thursday.

HMJr: Thank you.

M: I wish you'd make what use of me you can. I'm sorry I'm not available for a longer time, but you see how it is.

HMJr: All right.

M: Thanks very much.

HMJr: Thank you.

M: Good-bye.

October 21, 1941
1:18 p.m.

Grace
Tully: Hello.

HMJr: Yes.

T: Mr. Secretary?

HMJr: Yes.

T: Okay on your proposal.

HMJr: Listen, I still say that you're wasted over there.

T: (Laughs)

HMJr: All right.

T: All right, sir.

HMJr: Ever so much obliged.

T: You're welcome.

HMJr: Good-bye.

T: Good-bye.

October 21, 1941
2:45 p.m.

HMJr: Hello. Jesse?

Jesse
Jones: Yeah.

HMJr: We're all set to go on this financing. I sounded out the leaders in the Senate and the House as to issuing Treasury obligations and gradually pulling your stuff in and the other boys, and I've cleared it with the President. Hello.

J: Yeah.

HMJr: So I think what we'll do Thursday is, we'll offer five hundred million of Treasury notes and give the RFC and the Commodity Credit fellows a chance to convert into this, you see?

J: Yeah.

HMJr: We're going to give them the rights.

J: Yeah.

HMJr: And I'll sell something between a four and five year Treasury note.

J: I see.

HMJr: Now, is that all right?

J: Perfectly fine. I talked to our boys about it, and they all are agreeable.

HMJr: They're all agreeable.

J: After our talk the other day I discussed it with them, and they're perfectly happy about it.

HMJr: Did you have any trouble convincing them?

J: Not the slightest.

HMJr: Wonderful.

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J: Not the slightest. I told them I had assured you we were willing to cooperate and so forth and so on, and that you had agreed to - had stated what you would do on certain lines.

HMJr: That's right.

J: So that's all right.

HMJr: Thank you, Jesse.

J: Thank you.

October 21, 1941
2:45 p.m.

RE FINANCING

Present: Mr. Bell
Mr. Morris
Mr. Murphy
Mr. Haas
Mr. Hadley
Mr. Schwarz
Mrs. Klotz

H.M.Jr: I talked to the President and Barkley and Jesse Jones. I haven't said anything to Commodity Credit. Have you said anything to them?

Bell: Yes, they are all right. So is Federal Housing.

H.M.Jr: You (Schwarz) tell the boys that Thursday morning we will offer - is it five hundred million?

Bell: Thereabouts. You can say five hundred million or thereabouts.

H.M.Jr: Five hundred million or thereabouts of a long term note for conversion from the RFC note and the Commodity Credit.

Schwarz: The RFC seven eighths and Commodity Credit one?

H.M.Jr: RFC is seven eighths, three hundred million, and the CCC is one per cent, two hundred and four.

Schwarz: All right.

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H.M.Jr: Now, wait a second. Now, paragraph.

At some time during the next week or two I will clear up the question as to the future status of rights.

Schwarz: O.K.

Bell: All rights? Rights on directs as well as --

H.M.Jr: Yes.

Haas: Do you have to commit yourself on that?

H.M.Jr: No.

Haas: Not seeing --

H.M.Jr: I don't want them to think that this thing, you see --

Schwarz: This is pressing.

H.M.Jr: Why not simply say during the next week or two I will go into this whole question of rights?

Bell: If you want to say that, that is all right, but I am wondering if you need to say it.

H.M.Jr: Well, if I don't say it, that makes them think that they are always going to have the rights. This is the time to say something.

Haas: I guess so.

Morris: Would you want to say rights on guaranteed issues?

H.M.Jr: Well, that is worse.

Schwarz: Then you leave open the question of directs.

Bell: It keeps the market a little disturbed during the time you are having to finance.

H.M.Jr: Supposing I say the rights on guaranteed issues?

Bell: That would narrow it.

Murphy: It seems to me instead of keeping open the question of rights, I would tend to close the question on the directs. The market would tend to infer that the rights on directs would continue as heretofore.

H.M.Jr: But not if I say this.

Murphy: Not if you say on rights in general, but if you said rights on guaranteed issues, it would seem to me that the market would suppose that the rights on directs would continue as heretofore.

Bell: That is what Dan was trying to convey.

H.M.Jr: Supposing I just say this, that at an early date I will dispose of the question of rights as they affect - as they pertain to guaranteed issues. Then I don't commit myself on Treasuries. That leaves it open for me to say from now on there won't be any rights or there will be, or there will be partial rights.

Murphy: I wouldn't take it that way. This is a matter of interpretation. If you say now that you expect in several weeks to clear up the matter of rights on guaranteed issues and then if say ten days from now you made an announcement that applied both to guaranteed and Treasuries, it seems to me that a person who had bought Treasuries during the meantime might have some ground for complaint because the fact that you confined your statement to guaranteed

would create some presumption that Treasuries would continue as they have always been.

Bell: I thought you told Sproul the other day of your announcement that you had reference only to guaranteed issues and not to the direct, that he let that seep around.

H.M.Jr: Well, of course, I have never said anything about rights.

Haas: No.

Hadley: Why couldn't you just say you are going to make a statement about rights?

H.M.Jr: No, say nothing.

Bell: That would suit me a lot better.

Haas: I would be inclined to say nothing.

Schwarz: If there is doubt, leave it open.

Haas: What you might do, Mr. Secretary - you don't have many alternatives, and after seeing the alternatives you might decide you don't want to do anything.

(The Secretary held a telephone conversation with Mr. Sproul as follows:)

October 21, 1941
2:50 p.m.

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HMJr: Are you gents there?

Robert
Rouse: We're both here.

Allan
Sproul: Yes, sir.

HMJr: Well, I've finally cleared everything on the Hill with all Democratic and Republican leaders and with the President of the United States, so I'm ready to go.

S: Well, that's fine.

HMJr: Now, what I thought I would do is this, that I would tell my press man to tell the newspaper boys for immediate release, that Thursday morning we were going to offer five hundred million dollars of a long Treasury note.....

S: Yeah.

HMJr:and that the RFC and Commodity Credit would have a right to convert.....

S: Yeah.

HMJr:and that at a later date I would discuss the question of future rights.

S: I think that takes care of it.

HMJr: See?

S: Yeah.

HMJr: See, at a later date. Sometime within the next week or two I would try to clear up this whole question about rights.

S: I think that takes care of it, and I think that note issue - if you're still thinking of doing the four and a half year one that you mentioned this morning - is all right in that

setting as an issue which preserves the status quo while you are determining what you're going to do in the future on guarantees and rights.

HMJr: Now what do you mean by that?

S: I mean by that it gives them the - give the market something of the kind of an obligation it wants with full right privilege, and leaves them, I think, very well satisfied until there has been a determination of the final question of rights and guarantees.

HMJr: Yes. Well, now what the people think here is that if I announce this, that that will kind of let us estimate the thing better tomorrow. Is that right?

S: You mean the term and the.....

HMJr: Yes. I mean it - just that note in that section.

S: Do you want us to have any talks with anyone about that, either this afternoon or tomorrow - preferably after you've made that announcement?

HMJr: Preferably this afternoon.

S: All right. We could see two or three of the banks which are large holders of the maturing notes and some of the dealers.

HMJr: Now are you perfectly happy about a note in that area?

S: Yes, I am, and - that is - agreeing or taking the situation as it is, if we're not ready to decide these more difficult questions, I think it's a good note and will go well.

HMJr: Oh. All right. Well, I'll have it out on the wire in a few minutes.

S: All right; and we'll go right ahead and talk to some people here in the market about what

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kind of an issue might.....

HMJr: Now, a long note - I don't have to say between four and five. I could just say a long note, can't I?

S: Yes, I think so.

HMJr: Right. I mean, a long note can't be longer than five years.

S: No, they'll consider that four or five years so it will blanket the kind of an issue you have in mind very nicely.

HMJr: Righto.

S: All right. We'll go right to work.

HMJr: Thank you.

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- Schwartz: O.K. then, we will just limit it to --
- H.V.Jr: Now, sending this fellow to see Senator Hughes, he found I told the truth. You see, Barkley had seen Hughes and Hughes had told him that I said it was no Senator's business whom I appointed in the State of Delaware, that I would appoint anybody I wanted, and I wasn't going to let politics enter into this. Barkley says, "Here is this fellow that is the head of this thing that is going to run against this man a year from now. You have no right to appoint him." I said, "Did he tell you I said that? It just isn't true." I called him up and told him that as long as that is what he wanted, the fellow fortunately had heart trouble and he couldn't take the thing anyway. But you see, this thing - I am holding you on purpose. I don't want you to get out of here until three o'clock. I know just what I am doing, Chick (laughter). In a minute you can go. The thing hadn't caught. He had heard the first story, but he hadn't heard I had taken care of it. He went back, talked to him, saw that I had told the truth, and the thing went through.
- Kletz: It is marvelous that you always tell the truth.
- H.V.Jr: I never get caught not telling it. It works both ways.
- Pell: I thought he was very happy at the conversation you had with him the other day.
- H.V.Jr: Who?
- Pell: Hughes.
- H.V.Jr: Yes, but Barkley hadn't gotten the second story. He had gotten the first one before I had taken care of the thing. All right, gents.

October 21, 1941
2:56 p.m.

HMJr: Hello.

Allan
Sproul: Hello.

HMJr: Allan.....

S: Yes.

HMJr:my boys here think that I oughtn't to say anything about rights at this time. I haven't said anything. Just say nothing. Just have this announcement.

S: Well, you have said that you were studying the question of converting all guaranteeds into directs, and that has raised in the market the question of what was going to be done about rights.

HMJr: Yeah, but I haven't said anything publicly.

S: No.

HMJr: Now, supposing we give out this announcement and I say nothing. Now, I have a press conference Thursday and they can ask me. The boys are a little bit afraid that I tie my hands. You see, it's the newspapers that are carrying on this discussion. I haven't said anything.

S: No. I think that would be a better procedure in this official announcement of the - this offering - to say nothing about it, but to answer questions if they're asked at your conference Thursday. I think that would be better.

HMJr: Well, that's what they think around here.

S: I think that that would be a better procedure. Otherwise, you'd be dragging it in for the first time yourself in an official statement.

- 2 -

HMJr: It's just because - you see, the trouble is, you and I should never read a newspaper.

S: That's right. (Laughs)

HMJr: It gets us all muddled.

S: Sure.

HMJr: Okay?

S: I think that's right. I think that's a better procedure.

HMJr: All right. Everybody's satisfied.

S: All right.

HMJr: Hello.

S: Yes.

HMJr: You'll never know how far out on the end of the limb I was on this.

S: (Laughs) Well, I sort of gathered that you felt you were out there.

HMJr: Well, I had to settle a couple of patronage questions before these fellows would say yes.

S: (Laughs) Well, I'm glad that I don't have to do that.

HMJr: Well, you'd be surprised.

S: How far down it goes.

HMJr: Oh, yes. An eighteen hundred dollar clerk often settles the future of the nation.

S: (Laughs)

HMJr: And I'm not joking, either.

S: No, I know you're not.

HMJr: Yeah.

S: Well, it's.....

HMJr: Anyway.....

S:it's the way things are done, and you have to conform.

HMJr:I got my way and I didn't give up my shirt.

S: Well, that's all you can ask for. I think that's an accomplishment.

HMJr: All right. Good-bye.

S: All right. Good-bye.



THE SECRETARY OF THE TREASURY
WASHINGTON

TO THE PRESIDENT:

The present method of financing governmental corporations and credit agencies of the Government by issuing guaranteed obligations of the United States, is making our financing more complicated as time goes on, especially in view of the large Treasury financing requirements made necessary by the defense program. The maturities of these guaranteed obligations now usually fall between the Treasury's quarterly financing dates, but the Treasury's own financing program is now getting so heavy that we will hereafter be in the market more often than on the quarterly dates. From a practical standpoint, it means, therefore, that the Government will be under the present system in the market almost every month unless the two programs can be coordinated and simplified. I believe that the present methods can be changed so that the Treasury will not be in the market more often than once every other month, for its own account and that of the agencies.

With this in mind, I hope to be able eventually to eliminate entirely from the market all guaranteed issues by taking them up with direct Treasury issues. The guaranteed issues are now selling on the market to yield 1/8% to 1/4% more than the Treasury issues of comparable maturities. Because of this I believe that the Treasury, if it does all of the financing through the sale of direct Treasury obligations, would save money in total interest charges.

We have talked to the leaders of both parties in both Houses of Congress and have found that there is universal approval of this proposal.

There is set out below a table of the outstanding guaranteed issues maturing in the next four fiscal years:

Fiscal Year (Maturity or earliest call date)	E.F.C.	C.C.C.	U.S.H.A.	F.F.N.C.	HOLC	Total
1942	610	204	112	339*	-	1,265
1943	596	239	-	-	875*	1,760
1944	895	-	114	930*	779*	2,718
1945	-	412	-	-	755*	1,167
Total for period ending June 30, 1945	2,101	905	226	1,269	2,409	6,910

* Callable

It will be noted from the above table that the method, which I propose be followed, will increase the public debt in the fiscal year 1942 by \$1,265,000,000 in order to refinance the maturing or callable guaranteed obligations. It will probably be necessary to add from one billion to one and a half billion dollars for current cash requirements, or a total increase in the public debt for the fiscal year 1942 of possibly \$2,265,000,000 to \$2,765,000,000. The fiscal year 1943 would require a further increase in the public debt of \$1,760,000,000 to meet maturing or callable guaranteed issues. What the cash requirements will be for these agencies during the fiscal year 1943 is rather difficult to estimate at this time. Of the total increase in the public debt amounting to \$6,910,000,000 to meet the maturing or callable guaranteed issues set out above, approximately \$4,000,000,000 falls in the fiscal years 1944 and 1945. It may be possible to reduce some of these figures by the application of receipts brought in through the liquidation of assets of these corporations and credit agencies.

According to the latest Budget estimates, the gross public debt of the United States on June 30, 1942, will be more than \$61,000,000,000 without providing for the future accruals on United States Savings Bonds and for \$2,200,000,000 to replace the minimum guaranteed issues that would otherwise be put out in the fiscal year 1942. In any case, it will be necessary for the Treasury to ask Congress during the early spring of 1942 for an increase of several billions of dollars in the present debt limitation in order to meet the deficit for the fiscal year 1943. It seems to me that it would not be difficult to get an increase in the present debt limitation of \$65,000,000,000 of an amount sufficient to enable the Treasury not only to finance the deficit in regular receipts, but also to take care of the financial requirements of the governmental corporations and credit agencies.

On November 1, 1941, the EFC has a maturity of \$300,000,000 and the USEA has one of \$112,000,000, and on November 15, the CCC has a maturity of \$204,000,000. In carrying out the suggestions made above, I propose on Thursday of this week, subject of course to your approval in the regular manner, to offer a Treasury note for about \$500,000,000, to be issued only in exchange for the EFC and CCC maturities aggregating about that amount, and I propose to pay off in cash the USEA maturity of \$112,000,000. I hope that the method here suggested for financing future guaranteed issues and the proposal for financing the immediate maturities will have your approval. If so, I should be pleased if you would so indicate at the bottom of this memorandum.

*Not used.
Sey phoned
President -
Dew
10/21/41*

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Calendar of Direct and Guaranteed Bonds and Notes 1/

October 1, 1941

(In millions of dollars)

Date	Description	Fixed maturities		Callable issues			
		Direct	Guaranteed	First callable		Final maturities	
				Direct	Guaranteed	Direct	Guaranteed
1941-Jan.							
Feb.							
Mar.							
Apr.							
May							
June							
July							
Aug.							
Sept.							
Oct.							
Nov. 1	RFC 7/8% -----		300				
Nov. 1	USHA 1/4% -----		112				
Nov. 15	CCC 1% -----		204				
Dec. 15	Note 1-1/4% -----	204					
	Total	204	616				
1942-Jan. 15	RFC 7/8% -----		310				
Jan. 15	FFMC 3% (1942-47) -----				236		
Feb.							
Mar. 1	FFMC 2-3/4% (1942-47) -----						103
Mar. 15	Note 1-3/4% -----	426					
Apr.							
May							
June							
July 1	RFC 1% -----		276				
July 1	HOLC 2-1/4% (1942-44) -----						875
Aug.							
Sept. 15	Note 2% -----	342					
Oct. 15	RFC 7/8% -----		320(T)				
Nov.							
Dec. 15	Note 1-3/4% -----	232					
	Total	1,000	906		1,214		
1943-Jan.							
Feb.							
Mar. 15	Note 3/4% -----		66(T)				
Apr.							
May 1	CCC 3/4% -----		289				
June 15	Note 1-1/8% -----	629					454
June 15	Bond 3-3/8% (1943-47) -----						324(T)
July 15	RFC 1-1/8% -----						
Aug.							
Sept. 15	Note 1% -----	279					
Oct. 15	Bond 3-1/4% (1943-45) -----						1,401
Nov.							
Dec. 15	Note 1-1/8% -----	421					
	Total	1,395	613	1,855			
1944-Jan.							
Feb. 1	USHA 1-3/8% -----		114				
Mar. 15	Note 1% -----	515					
Mar. 15	FFMC 3-1/4% (1944-44) -----						95
Apr. 15	Bond 3-1/4% (1944-46) -----						1,519
Apr. 15	RFC 1% -----						571(T)
May 1	HOLC 3% (1944-52) -----						779
May 15	FFMC 3% (1944-49) -----						835
June 15	Note 3/4% -----	416					
July 1	HOLC 2-1/4% (1942-44) -----						875
Aug.							
Sept. 15	Note 1% -----	283					
Sept. 15	Note 3/4% -----	635(T)					
Oct.							
Nov.							
Dec. 15	Bond 4% (1944-54) -----						1,037
	Total	1,249	685	2,556	1,709		875

1/ Excludes special issues, issues redeemable at option of holder, postal savings bonds, FHA debentures, and depository bonds.

Calendar of Direct and Guaranteed Bonds and Notes ^{1/}

October 1, 1941

(In millions of dollars)

Date	Description	Fixed maturities		Callable issues			
		Direct	Guaranteed	First callable		Final maturities	
				Direct	Guaranteed	Direct	Guaranteed
1949-Jan.							
Feb.							
Mar.							
Apr.							
May 15	FFMC 3% (1944-49)						835
June 15	Bond 3-1/8% (1946-49)					819	
July							
Aug.							
Sept.							
Oct.							
Nov.					491		
Dec. 15	Bond 3-1/8% (1949-52)			1,786			
Dec. 15	Bond 2-1/2% (1949-53)						
	Total			2,277		819	835
1950-Jan.							
Feb.							
Mar. 15	Bond 2% (1948-50)					1,115(T)	
Apr.							
May							
June							
July							
Aug.							
Sept. 15	Bond 2-1/2% (1950-52)			1,186			
Oct.							
Nov.							
Dec. 15	Bond 2% (1948-50)					571	
	Total			1,186		1,686	
1951-Jan.							
Feb.							
Mar. 15	Bond 2-3/4% (1948-51)					1,223	
Apr.							
May							
June 15	Bond 2-3/4% (1951-54)			1,627			
July							
Aug.							
Sept. 15	Bond 3% (1951-55)			755			
Oct.							
Nov.							
Dec. 15	Bond 2-1/4% (1951-53)			1,118			
	Total			3,500		1,223	
1952-Jan.							
Feb.							
Mar. 15	Bond 2-1/2% (1952-54)			1,024(T)			
Apr.							
May 1	HOLC 3% (1944-52)						779
June							
July							
Aug.							
Sept. 15	Bond 2-1/2% (1950-52)					1,186	
Oct. 15	Bond 4-1/4% (1947-52)					759	
Nov.							
Dec. 15	Bond 3-1/8% (1949-52)					491	
	Total			1,024		2,436	779

^{1/} Excludes special issues, issues redeemable at option of holder, postal savings bonds, FHA debentures, and depository bonds.

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Calendar of Direct and Guaranteed Bonds and Notes 1/

October 1, 1941

(In millions of dollars)

Date	Description	Fixed maturities		Callable issues			
		Direct	Guaran- teed	First callable		Final maturities	
				Direct	Guaran- teed	Direct	Guaran- teed
1953-Jan. Feb. Mar. Apr. May June 15 July Aug. Sept. Oct. Nov. Dec. 15 Dec. 15	Bond 2% (1953-55)			725			
	Bond 2-1/2% (1949-53)					1,786	
	Bond 2-1/4% (1951-53)					1,118	
	Total			725		2,904	
1954-Jan. Feb. Mar. 15 Apr. May June 15 June 15 July Aug. Sept. Oct. Nov. Dec. 15	Bond 2-1/2% (1952-54)					1,024(T)	
	Bond 2-3/4% (1951-54)					1,627	
	Bond 2-1/4% (1954-56)			681			
	Bond 4% (1944-54)					1,037	
	Total			681		3,688	
1955-Jan. Feb. Mar. 15 Apr. May June 15 July Aug. Sept. 15 Oct. Nov. Dec.	Bond 2-7/8% (1955-60)			2,611			
	Bond 2% (1953-55)					725	
	Bond 3% (1951-55)					755	
	Total			2,611		1,480	
1956-Jan. Feb. Mar. 15 Mar. 15 Apr. May June 15 July Aug. Sept. 15 Oct. Nov. Dec.	Bond 3-3/4% (1946-56)					489	
	Bond 2-1/2% (1956-58)			1,449(T)			
	Bond 2-1/4% (1954-56)					681	
	Bond 2-3/4% (1956-59)			982			
	Total			2,431		1,170	

1/ Excludes special issues, issues redeemable at option of holder, postal savings bonds, FHA debentures, and depository bonds.

Calendar of Direct and Guaranteed Bonds and Notes ^{1/}

October 1, 1941

(In millions of dollars)

Date	Description	Fixed maturities		Callable issues			
		Direct	Guaran- teed	First callable		Final maturities	
				Direct	Guaran- teed	Direct	Guaran- teed
1957-Jan. Feb. Mar. Apr. May June July Aug. Sept. Oct. Nov. Dec.							
	Total						
1958-Jan. Feb. Mar. 15 Apr. May June 15 July Aug. Sept. Oct. Nov. Dec.	Bond 2-1/2% (1956-58) -----					1,449(T)	
	Bond 2-3/4% (1958-63) -----			919			
	Total			919		1,449	
1959-Jan. Feb. Mar. Apr. May June July Aug. Sept. 15 Oct. Nov. Dec.	Bond 2-3/4% (1956-59) -----					982	
	Total					982	
1960-Jan. Feb. Mar. 15 Apr. May June July Aug. Sept. Oct. Nov. Dec. 15	Bond 2-7/8% (1955-60) -----					2,611	
	Bond 2-3/4% (1960-65) -----			1,485			
	Total			1,485		2,611	

^{1/} Excludes special issues, issues redeemable at option of holder, postal savings bonds, FHA debentures, and depositary bonds.

Calendar of Direct and Guaranteed Bonds and Notes 1/

October 1, 1941

(In millions of dollars)

Date	Description	Fixed maturities		Callable issues			
				First callable		Final maturities	
		Direct	Guaranteed	Direct	Guaranteed	Direct	Guaranteed
1961-Jan. Feb. Mar. Apr. May June 1 July Aug. Sept. Oct. Nov. Dec.	Panama 3 $\frac{1}{2}$ % -----	50					
	Total	50					
1962-Jan. Feb. Mar. Apr. May June July Aug. Sept. Oct. Nov. Dec.	Total						
1963-Jan. Feb. Mar. Apr. May June 15 July Aug. Sept. Oct. Nov. Dec.	Bond 2-3/4% (1958-63) -----					919	
	Total					919	
1964-Jan. Feb. Mar. 15 Apr. May June July Aug. Sept. Oct. Nov. Dec.	FFKC 3-1/4% (1944-64) -----						95
	Total						95
1965-Jan. Feb. Mar. Apr. May June July Aug. Sept. Oct. Nov. Dec. 15	Bond 2-3/4% (1960-65) -----					1,485	
	Total					1,485	

1/ Excludes special issues, issues redeemable at option of holder, postal savings bonds, FHA debentures, and depositary bonds.

STRICTLY CONFIDENTIAL

RFC 7/8 Percent Notes Maturing on November 1, 1941

93

Amount Owned by the Largest Holders Reporting
to the Treasury as of August 31, and September 30, 1941

(In millions of dollars)

Investor	: Aug. : : 31 :	Sept. : : 30 :	: Net : change
Guaranty Trust Co., New York, N.Y.....	86.9	86.9	-
Metropolitan Life Insurance Co., New York, N.Y....	21.0	21.0	-
J. P. Morgan & Co., Inc., New York, N.Y.....	16.0	16.0	-
First National Bank of Chicago, Chicago, Ill.....	15.0	15.0	-
The Northern Trust Co., Chicago, Ill.....	11.0	11.0	-
Irving Trust Co., New York, N.Y.....	10.0	10.0	-
Bank of the Manhattan Co., New York, N.Y.....	10.0	10.0	-
National City Bank, New York, N.Y.....	9.0	9.0	-
Bankers Trust Co., New York, N.Y.....	1.3	6.9	+5.6
National Bank of Detroit, Detroit, Mich.....	6.7	6.7	-
French American Banking Corp., New York, N.Y.....	5.4	5.4	-
Penn Mutual Life Insurance Co., Philadelphia, Pa..	5.0	5.0	-
State Bank of Albany, Albany, N.Y.....	3.0	3.0	-
Maryland Casualty Co., Baltimore, Md.....	3.0	3.0	-
The New York Trust Co., New York, N.Y.....	2.5	2.5	-
The Cleveland Trust Co., Cleveland, Ohio.....	2.3	2.3	-
City National Bank & Trust Co., Chicago, Ill.....	2.2	2.2	-
Bayonne Trust Co., Bayonne, N.J.....	2.0	2.0	-
Union Planters National Bank, Memphis, Tenn.....	1.2	1.2	-
Union National Bank, Houston, Texas.....	1.2	1.2	-
Brown Bros. Harriman & Co., New York, N.Y.....	1.2	1.2	-
Emigrant Industrial Savings Bank, New York, N.Y..	1.2	1.2	-
Bank of New York, New York, N.Y.....	1.0	1.1	+.1
Marine Midland Trust Company, New York, N.Y.....	1.0	1.0	-
American Motorists Insurance Co., Chicago, Ill...	9.3	.5	-8.8
Total amount owned by largest holders.....	<u>228.4</u>	<u>225.3</u>	<u>-3.1</u>
Total amount outstanding.....	<u>299.6</u>	<u>299.6</u>	<u>-</u>
Percent of total owned by largest holders.....	76.2%	75.2%	-1.0%

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

October 21, 1941

CCC 1 Percent Notes Maturing on November 15, 1941

94

Amount Owned by the Largest Holders Reporting
to the Treasury as of August 31, and September 30, 1941
(In millions of dollars)

Investor	Aug. 31	Sept. 30	Net Change
National City Bank, New York, N. Y.....	23.3	23.3	-
Irving Trust Co., New York, N. Y.....	12.0	12.0	-
First National Bank, New York, N. Y.....	8.3	8.3	-
J. P. Morgan & Co., Inc., New York, N. Y.....	6.9	6.9	-
National Bank of Detroit, Detroit, Mich.....	6.2	6.2	-
The Cleveland Trust Co., Cleveland, Ohio.....	5.6	5.6	-
Manufacturers Natl. Bank, Detroit, Mich.....	5.0	5.0	-
First National Bank of Chicago, Chicago, Ill.....	4.9	4.9	-
First National Bank of Boston, Boston, Mass.....	4.7	4.7	-
First National Bank, Shreveport, La.....	4.2	4.2	-
The Northern Trust Co., Chicago, Ill.....	4.0	4.0	-
City Natl. Bk. & Tr. Co., Chicago, Ill.....	3.8	3.8	-
Bankers Trust Co., New York, N. Y.....	3.0	3.6	+ .6
Fidelity Union Trust Co., Newark, N. J.....	3.5	3.5	-
Camden Trust Co., Camden, N. J.....	3.0	3.0	-
Toledo Trust Co., Toledo, Ohio.....	2.5	2.5	-
Bank of North Dakota, Bismarck, N. D.....	2.2	2.2	-
Northwestern Natl. Bk. & Tr. Co., Minneapolis....	2.0	2.0	-
Public Natl. Bk. & Tr. Co. of N.Y., New York, N.Y.	2.0	2.0	-
The Detroit Bank, Detroit, Mich.....	2.0	2.0	-
Marine Midland Tr. Co. of N.Y., New York, N.Y....	1.8	1.8	-
N. Y. Life Insurance Co., New York, N. Y.....	1.6	1.6	-
Commerce Trust Co., Kansas City, Mo.....	1.6	1.6	-
The New York Trust Co., New York, N. Y.....	1.5	1.5	-
American Motorists Insurance Co., Chicago, Ill....	2.0	-	-2.0
Total amount owned by largest holders.....	<u>117.6</u>	<u>116.2</u>	<u>-1.4</u>
Total amount outstanding.....	<u>204.2</u>	<u>204.2</u>	<u>-</u>
Percent of total owned by largest holders.....	57.6%	56.9%	-.7%

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

October 21, 1941.

UNITED STATES SAVINGS BONDS

Comparative Statement of Sales During
First Seventeen Business Days of August, September, and October, 1941
(August 1-20, September 1-20, October 1-20)
On Basis of Issue Price

(Amounts in thousands of dollars)

Item	Sales			Amount of Increase or Decrease (-)		Percentage of Increase or Decrease (-)	
	October	September	August	October over September	September over August	October over September	September over August
Series E - Post Offices	\$ 27,833	\$ 26,137	\$ 27,987	\$ 1,696	-\$ 1,850	6.5%	- 6.6%
Series E - Banks	<u>51,503</u>	<u>45,264</u>	<u>53,118</u>	<u>6,239</u>	- <u>7,854</u>	<u>13.8</u>	- <u>14.8</u>
Series E - Total	79,335	71,402	81,105	7,933	- 9,703	11.1	- 12.0
Series F - Banks	14,700	11,353	14,534	3,347	- 3,181	29.5	- 21.9
Series G - Banks	<u>78,824</u>	<u>71,518</u>	<u>88,919</u>	<u>7,306</u>	- <u>17,401</u>	<u>10.2</u>	- <u>19.6</u>
Total	<u>\$172,859</u>	<u>\$154,273</u>	<u>\$184,558</u>	<u>\$18,586</u>	- <u>\$30,285</u>	<u>12.0%</u>	- <u>16.4%</u>

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

October 21, 1941.

Source: All figures are deposits with the Treasurer of the United States on account of proceeds of sales of United States Savings Bonds.

Note: Figures have been rounded to nearest thousand and will not necessarily add to totals.

UNITED STATES SAVINGS BONDS

Daily Sales - October 1941
On Basis of Issue Price

(In thousands of dollars)

Date	Post Office Bond Sales Series E	Bank Bond Sales				All Bond Sales			
		Series E	Series F	Series G	Total	Series E	Series F	Series G	Total
October 1941									
1	\$ 1,450	\$ 3,029	\$ 1,286	\$ 8,271	\$ 12,587	\$ 4,479	\$ 1,286	\$ 8,271	\$ 14,036
2	1,870	2,786	867	4,324	7,977	4,656	867	4,324	9,847
3	2,150	3,299	1,065	6,323	10,687	5,449	1,065	6,323	12,837
4	1,270	1,696	612	6,400	8,707	2,966	612	6,400	9,978
6	3,449	4,778	1,444	9,286	15,508	8,226	1,444	9,286	18,956
7	1,207	2,595	572	2,913	6,080	3,802	572	2,913	7,287
8	1,363	3,674	821	3,611	8,106	5,037	821	3,611	9,469
9	1,652	4,270	903	3,654	8,827	5,923	903	3,654	10,479
10	1,495	3,672	989	5,272	9,933	5,167	989	5,272	11,428
11	1,291	2,400	632	4,098	7,129	3,690	632	4,098	8,420
13	2,515	3,624	1,164	4,989	9,778	6,139	1,164	4,989	12,293
14	437	1,022	261	511	1,794	1,459	261	511	2,231
15	879	2,175	759	3,482	6,417	3,055	759	3,482	7,296
16	1,376	3,054	724	3,908	7,685	4,429	724	3,908	9,060
17	1,422	3,609	860	4,969	9,438	5,031	860	4,969	10,861
18	1,180	2,424	846	3,013	6,283	3,604	846	3,013	7,463
20	2,827	3,395	895	3,800	8,091	6,222	895	3,800	10,918
Total	\$ 27,833	\$ 51,503	\$ 14,700	\$ 78,824	\$145,026	\$ 79,335	\$ 14,700	\$ 78,824	\$172,859

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

October 21, 1941.

Source: All figures are deposits with the Treasurer of the United States on account of proceeds of sales of United States Savings Bonds.

Note: Figures have been rounded to nearest thousand and will not necessarily add to totals.

UNITED STATES SAVINGS BONDS
Defense Series F and G

CONFIDENTIAL

Number of Units, by Denomination, Sold Each
Month from May through August, 1941

97

Month	Units by Denomination						Total	Issue Price (in thousands)
	\$100	\$500	\$1,000	\$5,000	\$10,000			
Series F								
May	6,063	3,318	11,851	2,507	4,458	28,197	\$ 52,711	
June	5,500	2,410	7,191	1,184	1,541	17,826	22,404	
July	8,233	3,536	9,904	1,541	1,633	24,847	27,032	
August	<u>7,027</u>	<u>2,862</u>	<u>6,774</u>	<u>1,107</u>	<u>999</u>	<u>18,769</u>	<u>18,080</u>	
Total	<u>26,823</u>	<u>12,126</u>	<u>35,720</u>	<u>6,339</u>	<u>8,631</u>	<u>89,639</u>		
Issue Price (in thousands)	<u>\$1,985</u>	<u>\$4,487</u>	<u>\$26,433</u>	<u>\$23,454</u>	<u>\$63,869</u>		<u>\$120,228</u>	
Series G								
May	32,207	15,000	57,414	10,815	18,916	134,352	\$311,370	
June	20,331	9,423	33,435	5,400	7,389	75,978	141,070	
July	25,186	13,474	43,891	6,841	7,544	96,936	162,792	
August	<u>20,077</u>	<u>9,674</u>	<u>31,137</u>	<u>4,970</u>	<u>5,485</u>	<u>71,343</u>	<u>117,682</u>	
Total	<u>97,801</u>	<u>47,571</u>	<u>165,877</u>	<u>28,026</u>	<u>39,334</u>	<u>378,609</u>		
Issue Price (in thousands)	<u>\$9,780</u>	<u>\$23,786</u>	<u>\$165,877</u>	<u>\$140,130</u>	<u>\$393,340</u>		<u>\$732,913</u>	

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

October 21, 1941.

Source: Tabulations by the Division of Loans and Currency from an audit of original stubs.

Note: Issue price figures have been rounded to nearest thousand and will not necessarily add to totals. Amounts do not agree with released sales figures which were on the basis of deposits with the Treasurer of the United States.

My dear Mr. Attorney General:

I am enclosing copy of a self-explanatory letter which I sent to Secretary Stimson yesterday.

I am personally interested in this case, and am asking one of our lawyers to fly to Honolulu tonight to make an investigation of the facts on the ground. As soon as I have received a report I should like to have an opportunity to take the matter up with you again.

In the meantime, I hope it will be possible to secure a continuance of the case, which has been set for trial on October 27, 1941.

Sincerely yours,

(Signed) E. Berentson, Jr.

The Honorable

The Attorney General of the United States.

Enclosure
EHPJr/HC/mp
Typed 10/21'41

*Sent by messenger
1:30 - Sturgis*

October 20, 1941.

My dear Mr. Secretary:

On September 22, 1941, Lieutenant Martin R. Connelly of the United States Army was fatally shot by Customs Guard John E. Young at Honolulu, T. H., as the former was leaving the United States Army Transport "PMSIDNEY" CLEVELAND.

I am informed by the acting collector of customs at Honolulu that the shooting occurred while the guard was on official duty, in connection with an attempt of Lieutenant Connelly to pass through the customs lines with a package without submitting it to inspection upon the guard's request. Original presentation of Mr. Young on a charge of second degree murder has been instituted in the territorial courts, and I am informed by the Department of Justice that the case has been removed to the Federal courts. This case has been set for trial on October 27, 1941, and efforts of the counsel for the defendant to obtain a delay have been unsuccessful.

The Customs Agency Service of this Department is conducting an investigation to ascertain the facts and evidence in the case. Information has been received indicating that Lieutenant Connelly and an Army nurse and two naval officers, who were with him, were all under the influence of liquor at the time of the shooting. A man and woman, who apparently were waiting for Lieutenant Connelly outside the customs barrier, allegedly witnessed the scene and then fled.

The customs agent conducting the investigation has consulted Lieutenant Thomas H. Green of the Judge Advocate's office, Honolulu. Colonel Green indicated that he would insist upon a speedy trial; that he would prevent the agent from interviewing the many witnesses; and that the Army bitterly resented statements (which Colonel Green incorrectly attributed to the acting collector of customs) appearing in the press regarding Lieutenant Connelly's mental condition. Colonel Green at first refused permission for the agent to interview the Army nurse. On October 15, 1941, however, he stated that the agent would be permitted on October 20, but not sooner, to ask the nurse if she cared to make a statement. The impression gained by the agent from the manner in which this permission was granted was that the nurse would probably refuse to furnish information.

The information available to me indicates that an employee of the Bureau of Customs of this Department is awaiting trial on a charge

- 2 -

of murder for a shooting which apparently occurred in the course of performing his official duties; that the case is being rushed to trial before the Treasury Department has an opportunity to make the necessary investigation; and that the Treasury Department has been prevented from completing such investigation by the attitude of army officials in Honolulu. I am, therefore, constrained to urge upon you that you immediately instruct the appropriate army officials in Honolulu, by telegraph, to cooperate not only in making all witnesses available for interview by the customs agent, but also in encouraging such witnesses to disclose fully and freely the information in their possession. It is also requested that the local army officials be instructed to cooperate in further efforts of counsel for the defendant to delay the trial until the investigation can be completed.

Very truly yours,

(Signed) H. Morgenthau, Jr.

Secretary of the Treasury.

The Honorable

The Secretary of War.

RC:bl 10-20-41

(Note: This letter delivered by Secret Service agent to Secretary Stinson personally at his home after office hours, October 20, 1941.)

October 21, 1941
3:41 p.m.

HMJr: Hello.

Secretary
Stimson: Henry, I've looked into your case in
Hawaii.

HMJr: Yes.

S: I find that the matter is in the hands of
the Federal Court there.....

HMJr: Yes.

S:and that the Judge Advocate there has
no - nothing - no official function to perform
at all.

HMJr: I see.

S: I have telegraphed that - quoting the protest
that you made to me about it, and say that it's
my desire - that it's my instructions that they
do not interfere in any way in the fair trial
of that case. That I want justice done.

HMJr: Well, thank you so much. We've - we put.....

S: I know what the situation there can be where
the racial question comes in.

HMJr: That's right.

S: And I talked pretty Dutch to the Judge Advocate
here about it.

HMJr: Good.

S: I don't know how it may be done, but I hope.....

HMJr: Well, if I hear any more, I may take the
liberty of calling you.

S: All right.

HMJr: Thank you, Harry.

OFFICE OF THE SECRETARY OF THE TREASURY

Collecting the Revenues
from Customs, 1941

Washington, D. C.

October 21, 1941

Joseph B. Poindexter
Governor of Hawaii
Honolulu, Hawaii

ROBERT CHAMBERS CHIEF COUNSEL CUSTOMS AND FRED GARDNER
CUSTOMS AGENCY SERVICE ARRIVING HONOLULU ON FRIDAY
CLIPPER TO ASCERTAIN FULL FACTS FOR ME REGARDING FATAL
SHOOTING OF LIEUTENANT MARTIN R. CONNELLY, U. S. ARMY,
BY CUSTOMS GUARD JOHN K. YEUNG AT HONOLULU SEPTEMBER
22, 1941. I SHALL APPRECIATE ANY ASSISTANCE YOU MAY
BE ABLE TO EXTEND TO THEM.

(Initialed) H. M., Jr.

Henry Morgenthau, Jr.
Secretary of the Treasury.

Sent to telegraph office at 5:30 pm. -10-21-41
HMF Jr/RC/ea

October 21, 1941.

MEMORANDUM

TO: Secretary Morgenthau
FROM: Mr. Gaston

Elmer Irey went over to see McReynolds today by appointment, and by my direction, in order to clear up the situation with respect to character investigations of Defense candidates. He was surprised to find present Ugo Carusi, Assistant to the Attorney General; Arthur Flemming, Civil Service Commissioner; and Lawson A. Moyer and Mrs. McMillin of the Civil Service Commission staff.

Carusi stated flatly that Hoover desired to take over the investigations, leaving to us only the income tax check-ups and that this had the Attorney General's approval. He said the F.B.I. was unwilling to disclose its records to other agencies and that the F.B.I. had sole responsibility for investigating loyalty of candidates. Irey responded that it was plainly impracticable to have two different field investigations by two different agencies; that we did not ask for the responsibility of making these investigations and that we were willing to surrender it at any time when properly directed to do so. He mentioned some of the difficulties of getting adequate cooperation from the F.B.I.

McReynolds said that he would write a memorandum to the President recommending that the responsibility for the investigations be transferred to the F.B.I. and that a duplicate list be supplied to us solely for the purpose of checking the income tax records.

[Handwritten initials]

October 21, 1941
4:35 p.m.

HMJr: Hello.

William
McReynolds: How do you do, sir?

HMJr: Hello, Mac.

Mc: How are you feeling?

HMJr: Oh, a little cranky just at the moment. How are you?

Mc: Oh, a little cranky, too. You haven't fallen down in any more airplanes, have you?

HMJr: Not for the moment.

Mc: Not for the moment? (Laughs) You scared me to death. Has Mrs. Morgenthau permitted you to go in the air again?

HMJr: Yeah - under much stricter regulations.

Mc: (Laughs) I talked to - Rus Waesche told me about that, and I got scared all over again.

HMJr: Yeah.

Mc: Listen. I've been talking to Justice and Elmer about this - the investigation of personnel.

HMJr: Yes.

Mc: And we've come to an arrangement by which they take the stuff back and assume full responsibility for it. That is the OEM group.

HMJr: Yeah.

Mc: But I'm writing a letter - or memorandum - to you for the President's signature.....

HMJr: Yeah.

Mc:releasing you from the responsibility of doing that in accordance with his memorandum

- 2 -

of February 28.

HMJr:

Yeah.

Mc:

I didn't think it was fair to you to make an informal arrangement that this thing would be taken away.

HMJr:

I've got to have it in writing.

Mc:

You've got to have it in writing, and you've got to have it from the same source that started it.

HMJr:

That's right.

Mc:

And I told the boys they couldn't budge an inch or make any other arrangement until that was done.

HMJr:

That's right.

Mc:

Yes, we're on the way to do that. The only thing I've got is what Francis Biddle told me that the President said. He didn't say anything to me.

HMJr:

Well, I send them over there; and what Biddle tells me the President said, is no good with me.

Mc:

Yeah. Well, for that matter, neither is it with me.

HMJr:

What?

Mc:

Neither is it to me.

HMJr:

Yeah.

Mc:

And so I'm putting it up, and if - I was sure you wouldn't object as long as the President authorizes the thing to be done, and....

HMJr:

What makes you think the President's going to sign it?

- 3 -

Mc: I haven't the least idea whether he'll sign it.

HMJr: Well, if he wants to sign it, it's just one less worry.

Mc: Yeah, I should say so. And if he doesn't want to sign it, why I'm perfectly happy about it. But they come to me with instructions that we should do so and so because the President said so. Now I'm going to find out whether the President said so.

HMJr: Who brought it to you?

Mc: Biddle called me himself.

HMJr: I see. If the President wants to sign it, it's Jake with me, Mac.

Mc: Yeah. Well, I was sure. I just wanted you to know what I was doing on it.

HMJr: Well, I appreciate very much your calling.

Mc: Thank you, sir.

HMJr: It was very gentlemanly of you.

Mc: Thank you.

HMJr: Thank you.

Mc: Good-bye.

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ASSISTANT SECRETARY OF THE TREASURY

October 21, 1941.

MEMORANDUM

TO: Secretary Morgenthau
FROM: Mr. Gaston

Admiral Waesche is sending me over a copy of the Navy broadcast of last Friday to ships in the Pacific, but he remembers distinctly that it provided that all ships bound for Vladivostok should continue their voyages.

MSB.

The confidential material on broadcast was ret'd to adm Waesche personally per instructions of King

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

108

DATE October 21, 1941

TO Secretary Morgenthau
 FROM Mr. Thompson

Replying to your memorandum of today, I have obtained from the Bureau of the Mint the following figures showing the number of tons of metals used in our coinage. The figures shown are for the fiscal years 1940, 1941, and estimated for 1942.

TONS OF METALS USED IN UNITED STATES COINAGE

<u>Fiscal Year</u>	<u>Silver</u>	<u>Copper</u>	<u>Nickel</u>	<u>Zinc</u>	<u>Tin</u>
1940	665	2,235	242	60	15
1941	1,220	4,700	434	137	34
1942, estimated at 25% increase over 1941	1,525	5,875	542	171	43

Handwritten signature

OCT 21 1941

Mr. Donald M. Nelson,
Executive Director,
Supply Priorities and Allocations Board,
Social Security Building,
Washington, D. C.

Dear Mr. Nelson:

I have your letter of October 17, 1941, suggesting that the Mint consider the substitution of other materials for copper and nickel in the manufacture of the one and five cent pieces.

I have instructed the Director of the Mint to proceed at once with study and experimentation to determine what can be done toward conserving these metals. Obviously, any substitutes would have to be adaptable to the mechanical processes of the Mint. The Mint will be working under pressure between now and Christmas to meet the heavy coinage orders. Only limited progress, therefore, toward conservation of nickel and copper can be expected during that period. Already, however, the Mint has made some experimentation and finds that Monel metal can be substituted for electrolytic refined nickel, of which I understand there is a serious shortage.

However, any change in the content of these coins will require legislation. As soon as our experiments have been completed I shall request such change in the present laws as is deemed desirable in view of the experiments.

Sincerely,

(Signed) W. W. WOODWARD, JR.
Secretary of the Treasury.

By Messenger

[Handwritten signature]

100-100000-100000
100-100000-100000

SUPPLY PRIORITIES AND ALLOCATION BOARD
SOCIAL SECURITY BUILDING
WASHINGTON, D. C.

February 7, 1941

Mr. Secretary:

On behalf of the Supply Priorities and Allocations Board, I wish respectfully to direct your attention to a rather serious problem in the solution of which your Department can render an important contribution to the success of the effort in which our nation is now engaged.

As you know, we are expecting the phenomenon of priority unemployment to have severe repercussions upon civilian morale. In the industries using non-ferrous metals the shortage of materials will be extremely troublesome. Although we all realize that the consumption of copper and nickel in coinage is not normally a significant amount, it seems to me that the enclosed charts clearly indicate that consumption of these metals by the mint is today a matter regarding which the Supply Priorities and Allocations Board may properly concern itself. Accordingly, I wish to outline to you the situation with regard to the non-ferrous metals used in coinage.

The situation in copper is as follows. Defense and essential civilian requirements exceed available supply by approximately 230,000 tons per year. As a result of our efforts to stimulate domestic production and to increase imports of this metal, we expect an additional 100,000 tons to become available in 1942, but we do not expect this to keep pace with the increase in military needs. We must also remember that the substitution possibilities are drastically limited because of the electrical uses of copper. You can readily understand, therefore, why we are concerned regarding supplies of this metal.

Nickel has been under allocation since March of this year. Only 15,500,000 pounds is available each month against a demand of 20,000,000 pounds. Of this amount we are allocating 1,000,000 pounds each month to civilian uses which has enabled us to meet requests bearing a preference rating of B-2 or higher, i. e., "Materials for the manufacture of parts for the repair or replacement of existing apparatus, equipment, and devices which must continue to operate in order to preserve essential production and services." It has been impossible for the last eight months to meet requests for nickel bearing a preference rating of B-3 or lower, i. e., "Materials for new apparatus, equipment, and devices used directly in operations which must continue in order to preserve essential production and services."

Our forecasts of the supply available for 1942 indicate that we must expect the production rate to fall by approximately 500,000 pounds per month or 3.2 per cent. Our Iron and Steel Branch estimates that military nickel requirements in 1942 will show an increase of 70 per cent over 1941. In view of the fact that an increase of only 6.5 per cent will destroy the margin on which the Civilian Supply Division is now making allocations, an extremely severe shortage of nickel must be expected for 1942. The situation is rendered even more acute by the extremely small stock of nickel now on hand. Our military reserve amounts at the present time to only ten days' supply.

Considerable impairment to essential civilian industries has resulted from the nickel shortage, and we cannot be certain that some of this damage has not been the result of our efforts to fill the mint demands. It was recently the unpleasant duty of our Board to deny to the Tennessee Eastman Corporation the stainless steel they required for the construction of a plant for the manufacture of plastics. That corporation offered evidence that their proposed plant would have provided materials capable of replacing 8,000,000 pounds of aluminum, 18,000,000 pounds of chrome nickel plated steel, 6,000,000 pounds of stainless steel, and 34,000,000 pounds of zinc. This request was denied because of the nickel shortage, and the amount of nickel contained in the stainless steel requested by that corporation was approximately the same amount as is consumed by the mint in an average month.

Widespread unemployment has resulted from the copper and nickel shortages and many small business men, to whom a supply of metal means economic life or death, have suffered as a result of the demands of the mint. In the case of nickel, our Labor Division estimates that the metal allocated to the mint, if made available to the electrical products industry, would permit the employment of 55,000 persons.

I am sure it is not your wish to see this continue into 1942, particularly since we can state with assurance that no improvement in the metal shortage is in sight. I know you will be very deeply concerned by this situation, and I believe you will agree with me that decisive and prompt action must be taken. I am confident that you will insist that the Treasury Department assume its full share of this burden. It is our desire to extend all possible aid to your Department in its task of accommodating its policies to the changed conditions, and it is hoped that the Treasury will be able to come forward with its own solution.

Since legislation will probably be necessary, we believe it should be requested for by the Treasury with the purpose given as that of making available to the Armed Forces certain strategic metals. In the choice of substitute materials we certainly feel that the Treasury Department should make the decision in the light of its knowledge of the suitability of such materials for use in coinage.

In this connection, I want to pass on to you our thoughts on the materials with the hope that they may be of some value to the Treasury Department. First I wish to mention that my staff indicates that a lignin base plastic made from farm waste might prove a good substitute for the existing one-cent coins. These plastics are available and there is no shortage of any of the materials needed in their manufacture.

In the case of five-cent coins it will apparently be necessary to use a metal if we are to avoid causing trouble in the coin-operated machines now in use. The Division of Civilian Supply has circularized the manufacturers of "slug-rejecting" devices who state that a substitute metal should have a density above 8.2 grams per cubic centimeter and a minimum conductivity of 30 microhms per cubic centimeter. My staff tells me that an alloy of zinc and silver with small amounts of electrolytic manganese would have approximately these properties. Since a relative surplus of these metals exists, we would suggest the testing of such an alloy in your coining presses.

I might also say that it has been suggested that the resulting change in appearance of the coins might be turned to good account by designating these coins as "Defense" or "Victory" coins. This would probably increase the awareness of the man in the street to our problem, with a resultant stimulating of desire to follow the lead of the Treasury in the conservation of all strategic materials. Such action would have an excellent effect on the morale of the business community.

By making available to civilian industry the non-ferrous metals used in coinage we will obtain an increase of approximately 3 per cent in the amount of copper available for civilian use, and 14 per cent in the amount of nickel; at the expense of a reduction in the supply of copper available for civilian use of only 0.35 per cent. This supply of copper and nickel should enable us to increase production of useful goods and services to an extent which may contribute materially to the control of inflation. The virtues of this method of inflation control are obvious for comment.

I will greatly appreciate any recommendations for an equitable and rapid solution of this problem.

With best wishes.

Very truly yours,



Donald M. Nelson
Executive Director

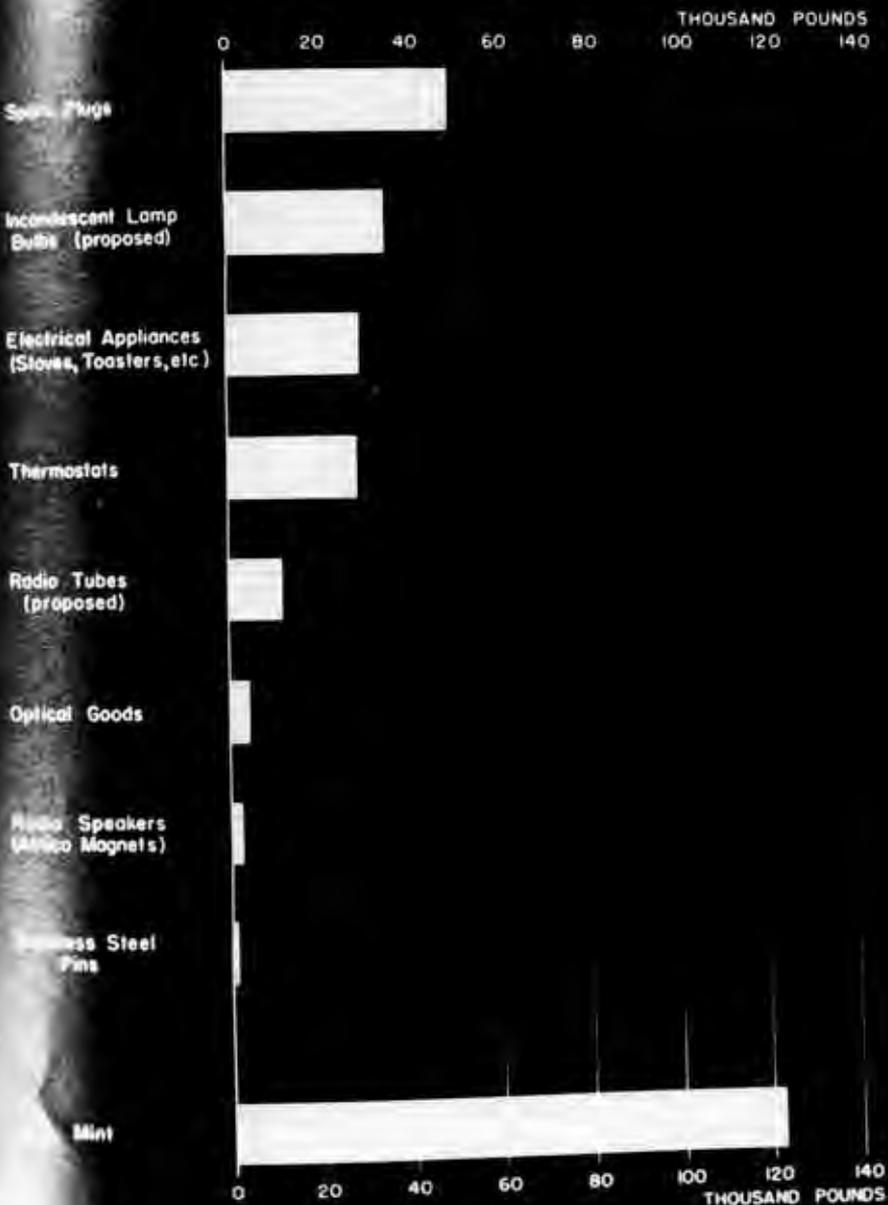
Supply Priorities and Allocations Board

Honorable Henry Morgenthau, Jr.

Secretary of the Treasury

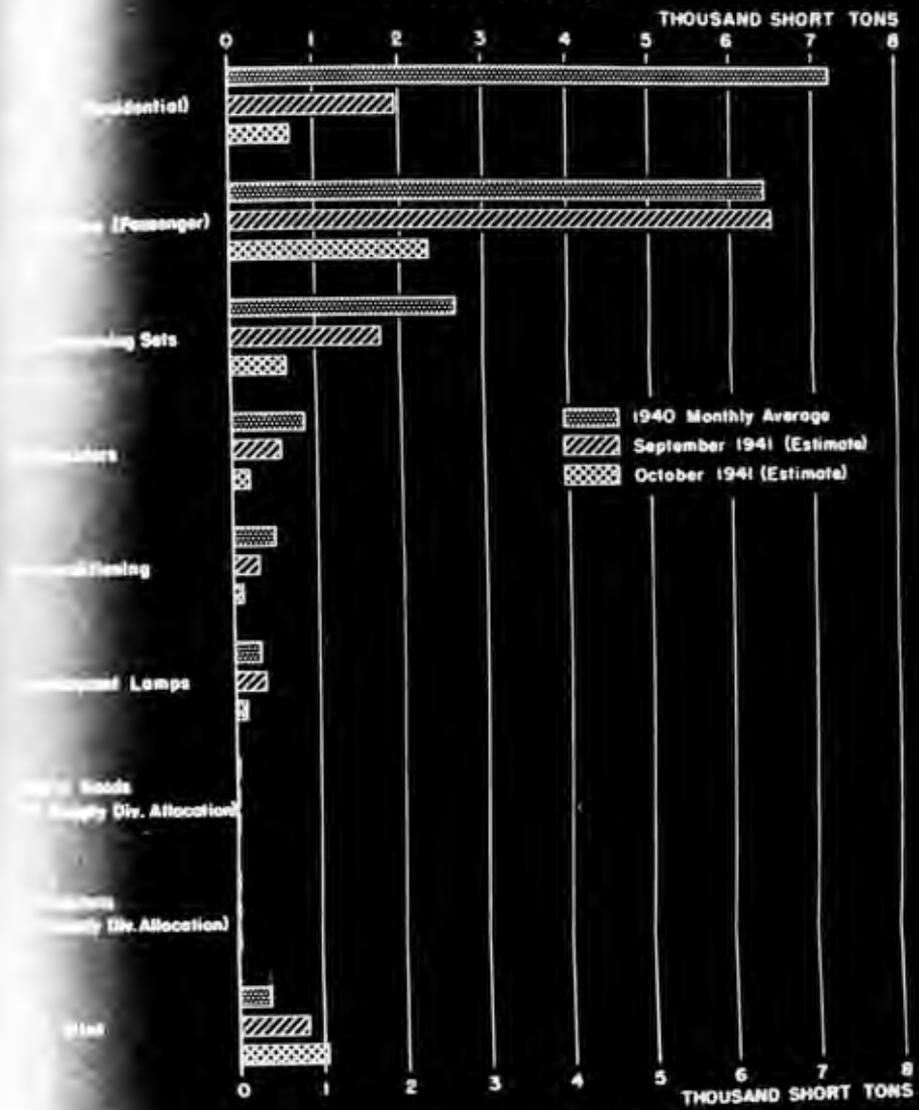
COMPARISON OF O. P. M. INDUSTRY ALLOCATIONS OF NICKEL WITH DELIVERIES TO U. S. MINT

AVERAGE DELIVERIES - 1st 8 MONTHS OF 1941

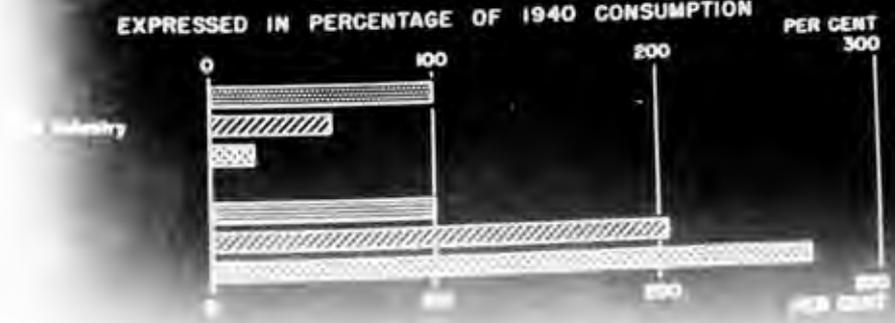


COMPARISON OF O.P.M. INDUSTRY ALLOCATIONS OF COPPER WITH ALLOCATIONS TO U.S. MINT

SEPTEMBER AND OCTOBER, 1941



EXPRESSED IN PERCENTAGE OF 1940 CONSUMPTION



- 2 - [REDACTED]

My dear Mr. Secretary:

Reference is made to a letter from Mr. Berle, dated October 16, 1941, (Bu 511.512342 Double/158), forwarding a note from the Canadian Minister and inquiring as to the date for the resumption of discussions relative to a convention between Canada and the United States for the avoidance of double taxation.

It is noted that the Deputy Minister of Finance and the Commissioner of Income Tax will be able to proceed to Washington in the latter part of October to continue the discussions which were held in Ottawa on October 6, 7, and 8. Accordingly, if convenient to the representatives to the discussions, we should desire to commence further consideration of the proposed convention on October 27, 1941, in the Board of Tax Appeals room, Bureau of Internal Revenue, Washington, D. C.

Sincerely yours,

(Signed) H. Morgenthau, Jr.

Secretary of the Treasury

The Honorable

The Secretary of State

Washington, D. C.

By Messenger

MA:FD
10/21/41

File to Mr. Thompson

DEPARTMENT OF STATE
WASHINGTON

October 18, 1941

In reply refer to
Bu 811.512342 Double/158

My dear Mr. Secretary:

Reference is made to Mr. Smith's letter of September 26, 1941, and to previous correspondence concerning the resumption of exploratory discussions with the Canadian authorities looking toward the conclusion of a Convention between Canada and the United States for the avoidance of double income tax.

There is enclosed a copy of note no. 630 dated October 13, 1941, from the Canadian Minister at Washington indicating that the Deputy Minister of Finance and the Commissioner of Income Tax will be able to proceed to Washington in the latter part of October to continue the discussions which were held in Ottawa on October 4, 7 and 8.

In

The Honorable

Henry Morgenthau, Jr.,

Secretary of the Treasury.

-2-

In order that I may be in a position to reply to the enclosed note, I should appreciate your informing me as soon as conveniently possible of the date on which officers of your Department desire to commence these further discussions.

Sincerely yours,

For the Secretary of State:



Adolf A. Berle, Jr.
Assistant Secretary

Enclosure:

From Canadian Legation,
October 13, 1941.

October 13, 1941

No. 630

Sir,

I have the honour to refer to discussions which took place in Ottawa on October 6, 7 and 8, between representatives of Canada and the United States, looking to the conclusion of a convention for the avoidance of double taxation, at which time a provisional draft convention was prepared to serve as a basis for further consideration. The representatives of the United States believed that another meeting should be held at an early date for the purpose of putting the provisional draft into final form for signature.

I am instructed by my Government to inform you that the Deputy Minister of Finance and the Commissioner of Excise Tax will be able to proceed to Washington in the latter part of October. I am to add that Parliament meets early in November and that it may prove difficult for these officials to be absent from Ottawa after Parliament convenes. In view of these considerations, I should be grateful to learn what date would best be convenient for the United States representatives for the proposed meeting.

I have the honour to be,
with the highest consideration,
Sir,

Your most obedient,
humble servant,

The Hon. Cordell Hull,
Secretary of State of the
United States,
Washington, D. C.

Leighton McCarthy

October 21, 1941

MEMORANDUM FOR THE SECRETARY

In accordance with your request of October 20, 1941, there are submitted for your information data on income and profits taxes paid by individuals and corporations in the United States, Great Britain, and Canada.

1. Income taxes on individuals

In the United States individuals are subject to one Federal income tax which includes the normal tax and surtax. Income taxes are also imposed by 31 States, the District of Columbia, and the city of Philadelphia.

In Great Britain as in the United States individuals pay one income tax which includes the income tax and surtax.

In Canada individuals pay two national income taxes, the income tax proper which includes the income tax and the surtax on investment income and the National Defence Tax which is collected at source. Income taxes are also imposed by 6 provinces.

As shown in Table 1, the individual income tax is lower in the United States than it is in Great Britain or Canada. For example, for a married man with no dependents and a net income of \$5,000, the income tax (including the New York State tax) is \$406 in the United States, \$1,855 (before post-war credit) in Great Britain and \$1,000 in Canada; that is, the American income tax at this level of income is approximately one-fifth of the British tax and two-fifths of the Canadian.

2. Income taxes on corporations

In the United States corporations pay an income tax, a surtax, and an excess profits tax. Corporation income taxes are also imposed in 32 States and the District of Columbia.

In Great Britain corporations pay an income tax and either the National Defence Contribution or the excess profits tax, whichever is greater.

- 2 -

In Canada corporations pay an income tax and an excess profits tax. In addition taxes are imposed by 5 provinces.

As shown in Table 2, the income tax rate in the United States (combining the Federal and New York State rates) is 35 percent. The minimum British tax is 55 percent (50 percent income tax and 5 percent National Defence Contribution). British corporations may reimburse themselves with respect to the income tax when distributing earnings to shareholders and are, therefore, merely the withholding agents with respect to the standard rate of 50 percent on dividends. The minimum rate of income tax in Canada is 40 percent (18 percent income tax and 22 percent minimum excess profits tax).

The United States excess profits tax rates range from 35 percent to 60 percent on excess profits in excess of (a) a credit of 95 percent of average earnings for 1936-1939, or 8 percent on the first \$5,000,000 of invested capital and 7 percent on the balance, whichever is greater, and (b) a specific exemption of \$5,000. The British excess profits tax is imposed at the rate of 100 percent on profits in excess of average profits with a minimum tax equal to 5 percent of net income. Under the Finance Act of 1941, provision is made to credit 20 percent of the net amount of excess profits tax paid by every concern and to refund such amount after the war. The Canadian excess profits tax is 75 percent of profits in excess of average profits, with a minimum tax equal to 22 percent of net income.

3. Social security taxes

In addition to income taxes social security taxes are collected from employees and employers in the United States and Great Britain. In the United Kingdom the amount of tax payable depends upon employees' age and sex and not upon the amount of earnings. The Dominion of Canada imposes no social security taxes but does maintain a voluntary annuity system. Provincial taxes for social work purposes such as, for example, the hospital tax in Quebec are also imposed. This tax is 5 percent of the sale price of meals if such price is 35 cents or more. The proceeds of this tax are devoted to the maintenance of charitable hospital facilities.

Roy Blough

Table 1

Comparison of present individual income taxes in United States
(including New York State), Great Britain and Canada 1/

Married person - no dependents

	United States : (including New York State) :	Great Britain 3/ Tax (before post-war credit) 4/ :	Post-war : credit 4/ :	Canada 2/
A. Amounts of tax				
\$46	-	\$ 5	\$ 5	-
100	-	52	52	-
200	-	111	61	-
300	-	235	76	-
400	-	325	112	95
500	42	505	127	175
600	90	730	143	275
700	147	955	160	400
800	406	1,250	227	1,000
900	1,524	4,505	260	3,080
1,000	21,700	38,455	260	26,965
1,200	54,808	84,080	260	61,875
1,400	747,861	961,850	260	371,045
B. Effective rates of tax				
\$46	-	0.3%	-	-
100	-	6.5	-	-
200	-	11.1	-	-
300	-	16.8	-	-
400	-	20.3	-	5.9%
500	3.4%	25.3	-	6.3
600	3.6	29.3	-	11.0
700	3.9	31.6	-	13.3
800	3.1	37.1	-	20.0
900	15.2	45.1	-	30.8
1,000	43.4	72.9	-	53.9
1,200	54.8	84.1	-	61.9
1,400	74.8	96.2	-	87.1

Treasury Department, Division of Tax Research

October 21, 1941.

1/ Maximum earned income assumed. Basis of computation: For United States (Revenue Act of 1941) earned income credit 10% (maximum \$1,400) and personal exemption \$1,500; for New York (Consolidated Laws, Chap. 60, Art. 16) no earned income credit, personal exemption \$2,500; for Great Britain, (Finance Act, 1941) earned income credit 10% (maximum £70) and personal exemption \$50. For Canada (Income War Tax Act of 1941) incomes up to \$3,000 assumed to be earned and incomes of more than \$30,000 assumed to include earned income of that amount and additional investment income to make up the total, exemption of \$1,500 for purpose of surtax on investment income and personal exemption \$1,500. The British surtax rates are applicable to total income before personal exemption and credit for dependents and "earned income" credit, the United States surtax rates apply after reduction of personal exemption and credit for dependents, but before "earned income" credit; the Canadian surtax applies only to investment income.

2/ Net income before deductions for State income tax and personal exemption. Under the New York law, the Federal income tax is not allowed as a deduction in computing net income, whereas under the Federal law, State income taxes are allowed as deductions in arriving at net income.

3/ Pounds converted at \$4.00.

4/ Under the Finance Act of 1941 the personal allowance of married persons was reduced from £170 to £140, and for single persons from £100 to £80. The exemption limit was decreased from £120 to £110 and "earned income" credit was reduced from 16-2/3% with a maximum credit of £250 to 10% with a maximum credit of £150. A system of forced saving was introduced. The saving is the difference between the tax computed on the basis of (a) the old personal exemptions and credits and (b) the new exemptions and credits and is to be repaid to the taxpayer after the war. This post-war credit is limited as follows: (a) All earned income £60 (\$240) for a single person and £65 (\$260) for a married person; (b) all investment income £10 (\$40) for a single person and £15 (\$60) for a married person.

5/ Canadian taxes only. Includes defense tax.

Table 2

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Comparison of present corporation income and excess profits taxes in the United States (including New York State), Great Britain, and Canada.

	United States (including New York State)	Great Britain	Canada
Income tax	35% ^{1/} (for corporations with normal tax net incomes of more than \$25,000)	50% ^{2/}	16% (20% for corporations filing con- solidated returns)
Minimum under excess profits tax	-	5	22
Total income tax	35%	55% ^{2/}	40%
Excess profits tax	35%-60% ^{3/}	100% of excess profits ^{4/} or 5% of net income whichever is greater	75% of excess profits ^{5/} or 22% of net in- come whichever is greater

Treasury Department, Division of Tax Research

October 21, 1941

- 1/ Includes Federal normal tax of 24%, surtax of 7% and New York State tax of 6%. The New York tax is allowed as a deduction in determining net income subject to Federal normal and surtax. The total rate, when this deduction is considered, can not exceed 35%.
- 2/ The corporation may reimburse itself for the tax when distributing earnings to shareholders. The corporation therefore is merely the withholding agent with respect to the standard rate of 50% on dividends
- 3/ The excess profits tax is imposed at graduated rates on excess profits net income in excess of (a) a credit of 95% of the average earnings for 1936-1939 or 8% on the first \$5,000,000 of invested capital and 7% on the balance, whichever is greater and (b) a specific exemption of \$5,000. New York State imposes no excess profits tax.
- 4/ The excess profits tax is imposed on the excess of profits of the taxable year over profits for 1935, 1936, the average of 1935 and 1937 or the average of 1936 and 1937. Under the Finance Act of 1941, 20% of the net amount of excess profits tax paid by every concern (after deducting any repayment on account of deficiencies) is treated as a credit to be refunded to the taxpayer after the war at such date as Parliament may determine.
- 5/ The excess profits tax is imposed on excess profits net income in excess of the average profits for 1936-39.

TREASURY DEPARTMENT

123

INTER OFFICE COMMUNICATION

DATE October 21, 1941

TO Secretary Morgenthau
FROM Vincent F. Callahan

With regard to your memorandum of October 21st asking if the farm announcements of the Treasury Department were cleared with the Department of Agriculture, I wish to advise that we have not checked the farm announcements with the Department of Agriculture. However, arrangements are being made to check all future announcements with them.

For your information the farm announcements were written by several experienced farm directors of radio stations in the Middle West. These men are actively engaged in broadcasting to farmers every day.

Vincent F. Callahan

TREASURY DEPARTMENT

123-A

INTER OFFICE COMMUNICATION

DATE October 21, 1941

TO George Haas
FROM Secretary Morgenthau

I wish you would find out whether there is any way of our learning whom the real speculators have been recently in cotton, wheat, lard and some of the other commodities. I am really interested.

I wish you would talk to somebody in Secretary Wickard's office. I think it would be very interesting if we could find out whom these people are because I feel that the speculation has had a lot to do with the price rise. Let me know about it as soon as possible.

Meeting arranged at 3:30 Today

*get minutes of meeting.
(meeting not recalled but lists
of speculators were shown
to Haas by Dg. Dept. -*

Every trader in the futures markets for the following commodities, having a position in any one future in any one market equal to or greater than the limit mentioned, must report to the Commodity Exchange Administration daily (or whenever any change in his position is made).

Commodity	Limit
Wheat	200,000 bushels
Corn	" "
Oats	" "
Barley	" "
Rye	" "
Flaxseed	" "
Soybeans	" "
Butter	25 carlots
Eggs	" "
Potatoes	" "
Lard	250,000 pounds
Cottonseed oil	300,000 "
Soybean oil	" "
Cotton	5,000 bales
Cottonseed meal	1,000 tons
Soybean meal	1,000 "
Mill feeds	1,000 "
Wool tops	125,000 pounds

In addition to the above commodities, the Commodity Exchange Administration has similar authority over certain other commodities in which there is at present no futures trading, namely, rice, grain sorghums, tallow, cottonseed, peanuts, and peanut oil.

THE BRITISH SUPPLY COUNCIL IN NORTH AMERICA

124

TELEPHONE: REPUBLIC 7660



Box 680
BENJAMIN FRANKLIN STATION
WASHINGTON, D. C.

October 21, 1941

Dear Mr. Morgenthau:-

My colleagues, who have just returned from an interesting and delightful interlude in your little theatre, wish to join their hearty thanks and appreciation with mine for your kindness in giving them this opportunity of seeing two fascinating films, "The Bomber" and "Revolt in Norway".

Yours sincerely


Morris W. Wilson
Chairman

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

Free Synagogue
NEW YORK

125

Synagogue House
40 WEST 68 STREET
NEAR 63RD ST. N.Y.C.

October 21, 1941.

Hon. Henry Morgenthau, Jr.
Treasury Department
Washington, D.C.

Dear Henry:

My heartfelt thanks for your fine word about Justice Brandeis, which we shall be glad to publish. I have not seen you since the day that Brandeis spoke of you to me in terms of high appreciation. It rejoiced my heart to hear him speak of you as he did. I am grateful to you for having said and done things which brought comfort to his great heart,

Painfully yours,

Abraham S. J.

✓ for other things

SSN:W

126

1601 V STREET N. W.
WASHINGTON, D. C.

October 21, 1941

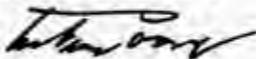
The Honorable
The Secretary of the Treasury
Washington, D. C.

My dear Mr. Secretary:

The changes which have been taking place in the past few weeks in the Far Eastern front and the enormous importance of preventing Japan from stabbing Russia in the back while she faces Germany in Europe have raised new problems in the operations of "China Defense Supplies", about which I would like to have the guidance of the President.

Just as appointments for diplomatic representatives are arranged on the advice of the Secretary of State, I understand it will be proper for a technical representative such as myself to be introduced for a personal interview of this importance through the Secretary of the Treasury. I have had indications that the President would be willing to see me at this time. But because I wish to make sure that I act in accordance with the procedure indicated, I am applying to you for the courtesy of arranging an appointment as early this week as possible.

Respectfully yours,



T. V. Soong

24 27
P. 10 10-22-41

October 21, 1941

Dr. Fois

D. V. Bell

Please send the following cable to the American Embassy, Chungking:
"For Fox from Under Secretary Bell."

As you remember Froese was to assist in establishing the accounting procedure in connection with the operations of the Stabilization Fund. As the Fund is now actively operating I assume that his assignment is completed. As Froese is now needed here in the Treasury I suggest that arrangements be made so that he can return to this country with Beckman or sooner. Best regards."

TELEGRAM SENT

PM

GRAY

October 21, 1941

10 p.m.

AMEMBASSY,

CHUNGKING VIA N.R.

246.

FOR FOX FROM UNDER SECRETARY BELL.

"As you remember Fress was to assist in establishing the accounting procedure in connection with the operations of the Stabilization Fund. As the Fund is now actively operating I assume that his assignment is completed. As Fress is now needed here in the Treasury I suggest that arrangements be made so that he can return to this country with Cochran or sooner. Best regards."

W:FVCL

HULL.
(PL)

DEPARTMENT OF STATE
WASHINGTON

CO
P
Y
In reply refer to
FF FW 893.51/7323

October 21, 1941

The Secretary of State presents his compliments to the Honorable the Secretary of the Treasury and transmits herewith five copies of the paraphrase of telegram no. 404, dated October 9, 1941, from the American Consulate General at Hong Kong concerning the report by the Stabilization Board of its statement of operations for the period, August 18 to September 30.

Enclosure:

No. 404, October 9, 1941,
from Hong Kong.

Copy:vw:10-21-41

Corrected Copy

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Consulate General, Hong Kong.

DATE: October 9, 1941, 5 p.m.

NO. : 404.

THE FOLLOWING IS IN STRICT CONFIDENCE TO THE SECRETARY OF THE TREASURY FROM FOX.

It is decided by the Stabilization Board of the assembly that I report that its statement of operations, covering the period from the 18th of August to the 30th of September, has been drafted and that the Board is now reviewing it. This statement will be sent on the next Clipper. In the meantime, the Board wishes to make the following report for your confidential information:

APPLICATIONS

Rejected: \$ 3,755,881
 Approved: 6,894,108

Rejected: pounds sterling - 224,291
 Approved: pounds sterling - 913,665

The above message is a paraphrase of the original one.

SOUTHARD

MPL

FF:VCL

Copy:vw:10-21-41

C
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Y

131

DEPARTMENT OF STATE
Washington

In reply refer to
FF 840.51 Frozen Credits/3952

October 21, 1941.

The Secretary of State presents his compliments to the Honorable the Secretary of the Treasury and transmits herewith copies of telegram no. 413, dated October 17, 1941, from the American Embassy at Chungking concerning the freezing of Chinese capital in the United States.

Enclosures:

No. 413 from Chungking,
October 17, 1941.

Chungking via H.R.

Dated October 17, 1941

Rec'd 11 p.m.

Secretary of State,

Washington.

413, October 17, 2 p.m.*

The Embassy has received a third person note from the Minister for Foreign Affairs which reads substantially as follows:

"At the request of the Chinese Government the American Government has frozen the capital of the Government and people of China in the United States. For future remittances of the Chinese Overseas, the Chinese Government has now fixed four principles as follows:

(One) The remittances of Chinese residents at various localities abroad shall be concentrated in and handled by the Central Bank of China;

(Two) The Central Bank of China may at places abroad commission the Bank of China, Bank of Communications, or Farmer's Bank of China as its agent banks, but it shall commission only one agent bank each locality;

(Three) Having obtained the permission of the Central Bank of China and the concurrence of the aforementioned agent banks, the banks originally handling remittances of Chinese Overseas, make application

* This telegram is a correction of Message No. 414 from Chungking, dated October 7, 1941.

to do so but shall pay the local currencies received to the agent banks commissioned by the Central Bank of China and the agent banks shall credit the amounts (?) Central Bank's account; and,

(Four) The equivalent in legal tender notes shall be reimbursed by the Central Bank of China to the remitting banks through the commissioned agent banks.

The Bank of China at New York and the Bank of Communications at Manila have been commissioned agent banks for the American continent and the Philippine Islands respectively."

The Ministry requests that the appropriate American authorities be informed of the foregoing in order that they may be able to assist in the matter.

GAUSS

NPL

Copy:bj:10-21-41:eh

PARAPHRASE OF TELEGRAM RECEIVED

134

FROM: AMERICAN CONSUL, SHANGHAI
TO: Secretary of State, Washington
DATED: October 21, 1941, 5 p.m.
NO.: 1523

A United Press despatch from Washington indicating that as a result of recent conference between Chinese and American and British financial representatives Chinese currency at Shanghai may no longer be supported by Stabilization Board disturbed Shanghai yesterday. While discrediting the report with its implied imminent application, Chinese bankers expressed belief that abandonment of official exchange would not be advisable under present Far East circumstances. Such action they believe would promptly result in Japanese or Nanking authorities placing Shanghai foreign trade under complete control perhaps instituting for foreign trade something akin to barter system. If such action were not taken with regard to import trade control, however, black market exchange operations would increase greatly although substantial limitations would be provided by effective export controls in foreign countries.

It would obviously be very difficult for Nanking or Japanese regime to effect any immediate displacement with their own fiat currencies owing to the enormous volume of Chinese national currency in circulation in Shanghai foreign controlled areas and east (?) region. The Nanking regime would probably announce severance of parity between the Chinese national currency and

the

the "Central Reserve Bank" currency and would then establish an arbitrary ratio between these two currencies. There would also doubtless be an announcement for retirement of the Chinese national currency in progressive stages over a considerable period as time would be required for either the Nanking or Japanese regime to print enough of their own notes to make the replacement owing to acute shortages in Japan and here of paper and printing facilities. There would be acceleration of advance in commodity prices in Shanghai in terms of Chinese national currency beyond the present upward pace despite official exchange for imports being available. Public consumption goods shortage might thus become acute and it could be anticipated that there would be serious privation as in Japan, Manchuria and other warring countries. If equitably distributed locally without diversion for outside purposes, present abnormal stocks of most staple commodities in Shanghai are probably adequate for six months requirements or more.

Although perhaps with more restricted allotments it is the belief according to indications that local Chinese bankers expect Stabilization Board policy will be to continue exchange support of Shanghai. This belief appears to be confirmed by official denial today of press reports issued yesterday in Chungking, but it is anticipated that further measures to eradicate local black exchange market will be taken.

LOCKHART

Copy:hr:10-27-41.

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Rio de Janeiro, Brazil.

DATE: October 21, 1941, 9 p.m.

NO.: 1583.

The Bank of Brazil has been informed by the Government banks of Switzerland and Portugal that the latter two Government banks may ship gold to Brazil for safekeeping and the Bank of Brazil replied that it is disposed to cooperate in the matter under reference.

CAFFERY

BB

TO THE DIRECTOR
OF THE FEDERAL BUREAU
OF INVESTIGATION
WASHINGTON, D. C.

PER OCT 24 PM 2:41

1941 OCT 23 10:00 AM

KA:GL:ME

TREASURY DEPARTMENT

137

INTER-OFFICE COMMUNICATION

DATE October 21, 1941

to Secretary Morgenthau

CONFIDENTIAL

FROM Mr. Dietrich

Registered sterling transactions of the reporting banks were as follows:

Sold to commercial concerns	£51,000
Purchased from commercial concerns	£14,000

Open market sterling was again quoted at 4.03-1/2, and there were no reported transactions.

In New York, closing quotations for the foreign currencies listed below were as follows:

Canadian dollar	11-1/8% discount
Argentine peso (free)	.2370
Brazilian milreis (free)	.0505
Colombian peso	.5775
Mexican peso	.2070
Uruguayan peso (free)	.4650
Venezuelan bolivar	.2650
Cuban peso	1/8% discount

We sold \$20,000,000 in gold to the Swiss National Bank, which was added to its earmarked account.

No new gold engagements were reported.

In London, both spot and forward silver were again priced at 23-1/2d, equivalent to 42.67¢.

The Treasury's purchase price for foreign silver was unchanged at 35¢. Lundy and Harman's settlement price for foreign silver was also unchanged at 34-3/4¢.

We made no silver purchases today.

The Federal Reserve Bank's report of October 15, listing deposits of banks in Asia with the New York agencies of Japanese banks, showed that such deposits totaled \$57,741,000, an increase of \$155,000 since October 8. Also reported were selected items from the statement of the Yokohama Specie Bank's New York Agency, which revealed no appreciable changes.

- 2 -

The report of October 15, received from the Federal Reserve Bank of New York, giving foreign exchange positions of banks and bankers in its district, revealed that the total position of all countries was short the equivalent of \$3,591,000, a decrease of \$295,000 in the short position since October 8. Net changes were as follows:

Country	Short Position October 8	Short Position October 15	Change in Short Position*
England**	\$ 831,000 (Long)	\$1,167,000 (Long)	- \$336,000
Europe	2,570,000	2,465,000	- 105,000
Canada	191,000 (Long)	32,000 (Long)	+ 159,000
Latin America	11,000 (Long)	51,000	+ 62,000
Japan	314,000	351,000	+ 37,000
Other Asia	2,115,000	1,979,000	- 136,000
All others	80,000 (Long)	56,000 (Long)	+ 24,000
Total	\$3,886,000	\$3,591,000	- \$295,000

*Plus sign (+) indicates increase in short position, or decrease in long position.
 Minus sign(-) indicates decrease in short position, or increase in long position.

**Combined position in registered and open market sterling.



CONFIDENTIAL

RESTRICTED

G-2/2657-220; No. 524 M.I.D., W.D. 11:00 A.M., October 21, 1941

SITUATION REPORTI. Eastern Theater.

Ground: Information is lacking on the progress of military operations on the Central Front. German armored units appear to be pushing against strong Russian fortifications north, west and south of Moscow. The mass of the German infantry has not yet closed up on their armored divisions.

South of Kharkov, the German High Command claims the capture of Stalino, 100 miles northwest of Rostov.

German troops have gained a footing on the island of Dagos.

II. Western Theater.

Air: The British Air Ministry communique claimed heavy action against Bremen, Wilhelmshaven and Emden, and other parts of northwest Germany during last night. There was daylight action over France but weather conditions limited the action.

No German activity has been reported for this theater last night.

III. Middle Eastern Theater.

Air: British sources admit another bombing of Tobruk, but claim effective action against Axis shipping in the Mediterranean and the bombing of Comiso and Licata, in Sicily, and Benghazi, in Libya.

RESTRICTED

October 22, 1941
9:30 a.m.

GROUP MEETING

Present: Mr. White
Mr. Gaston
Mr. Bell
Mr. Blough
Mr. Thompson
Mr. Schwarz
Mr. Sullivan
Mr. Foley
Mr. Kuhn
Mr. Haas
Mr. Morris
Mrs. Klotz

H.M. Jr: After the meeting I would like Mr. Bell and
Thompson and Mrs. Klotz to stay.

Herbert?

Gaston:

I have a memorandum here about a visit of
Elmer Ireys to McReynolds yesterday. We
decided that that matter of investigations
was really a matter that was up to the
White House to decide, and I asked him to go
over and see McReynolds. When he went over
there he found that McReynolds had with him
Carusi and a delegation from the Civil Ser-
vice Commission. Carusi said flatly that
Hoover wanted to take over those defense
personnel investigations because he did not
want to reveal his records to any other agency,
and he thought there ought not to be two different
field investigations. Elmer Ireys agreed
that there ought not to be two

- 2 -

different field investigations, and we were quite willing, if the White House wished to take it back from us - that it wasn't at our request that we took it, and we were perfectly agreeable to whatever the White House decided.

The upshot of the meeting was that McReynolds said he would write a memorandum to the President recommending that the investigations be turned back to the FBI and that we would have duplicate lists for checking income taxes only. That is the way the thing stands.

H.M., Jr.: That isn't what Mr. - the Attorney General told me.

Thompson: No. His proposal was that Elmer Irey investigate everything but loyalty and subversive activity, but I think that would have been impossible to do.

H.M., Jr.: That isn't what he told me.

Thompson: No.

Gaston: They had changed positions and - well, in the first place we were surprised to find they were there. In the second place, they had changed positions. They wanted to take the whole thing back again. I think Elmer was right. I think our only position could be that we didn't ask for the stuff, and if the White House wants to take it back, let them take it back.

H.M., Jr.: If you were me, Ed, would you call up Francis Biddle and just let him know that he wasn't being straightforward on this with me, or would you let it go?

- 3 -

- Foley: I would let it ride.
- H.M.Jr: McReynolds called me up himself to tell me what he was doing. He didn't want to do it unless it was agreeable to me.
- Gaston: Did he? I am glad of that.
- H.M.Jr: So I know all about it. I told McReynolds last night as far as I was concerned, whatever the President wanted was agreeable to me, and the less outside things I have to fool with, the better.
- Gaston: That is exactly the position Elmer took.
- H.M.Jr: He called me up last night.
- Thompson: The Attorney General has also written you that he is going to undertake the investigations of employees of all branches of the Government who are members of subversive organizations and the investigations will be undertaken without notice to the heads of the agencies or the departments concerned. After the investigations are completed, a factual report will be sent to the head of each agency or department without recommendation, and he would like to know what action is taken. He stated the President approved the plan, and State. I think you will go along with that.
- H.M.Jr: No, I am not going to sign this. You write it back. I want documentary evidence that the President approved it. I won't sign it. I want word from the President of the United States that he wants a Federal OGPU going into every Treasury employee. I want a good stiff letter. You had better let Foley see it.

- 4 -

- Thompson: This is based on the law which gave FBI the direction to make such investigations.
- H.M.Jr: That is all right. I want to know from the President of the United States that he wants them to investigate, because I know what will happen. I mean, they are not going to stop at subversive. They are going into everything. I want it limited to subversive, and I want to know that the President said it. In view of the position, I want to take a stiff position and I want Foley in on it. I want to know from the President of the United States that he wants it, and I may bring it up in Cabinet, that he wants the FBI going in and investigating all Government employees.
- Thompson: I should think they would give us the names.
- H.M.Jr: After all the contacts I have had with the FBI there is no reason for it. I won't sign it.
- Gaston: I have nothing else.
- Foley: Following that situation out on the West Coast of the Yokohama Specie Bank, it wasn't necessary to do anything yesterday.
- H.M.Jr: Are you doing that through the Comptroller's office?
- Foley: Yes.
- H.M.Jr: Does Bell know about it?
- Bell: Nothing more than what I heard yesterday.
- Foley: Everything that we are doing is being done through Preston Delano. I have a memorandum here from him.

- 5 -

H.M.Jr: anything else?

Foley: That is all.

H.M.Jr: John?

Sullivan: Arthur Anderson and Mr. Evans will be here Monday morning. They couldn't come before. They are both coming. Randolph Paul is expected in today. Shoup and Magill will be here tomorrow morning.

H.M.Jr: Randolph Paul will be here today?

Sullivan: That is right.

Klotz: Magill said he could come Thursday.

H.M.Jr: I spoke to him last night, and he said he was coming. Well now, who is going to receive these people?

Sullivan: I am going to talk with Randolph and turn him over to Mr. Blough and have him get the general plan.

H.M.Jr: Well, supposing Randolph Paul comes in to see me at eleven. Will you have him?

Sullivan: Yes, sir.

H.M.Jr: I want to talk to him myself, and I think, Mrs. Klotz, if you will - well, I will see these people - tell Chester Barnard we will have a meeting in my office at 11:00 tomorrow on his proposal. And then Mr. Barnard ought to receive these other people the first thing tomorrow morning, these other people who are coming in, you see, and get them going, Magill and Shoup.

Klotz: Will they contact you (Sullivan)?

- 6 -

Sullivan: I told them I wouldn't be here, and to get in touch with Mr. Tarleau, and he would refer them to Blough.

H.M.Jr: Anyway, they should get in touch with Barnard just as soon as they get here.

Sullivan: Shoup will get in touch with Roy, of course.

H.M.Jr: Anyway, between the lot of you, will you please?

Sullivan: Yes, we will see that they get to Barnard in a split second.

H.M.Jr: You are not going to be here?

Sullivan: Not tomorrow. I would like to have you look over that talk I am going to give out there.

H.M.Jr: Will you show it to Kuhn first?

Sullivan: Yes, indeed.

H.M.Jr: Then Kuhn can bring it to me.

Sullivan: Right.

H.M.Jr: Now, we are all cleared up. I mean, I cleared with Barkley, so everything is all right.

Sullivan: They are going to do it?

H.M.Jr: Yes, we announced it at three o'clock yesterday.

Morris: We have the first report from the New York Federal on the capital issues proposition. I was wondering who you wanted me to work with on that. George Haas and Bell?

H.M.Jr: Yes. And when you have got something that is significant, bring it to me.

- 7 -

- Morris: Well, this first report needs a little study to find out - it doesn't prove anything. We don't know what the amounts are for, and I think we can find out in some cases.
- H.M.Jr: Did you get anything out of your trip to New York last time?
- Morris: Yes, I did, a good deal.
- H.M.Jr: I think you might go up again tonight and spend Thursday and Friday at the Fed and then be back here Monday morning. I want you to get as much as you can on this financing, because I will use you more and more in the financing.
- Morris: All right.
- H.M.Jr: If you spend a couple of days in the Fed with them, I think it would be good.
- Morris: All right.
- Bell: Mr. Secretary, was there a luncheon today?
- H.M.Jr: No, I have Harriman today.
- Bell: Some of the people at that luncheon last Wednesday had an idea there was going to be another luncheon this week. I didn't get that, but they did.
- H.M.Jr: No, we only discuss it when we are not financing. Not today. If you want one next week, we will.
- Bell: No, I didn't particularly want one. They got the impression there would be another luncheon this week.
- H.M.Jr: I think they are right. I think you (Morris) might go up and spend another two days.

- 8 -

I want you really to get proficient and efficient in this. I think two days up there would be helpful with the Fed.

Morris: All right.

H.M.Jr: I will tell them you are coming.

Kuhn: I have nothing.

Blough: Nothing.

H.M.Jr: A little later on I want to go over that tax thing with you (Blough), because I need a little help.

Blough: I am sorry that it is --

H.M.Jr: No, no, it is a good job. I am complimenting you, but I want a little --

Blough: It is supposed to be so easily understood that you can go right through it.

H.M.Jr: Well, you escort me through it the first time.

Blough: All right.

H.M.Jr: What Blough has done, if anybody is interested, he has given me a report on the comparisons of the various incomes in the United States with Canada and England. It is a swell job, if anybody wants it.

Sullivan: I would like a copy of that.

Gaston: Taxes?

H.M.Jr: Yes.

Foley: I would like a copy.

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Gaston: I would like to see it.

H.M.Jr: It is a swell job.

Blough: Just income taxes. All you wanted was income taxes on that, wasn't it?

H.M.Jr: That is right.

Well, you might do inheritance and estate too.

Blough: We would be glad to expand that.

H.M.Jr: I would go right on with excises and everything else.

White: It is highly desirable to do a complete job on them.

H.M.Jr: I would do the whole works.

Gaston: That is what the Brooklyn report was supposed to be on.

H.M.Jr: I want to read Shoup's report. Who has that for me?

White: You have on your desk a report, and you have a summary too.

Gaston: I just handed a copy to Dave Morris.

White: There is one addressed to you which Miss Chauncey has.

Bell: It is quite long.

H.M.Jr: George? Did you get my thing on that food business?

- 10 -

Haas: That is in there. (Handing reports to Secretary.) I talked to Carl Hamilton. I think you told him what you wanted.

H.M.Jr: I would like to see the names. Should I write a letter to Wickard and say I want it?

Haas: It may help.

H.M.Jr: I wish you would try it today.

Haas: There are about twenty commodities. Do you want to start with one, say wheat and lard?

H.M.Jr: Start with wheat and cotton, whichever the big ones are. Ask him which ones he is suspicious of. Who is in charge of that?

Haas: It is a man by the name of Mehl, I think.

H.M.Jr: That isn't the man we used to work with, is it?

Haas: No, he is still over there, but he is not in charge of it.

H.M.Jr: I am terribly interested in this.

Haas: They have the names. They may not give them to me, but they may send them direct to you. You see, it is very important information if it got out in the market.

H.M.Jr: Well, you tell them I would like to have it, and I would be very glad if the man would bring them to me himself, but I want Mr. Wickard to know beforehand that I am getting them.

Haas: I see.

- H.M.Jr: And if the man can do it, I am available at three-thirty today. I will put you down. But if the man would come over and explain it to me, but he should tell Mr. Wickard that I am doing it, that I want it, you see.
- Haas: All right. I think that--
- H.M.Jr: Why not have him come over at three-thirty?
- Haas: All right.
- H.M.Jr: I want you here, Ferdie.
- Kuhn: Three-thirty?
- Haas: Do you want me?
- H.M.Jr: Oh, definitely.
- Haas: Here is the report by denominations. The report shows that the ten thousand denomination accounts for over half of the sales.
- H.M.Jr: I see. Let's try and bring him over here at three-thirty today, but tell him to tell Mr. Wickard that I am doing this, you see.
- Haas: Yes, sir, I will.
- H.M.Jr: I mean, I want the Secretary's office to know it.
- Schwarz: For our information, I understand the Federal is seriously considering an extensive educational campaign on Consumer Credit.
- H.M.Jr: Well, do you want to get a free ride in connection with Foreign Funds, Ed? Do you know about it?

Foley: No.

H.M.Jr: Supposing you (Schwarz) talk with Ed.

Schwarz: I will tell him.

H.M.Jr: Anything else?

Schwarz: That is all.

H.M.Jr: Harry?

White: You asked about the industrial consumption of silver. This year there will be seven million ounces more used than last year. There is fifty-one million ounces as against forty-four, instead of the doubling which somebody gave you the figure of.

H.M.Jr: Now Bell or somebody came in and told me - on this future business, when we wanted to give up this future contract, you said it was going to be seventy million.

Bell: Somebody told us the industrial would require between seventy and eighty million ounces.

White: I guess that is also right, but twenty-five million ounces of that, approximately, is re-used old silver. The industrial use of silver this year totals seventy-nine million ounces as against sixty-seven million ounces the previous year, but of that, from twenty-five to thirty million ounces is reworked old silver.

H.M.Jr: The figure that was given me, the arts use eighty million.

White: Well, that is true.

H.M.Jr: No statement was made as to whether it was

new silver or old silver.

White: No, but I thought the statement was made that there was a terrific increase in the use of silver.

W.H.Jr: That was my interpretation.

White: Oh, I see. Well, there is some increase, but it is about seven or eight million ounces.

W.H.Jr: Then this thing was brought to my attention to release this future contract because there is a shortage of new silver.

Bell: It was indicated that there would be a shortage in the next few months of industrial silver in the market.

White: Well, I don't know. We called up OPM, Bureau of Mines, and OPA and all the organizations who would know about it and to their knowledge there are no new uses of silver that are significant beyond what we have. There is some increased use for soldering and so forth, but it is all rather small.

W.H.Jr: Who asked us to release this?

Bell: I don't know. I haven't my memorandum now, but somebody in New York who couldn't buy it. Is there any silver coming in from abroad?

White: Some from Canada and some from Mexico. There is very little to my knowledge coming in from anywhere else. I will check up on that. Peru, we get some.

Bell: We get Canada's production.

White: We get Canada's production. We get Peru.

- 14 -

Bell: They can't buy domestic production because it is too high.

White: No, they can't buy silver that is mined in the United States. That sells for seventy-nine cents an ounce - seventy-one cents an ounce.

H.M.Jr: I told Bell to ask you (Foley) to prepare some legislation on that.

Foley: All right, he hasn't spoken about it.

Bell: No, I have not. I have got it on my desk.

H.M.Jr: I see.

White: You asked about exports to the Philippine Islands. It took us a long time to get that. We had to send them about three cables. They had to build up an organization, but we have been getting it. Three days ago we got the first batch coming in in three weeks. I have the report here on one page. I can give you the report briefly orally, or I can leave it with you.

H.M.Jr: I would like you to talk to me about it. Are you familiar - because Mr. Wallace told me there has been - after it was decided at Cabinet that Jesse Jones should buy up all the output of the Philippine iron ore mines--

White: Yes, I am familiar with that story.

H.M.Jr: I never got it from you. There was a vote, and they voted seven to one to go ahead.

White: Well, they did that at the last defense meeting and there was a report of the meeting and at this meeting, which I didn't attend but just got the notice of, they

brought that one notch forward. I can give you the whole story whenever you want it.

H.M.Jr:

Tell Fitz I want to see you, and I want to know the whole Philippine situation.

White:

Yes. This letter from Soong - I think the appropriate thing is merely to telephone to ask him to come in to see you and tell you what he has got on his mind before you make an appointment. Is that all right?

H.M.Jr:

Tell Fitz.

White:

And have Fitz get in touch with him?

H.M.Jr:

Yes.

White:

That is all.

H.M.Jr:

Dan?

Bell:

You have been interested in these dismissed employees, people we had to dismiss because of consolidating offices throughout the country. This is just to let you know that the New York office where they consolidated Albany they had to let fifty-eight employees go, and they were all replaced and forty-seven of them were placed at higher salaries, which averaged about forty-three percent more than they were getting with the Treasury. It shows that the Treasury is paying too little or the others are paying too much, I don't know which.

Did Governor Neely call you or McNutt?

H.M.Jr:

He called me and said he had talked to Paul McNutt. McNutt said he had nothing to do with that.

Bell: That isn't true. A fellow by the name of Powell is the Executive Director to the Board and Mr. Powell wrote to the Director of the Unemployment Compensation Commission in West Virginia on September 22 and told them that if they didn't straighten out their matter of collecting and depositing the unemployment taxes that they would not give them any further administrative funds. That is what he is faced with now. They won't give him a further allotment for administrative funds.

H.M.Jr: Will you take it off my shoulders and see it through?

Bell: It isn't on your shoulders.

H.M.Jr: Then will you prepare a letter for me today?

Bell: On that subject, we got a very nice letter from Altmeyer on the cooperation of the Treasury and the money we have saved them through these depositories.

H.M.Jr: Could you prepare a letter this afternoon for me to sign?

Bell: To whom, Neely?

H.M.Jr: Yes. And I will send a copy to McNutt. What?

Bell: Yes.

H.M.Jr: Could I have that this afternoon?

Bell: Yes. Do you want to cover the depository situation too?

H.M.Jr: Whatever it is.

Bell: I covered that very fully in a letter to Congressman Edmiston who was also interested in the letter. I will enclose a copy of this letter if you want to.

H.M.Jr: Do that. If it is to McNutt, let's send him a copy of the whole business.

Bell: If you are interested for just a minute; what they do is bring all of the collections of checks on these taxes into Charleston. Then they divide them seventeen ways and send them to seventeen banks for collection. Those banks collect them and hold that money for a period of anywhere from ten to fifteen days, and then the central office draws checks on those seventeen banks and deposits those checks in a Charleston bank, and the Charleston bank holds them for ten or fifteen days, and then they draw a check and send it in to the Treasury.

Now, those banks have anywhere from eight hundred fifty to a million dollars on deposit for anywhere from two to three weeks all the time of collected funds.

H.M.Jr: Well, if you will fix me up a letter, I will sign it this afternoon.

Bell: It is the only state in the Union that hasn't come around to our system. We have been out there and talked to them, and they just won't budge.

H.M.Jr: Anything else.

Bell: That is all.

Thompson: Here is that letter on Mr. Barth.

H.M.Jr: How did you fix it?

Thompson: Well, fortunately he is on the Foreign Funds roll which is now subject to classification. It will have to go through the Civil Service Commission.

H.M.Jr: Ferdie, hang on to this until this afternoon for me.

Thompson: The next grade would be fifty-six.

H.M.Jr: Is that all?

Thompson: That is all.

H.M.Jr: Thank you all.

Original to Mr. Thompson to investigate. **158**

Brunswick, George Agent \$2000
423 Mellon St. SE Internal Revenue
Washington, D.C.
Member Washington Committee for Democratic Action
Member American League for Peace and Democracy

Carter, Kenneth H. Messenger
733 13th NE Internal Revenue
Washington, D.C.
Member Washington Committee for Democratic Action

Casady, Lauren W. Sr. Economist \$4600
6702 5th NW Monetary Research
Washington, D. C.
Member Washington Committee for Democratic Action
Member Washington Book Shop

Chaiken, Al Clerk \$1620
1346 Quincy St. NW Accts & Deposits
1027 Quebeck St NW
Washington, D.C.
Member American League for Peace and Democracy

Chambers, Robert Sr. Attorney \$4600
Gaithersburg, Md. Customs
Member Washington Committee for Democratic Action
Member New York Committee, American Committee for
Democracy and Intellectual Freedom
Signer, Open letter for Closer Cooperation with
the Soviet Union

Cohen, Ethel Stenographer \$1800
303 Roosevelt St.
Bethesda, Md.
Member Washington Committee to Aid China

Duffield, Mr. Eugene Asst. to Secretary \$7000
Great Falls St.
East Falls Church, Va.
Member Washington Committee for Democratic Action

Feter-Bass, L. Leslie Sr. Economist-Analyst \$5200
2333 S. Nash St. Bureau of Internal Revenue
Arlington, Va.
Member Washington Committee for Democratic Action

Eichholz, Robert B. Sr. Atty. \$4600
1423 34th St. NW Office of Secretary
Washington, D.C. Internal Revenue
Member Washington Committee for Democratic Action

Feinberg, Benj. Clerk \$1620
2115 Eye St. NW
Washington, D.C.
Member American League for Peace and Democracy

Fox, Melvin Clerk
3002 P St. NW
Washington, D.C.
Member Washington Committee to Aid China

Glasser, Esther G. Clerk \$1620
3616 Conn. Ave. NW
Washington, D.C.
Member Washington Committee for Democratic Action

Glasser, Harold Director, \$6500
339 Willard Avenue Monetary Research
Friendship Heights, Md.
Member Washington Committee for Democratic Action

Gottlieb, Lillian Printers Acct. \$.72 per hr.
Clifton Terrace East Engraving and Printing
14th & Clifton St. NW
Washington, D.C.
Member Washington Book Shop

Johnston, J. Richard Attorney
4135 N. Henderson Rd.
Arlington, Va.
Member Washington Book Shop

Kaplan, Herbert Architect \$3300
4141 N. Henderson Rd.
Arlington, Va.
Member American League for Peace and Democracy

Kaplan, Morris Associate Chemist \$3200
4119 Davis Pl. NW Customs - Baltimore, Md.
Washington, D.C.
Member Washington Committee for Democratic Action
Member American League for Peace and Democracy

Katz, Sol Agent \$2000
2106 N St. NW Internal Revenue
Washington, D.C.
Member Washington Book Shop
Member Washington Committee for Democratic Action

Kaufman, Harry Agent \$2000
1801 Wyoming Ave. NW Internal Revenue
Washington, D.C. Baltimore, Md.
Member of Washington Book Shop

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Kessler, Gertrude Operator \$1370
 1139 Conn. Ave. NW Engraving and Printing
 200 11th St. NE SW
 Washington, D.C.
 Member American League for Peace and Democracy

Klein, Bertha Typist \$1440
 3616 Newark St. NW.
 Washington, D.C.
 Member Washington Book Shop

Letcher, Isadora A. Operator \$.96 per hr.
 1835 5th St. NW Engraving and Printing
 Washington, D.C.
 Member Washington Committee for Democratic Action
 Member Marian Andersen-Citizens-Committee

Levenstein, Myrtle Stenographer \$1620
 1430 Belmont St. NW Internal Revenue
 Washington, D.C.
 Member of Washington Book Shop

Lloyd, Mary M. Asst. Printer \$2304-39
 1747 E St. NW
 Washington, D.C.
 Member Washington Committee for Democratic Action

Logue, Francis S. Engineer and Draftsman \$3200
 1322 I St., NW Procurement
 Washington, D.C.
 Member American League for Peace and Democracy
 Member Washington Committee for Democratic Action

Lyman, Henry L. Assist-Struck
 145 Carroll St. SE Engineer
 Washington, D.C.
 Member of Washington Book Shop

McDonald, W.O. Electrician \$10.50 p.d.
 3016 11th St. NW Engraving and Printing
 Washington, D.C.
 Member Washington Committee for Democratic Action

McKennis, Mrs. Golden V. Printers Asst. \$.60 per hr.
 40 N. St., NW Engraving and Printing
 Washington, D.C.
 Member Washington Committee for Democratic Action

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Morse, Andrew S. Messenger \$1260
 413 11th St. SE
 Washington, D.C.
 Member Washington Book Shop

Pollock, Tillie W. Asst. Clerk-Stenographer \$1620
 219 N. Glebe Rd. Coast Guard
 Arlington, Va.
 Member Washington Committee for Democratic Action

Robertson, John R. Sr. accountant and Auditor \$3500
 1835 K St. NW Internal Revenue
 Washington, D.C.
 Member Washington Committee for Democratic Action

Rollins, Milton Sr. Clerk \$2000
 5809 14th St. NW Internal Revenue
 Washington, D.C.
 Member Washington Committee for Democratic Action

Smith, Daisy C. Operator f.&A per hr.
 1028 Lament St. NW
 Washington, D.C.
 Member Washington Committee for Democratic Action

Spiegel, Ann B. Clerk-Stenographer \$1800
 1929 16th St. NW Research and Statistics
 Washington, D.C.
 Member Washington Book Shop
 Member Washington Committee for Democratic Action
 Member American League for Peace and Democracy

Stanton, E.C. Sr. Mech. Engr. \$4800
 4815 Battery Lane Procurement Division
 Bethesda, Md.
 Member Washington Committee for Democratic Action

Stein, Pearl B. Typist \$1440
 1228 Eye St. NW Internal Revenue - New York, NY
 Washington, D.C.
 Member Washington Committee for Democratic Action

Sturner, William A. Principal Clerk \$2300
 4910 3rd St. NW Internal Revenue
 Washington, D.C.
 Member Washington Committee for Democratic Action
 Member American League for Peace and Democracy

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Butten, James Attorney
 1020 - 19th St. NW General Counsel's Office
 Washington, D.C.
 Member Washington Book Shop

Topley, Cleveland L. Foreman \$3250
 1527 N. Randolph St.
 Arlington, Va.
 Member Washington Committee for Democratic Action

Kalton, Dorothy (Mrs. Stanley Surray)
 2715 Cortland Pl., NW
 Apt. 1 Asst. Legislative Counsel \$6500
 Washington, D.C.
 Member American League for Peace and Democracy

Ford, Anna Sr. Clerk \$2300
 1223 Vermont Ave. Internal Revenue
 Washington, D.C.
 Member American League for Peace and Democracy

Wechsler, Sanford L. Clerk \$1625
 1733 N St., NW
 Washington, D. C.
 Member Washington Book Shop

Testfall, Benton E. Chemist \$3200
 104 Allegheny Ave.
 Takoma Park, Md.
 Member Washington Book Shop

White, Harry Dexter Under Clerk \$1380
 8610 Fairfax Rd.
 Bethesda, Md.
 Member Washington Committee for Democratic Action

Wilmerding, Lucius Tech. Asst. \$5000
 2823 N St. NW Accts and Deposits
 Washington, D.C.
 Member Washington Committee for Democratic Action

Rollner, Mrs. Herbert J. Chemist
 1341 30th St. NW
 Washington, D.C.
 Member Washington Committee for Democratic Action

Wood, Herbert S. Sr. Technical Advisor \$6500
 2909 Brandywine St. NW Internal Revenue
 Washington, D.C.
 Member Washington Book Shop
 Mr Sponsor, Washington Committee to Aid China

October 22, 1941

TO: THE SECRETARY
FROM: MR. GAS ON

I have asked Elmer Ireby to get everything they have on Roswell Russell and Roy V. Fox.

The substance of the matter is that with respect to the man Russell, Henry J. Paynter, formerly of the AP in New York and formerly of PM, was added to Bob Horton's public relations staff and he was interviewed by Russell. He wrote you saying that man was employing a line of conversation very much like that of Wheeler and Nye. He did not mention the man. We readily found out who it was. We interviewed Russell and found he had entertained those views. He admitted he had said something along that line to Paynter in conversation with him. Russell is a young fellow, an Alcohol Tax man. He is the Middle Western type of apparently Isolationist who has been influenced by the Wheeler-Nye propaganda. We did not think there was any basis on which we could prefer charges against Russell. We simply sent him back to his Alcohol Tax post.

The second case was that of Fox. He is a Customs Agent, formerly attached to Erwin May's force in Berlin. The complaint on him came to me from David Cushman Coyle who relayed it from Barrow Lyons, newspaper man, formerly financial writer, also employed by Bob Horton. The story was much the same. We looked into the records and found Fox was the man who interviewed Lyons. Fox was confronted with the story and said it was not true, but we found by talking to his associates upon the Interview Staff that he had expressed the views in talking to them that it was a concerted drive by certain elements to get us into this war and it was none of our business -- in effect, the Isolationist point of view. We acted in the case of Fox the same as we did in the case of Russell. We turned him right back to Customs and I have talked to John about the case. Fox

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is on his previous assignment of Customs Agent at Norfolk. Vlopond, Assistant Collector down there, does not think highly of him on the ground that he talks too much and does not accomplish much, but we are planning in the case of both of these men to keep them under observation and in the case of Box I hope to learn something more about him through Erwin May.

I don't think that in either case we have any more than evidence of views and argumentative disposition that unfits them for the work of interviewing candidates for defense jobs.

OCT 22 1941

My dear Governor:

Reference is made to your telephone call yesterday concerning certain proposed banking arrangements in connection with the Unemployment Insurance funds in the State of West Virginia. In the conversation you referred to a communication which had been received from a Mr. Powell and apparently assumed that he was connected with the Treasury Department.

Upon looking into the matter, I find that you probably were referring to Mr. Oscar M. Powell, Executive Director of the Social Security Board. Mr. Powell, it appears, addressed a letter under date of September 22, 1941, to Mr. Homer V. Hanna, Director, Department of Unemployment Compensation, Charleston, West Virginia, on the subject of the procedure and practices of the West Virginia Department of Unemployment Compensation, with respect to the handling of contributions collected from the time of receipt until their subsequent deposit to the State's credit in the Unemployment Trust Fund in the United States Treasury. This letter, I am informed, stated that the Social Security Board had taken the position that the procedure now in use in West Virginia did not conform with the provisions of existing law requiring the immediate deposit of contributions into the Unemployment Trust Fund in the Treasury and suggested corrective action in order that there may be no delay in the consideration of grants for administrative expenditures.

For your information as to the part which the Treasury has taken in this matter, I enclose a copy of a letter addressed to Honorable Andrew Edmiston, House of Representatives, by Under Secretary Bell under date of July 17, 1941. As you will note from this letter, the Treasury has no direct jurisdiction, but is cooperating with the Social Security Board to the extent of making available certain essential depository facilities which, I am informed, have already been accepted by all States with the exception of West Virginia. The use of the facilities afforded by the Treasury's depository system has been advantageous not only to the Social Security Board in reducing grants for administrative costs, but has been of substantial benefit to the individual State Unemployment Trust Funds inasmuch as the arrangement for immediate clearance of the contributions into the Unemployment Trust Fund of the Treasury permits the retention of the funds upon an interest-bearing basis to the fullest extent.

It is regretted that the Treasury could not entertain a proposal to maintain balances of Treasury funds in more than one bank in West

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Virginia as a basis for servicing the State Unemployment Insurance Funds as experience has demonstrated that consolidation of the accounts in one bank is much more economical from an administrative standpoint, and minimizes the balances which it is necessary for the Treasury to tie up in the form of fixed deposits with banks for this purpose.

As previously indicated, this arrangement has been perfected in all States except West Virginia to the mutual advantage of such States and the Social Security Board. There is no direct benefit to the Treasury under this arrangement, but on the contrary, the Department has incurred some expense in supervising the depository set-up and in maintaining balances of Government funds as offsets to the costs incurred by the banks in servicing the State accounts. The Treasury has been glad to cooperate with the Social Security Board in the matter, in view of the broad interest of the Federal Government in promoting and sponsoring the Social Security program.

Very truly yours,

(Signed) H. Morgenthau, Sr.

Secretary of the Treasury.

Honorable Matthew M. Neely,
Governor,
State of West Virginia,
Charleston, West Virginia.

Enclosure. *Send*

EDB:ew 10-22-41

*M. M. C.
File in Mr. Bell*

October 22, 1941

Dear Mr. McNutt:

For your information, I am enclosing herewith a copy of a letter which the Secretary is today sending to Governor Healy of West Virginia, together with a copy of my letter to Congressman Edmiston dated July 17, 1941.

Very truly yours,

Under Secretary of the Treasury

Honorable Paul V. McNutt,
Administrator,
Federal Security Agency,
Washington, D. C.

DWB:ce

17-011

My dear Mr. [redacted]

I have your letter of July 8, 1941, in which protest is made against a proposed plan to place the Unemployment Insurance funds in the State of West Virginia in one bank instead of twenty-one. In view of your interest in this proposed change, this Department has reviewed the matter and the following is submitted for your information.

As you are aware, while the Social Security Act, as amended, places certain duties upon the Secretary of the Treasury, the administration of that act generally is vested in the Social Security Board. Early in the development of the program the Social Security Board called the attention of the Treasury to an administrative problem which had arisen involving banking facilities in the various States.

The Social Security Board pointed out that certain sections of the Social Security Act provide, in effect, that the Board shall make no certification for payment to any State, from funds appropriated by the Congress for the purpose of assisting in the administration of State unemployment compensation laws, unless the Board finds that the law of the particular State includes, among other things, provision for "the payment of all money received in the unemployment fund of such state, immediately upon such receipt, to the Secretary of the Treasury to the credit of the Unemployment Trust Fund established by section 904;" and "expenditure of all money requisitioned by the State agency from the Unemployment Trust Fund, in the payment of unemployment compensation, exclusive of expenses of administration; * * *"(underscoring supplied).

It was brought to the attention of the Treasury also, that the General Counsel of the Social Security Board had raised the question of the legality of permitting the retention of balances in clearing accounts and benefit payment accounts in banks as a basis for the servicing of such accounts. The Board requested, in view of the broad interest of the Federal Government in promoting and sponsoring the social security program, which, in effect, is a cooperative arrangement between the States and Federal Government, that the Treasury authorize the use of its established depository system in connection with the clearing accounts and the benefit payment accounts in the several States. The Treasury agreed to provide the necessary depository facilities under certain conditions, one of which was that the State agencies would cooperate to the extent of consolidating both their clearing accounts and benefit payment accounts in order that the most economical and expeditious arrangements might be perfected. There

is an direct benefit to the Treasury under this arrangement, but, on the contrary, the Department has incurred some expense in supervising the depository set-up and in maintaining balances of Government funds in banks as an offset to the cost incurred by the banks in servicing the State accounts. The Department has been advised by the Social Security Board that the use of the Treasury's depository facilities has saved an approximation of \$1,000,000 per year, which it otherwise would have been necessary for the Board to grant to the States as costs of providing the necessary banking service. Furthermore, this arrangement is of substantial benefit to the individual State unemployment trust funds inasmuch as it permits retention of the funds in the unemployment trust fund in the Treasury upon an interest-bearing basis to the fullest extent.

With respect to the situation in West Virginia, it is noted from the records of the Treasury that the benefit payment account is divided among four banks and the clearing account among sixteen banks. So far as the Treasury is aware, West Virginia is now the only State in which these accounts are so divided. It appears, upon the basis of the best information available in the Treasury, that the Unemployment Trust Fund of the State of West Virginia, due to its present system of dividing accounts and failing to take advantage of the banking facilities which the Treasury stands ready to make available, is losing a substantial amount in interest, inasmuch as there are, at times, balances in banks aggregating about \$1,000,000, which, if deposited in the Treasury, would be earning interest at a rate averaging approximately 2½% per annum. Whether the Unemployment Compensation Commission of the State of West Virginia is complying with the terms of the Social Security Act is, of course, a question for determination by the Social Security Board.

Mr. H. . . Rabon, a representative of this Department, conferred with Dr. G. C. Robertson, Director of the West Virginia Unemployment Compensation Commission, on May 28, 1941, regarding a proposed modification of the procedure now being followed in handling the benefit payment account and the clearing account. Dr. Robertson was advised that the Treasury could not consider placing balances of its funds with the various banks handling the accounts as a basis for services rendered. In accordance with arrangements which have been set up in other States, it was suggested that the entire benefit payment account and clearing account be placed with one bank. The Charleston National Bank, Charleston, West Virginia, was mentioned as the depository bank since this bank had been previously contacted by the West Virginia agency and the Treasury concerning the matter. With the knowledge and consent of Dr. Robertson, Mr. Rabon called at The Charleston National Bank and discussed the matter with Mr. Mason Crickard, Vice President. The bank agreed to handle the entire benefit payment account and clearing account. Mr. Rabon returned to Dr. Robertson's office and advised him that tentative arrangements had been made with the bank.

The Treasury has been informed by the Social Security Board that the consolidation of the State accounts has been of great benefit, not only to the State Commissions, but in the administrative functions of the Board. This procedure is now in operation in all States, with one or two exceptions. As previously indicated, the matter is not, of course, under the direct supervision of the Treasury, but in view of your interest in this question, I have taken the liberty of explaining the Treasury's position at some length. Should there be any further information which you might desire, please do not hesitate to call upon this office.

Very truly yours,

W. A. Bell
Under Secretary of the Treasury

Honorable Andrew Edmiston
House of Representatives
Washington, D. C.

:mlp
7/12/41