

Book No. - 456

continued

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October 31, 1941
8:30 a.m.

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RE SOCIAL SECURITY (COMPULSORY SAVINGS)

- Present:
- Mr. Odegard
 - Mr. Gaston
 - Mr. Barnard
 - Mr. Kades
 - Mr. Paul
 - Mr. Buffington
 - Mr. Morris
 - Mr. Friedman
 - Mr. Shere
 - Mr. Blough
 - Mr. Coe
 - Mr. Bell
 - Mr. Foley
 - Mr. Groves
 - Mr. Sullivan
 - Mr. Kuhn

H.M. Jr: The thing that we are starting with, gentlemen, is how much money do we have to mop up, and fortunately - I don't know who wrote this memo, so I can criticize it. Don't tell me. (See attachment).

Barnard: Well --

H.M. Jr: Don't tell me.

Barnard: Oh, excuse me. We all wrote one and he tried to make English out of it.

H.M. Jr: Who did?

Barnard: You didn't want to know (laughter).

Flough: He is not here.

H.V.Jr: Well, you pointed at Kuhn. Well, the fact remains, I have read it three times, and I can't understand it. I have had a high school education. You just go backward and forward and don't get anywhere. I would like to have it explained to me. I have read it three times and I don't understand it. Now, who wants to explain it and let me ask questions?

Barnard: Why, you do it.

Fell: Is that memo the same as we got?

Flough: No, that is another one, but you have much the same thing in this one.

Bell: I see.

Flough: Do you want me to take a crack at it?

H.V.Jr: It is like the kind of question they put to the quiz kids. Only they can answer. Go ahead. You try to explain it, and I will ask the questions.

Flough: Let me try.

H.V.Jr: Go ahead.

Flough: The problem, as I understand, that they faced and that you face, and we all face, is this: how much spendable income must be mopped up? Now, they took it - to make their problem relatively simple, they took a month, the month of June, 1942, and they decided to compare the month of June, 1942 with the month of June, 1941, to see how much more income there would be, how much more or less goods there would be, and accordingly how much more spendable income would have to be mopped up

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if the goods were to go around for the income that was available. So that this is based on June, '42 as compared to June, '41, but all the figures placed on an annual basis, so that it is the rate of, for a whole year - but it is the rate that would prevail in June, 1942.

H.V. Jr:

I have got that.

Blough:

So they start out by finding out what will happen, is likely to happen to the defense spending in the Federal Government, and they conclude that the defense spending in the Federal Government will be about fifteen and one half billion dollars more in 1942 than in 19-- than in June, 1941.

H.V. Jr:

This is where we begin to part company. When you say fifteen and a half billion more, more than what?

Blough:

That the expenditures in June, '42 will be at the rate of fifteen and a half billion more than they were in June, '41.

(Mr. Gaston entered the conference).

H.V. Jr:

What were they in June, '41? You don't say.

Blough:

That is the first criticism made of this memorandum yesterday. Do you have that figure?

Friedman:

About ten billion dollars.

H.V. Jr:

Now, what was it in June, '41?

Blough:

At the rate of ten billion dollars. About eight hundred million dollars a month.

Bell:

That is about it.

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H.M. Jr: Now, wait a minute, in June, '41 we were doing what?

Blough: We were spending for defense at an annual rate of ten billion dollars.

Bell: That is something over eight hundred million dollars a month. That is about right.

H.M. Jr: Somebody else criticized this, did they?

Blough: Mr. Barnard.

H.M. Jr: You were spending at a rate of how much?

Blough: Ten billion dollars a year.

H.M. Jr: All right. Then you come to June --

Blough: '42.

H.M. Jr: And you are spending at the rate of --

Blough: They believe it will be at the rate of twenty-five and one half billion dollars a year.

H.M. Jr: That figure doesn't appear in the memo, either. Twenty-five and a half billion. All right. Or --

Blough: An increased rate of expenditure of fifteen and a half billion dollars.

H.M. Jr: Now you see we are getting somewhere. I suppose if I knew what "X" was I could have done it, but I didn't have my slide with me.

Blough: There is no way you could have gotten at this.

H.M.Jr: I don't think so either. Now we have got the fifteen and a half billion.

Blough: That is right. Now, they also figure that taxes and revenues will be coming in at the rate of about six billion dollars a year more in June, '42 than in June, '41. Do you have the annual rate there?

Friedman: Nine in June, '41.

H.M.Jr: How much in taxes?

Blough: In June, 1941 the taxes were coming in at the rate of nine billion dollars a year.

H.M.Jr: Yes.

Blough: And they anticipate that in June, 1942, taxes will be coming in at the rate of fifteen billion dollars a year.

H.M.Jr: What you do is this: let me just take a minute now and get this thing. 1941, June, you have got fifteen billion - let's see, you have got ten billion expenditures and nine billion taxes. Right?

Blough: On defense expenditures, that is right.

H.M.Jr: So the excess is plus one.

Blough: As far as defense is concerned alone. The non-defense expenditures were about the same for the two periods.

(Mr. Odegard entered the conference).

H.M.Jr: Well, I mean you have got one billion more expenditures than receipts.

Blough: Counting only defense expenditures, yes.

H.M.Jr: Well, that is what you have been talking about.

- Blough: That is right. We are interested, though, in increases and not in absolute amounts.
- H.M.Jr: Well now, wait a minute, I want to get this. I just want to get this. There is one billion excess and in June, '42 - if this isn't the right way, we can go back - the expenditures are twenty-five and a half billion, and the receipts are fifteen or ten and a half. Right?
- (Mr. Sullivan entered the conference).
- Blough: Yes.
- H.M.Jr: And that is how you get the ten and a half? Is that the figure you use?
- Blough: Well, you have fifteen and a half defense expenditures higher in June, '42 than in June, '41. Taxes are six higher. And if you subtract, then you have nine and a half. You should have nine and a half in toto. Subtract the one from the ten and a half, giving you nine and a half, which is surplus.
- H.M.Jr: But the way I have done it, you come out with the same rate.
- Blough: Exactly.
- H.M.Jr: Ten billion expenditure, nine billion taxes, plus one. Twenty-five billion expenditures, fifteen taxes, and you get plus ten. Then you take the one and you have got nine and a half excess as of June, '42.
- Blough: So to date thus far you have got nine and a half excess.
- H.M.Jr: I defy anybody to have gotten that out of that memorandum. All right. Now we have got the nine and a half. What?

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Blough: Yes.

H.V.Jr: All right.

Blough: But now private spending is going to be cut down to some extent because of goods we can't get, consumers' goods and services which are cut off through priorities and business capital which is cut off, savings bonds purchases, and so on are expected without additional definite action on the part of the Government to result in three billion dollars reduction in purchases of certain kinds of goods.

H.V.Jr: I have got to do that again, Roy.

Blough: By June, 1942 it is expected that due to savings bonds, defense bond sales, priorities which are taking away the possibility of producing some goods and so on, that business men won't be spending as fast to build their buildings and new machinery and so on, and that consumers won't be buying as many cars and as many washing machines and a number of other things, so that there will be three billion reduction in consumer spending on consumption goods and services and business spending, so to - in effect to offset this nine and a half excess of Federal spending, there would be three less of the consumer spending.

H.V.Jr: Well, whoever is doing this memo, that three billion has got to - you can't explain it in one paragraph. Anybody reading that, it wants more than twenty words to explain the three billion.

Fell: You could set that whole thing out, couldn't you, Roy?

Blough: Yes, sure.

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Bell: With totals and reductions.

Blough: We probably should have done it that way.

H.V.Jr: All right, that brings you down to six and a half. When did you come in, John?

Sullivan: I beg your pardon, sir? (Laughter).

Bell: He was out looking for a chair.

H.V.Jr: I see. I see you are working for Mr. Ickes and had gasoline trouble.

Sullivan: No, as a matter of fact, I completely forgot about the meeting, and just came down at my usual time (laughter).

Gaston: I wonder if it would help with that three billion if you turned the paragraph right around.

H.V.Jr: This isn't enough for the public to understand. It isn't enough for me. I am the public.

Gaston: I wonder if it would help with that three billion if you turned the paragraph right around and explained that there would be less consumption expenditure on account of certain factors, such as savings bonds, priorities, unavailability of goods, and that would probably result in a net reduction of expenditures of three billion. You can just turn it the other way around.

H.V.Jr: Well, something like that.

Gaston: Yes.

reserves and inability to spend their money and fear of the future, and so on, are expected to increase their corporate reserves at the rate of about a billion dollars more, which brings it down to five and a half. In other words, it is five and a half more spendable income exerting pressure upward on prices.

H.W.Jr: Because you see when we give out these figures we are immediately subject to attack from all sides. We have got to justify this stuff.

Plough: Oh, absolutely. That is why we rather hoped they wouldn't be given out yet.

H.W.Jr: Well, there was nothing given out yesterday. I would contradict this New York Times story, that is all. Go ahead.

Plough: That is the purchasing power side.

H.W.Jr: I mean, I didn't give anybody any figures or details. The Wall Street Journal has an accurate story.

Plough: On the spendable income side, then, there is five and a half billion dollars more. You have come down to that. Now, the next question is, what about the goods which will be available on which to spend that five and a half billion more?

H.W.Jr: That is right.

Plough: Will there be enough more goods or will there actually be less goods?

H.W.Jr: That is right.

... they start with that computation by saying that, as previously indicated, the defense

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expenditures are expected to be fifteen and a half billion more next June, in June, '42.

H.M.Jr: All right.

Blough: Well, now --

H.M.Jr: There is going to be twenty-five and a half billion anyway.

Blough: And there will be fifteen and a half billion more than there was in June, '41.

H.M.Jr: That is right.

Blough: But the total production, including defense, including non-defense, including everything, is not expected to be more than ten and a half billion dollars more by June, '42 than it was in June, '41.

H.M.Jr: Yes.

Blough: I think the language is wrong there, as a matter of fact, because I think it says "civilian", but that is total output of everything, military goods, defense goods, and so on. Well now, if defense spending is going to be fifteen and a half billion dollars more, and total production is only going to be ten and a half billion dollars more, obviously civilian production must come down some because there is going to be fifteen and a half billion more defense production.

H.M.Jr: All right. You have got a figure of six and a half billion. Now --

Blough: There is that much more spending --

H.M.Jr: That is six and half more. Now you are talking about production.

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Blough: You are talking about the goods on which that money is to be spent.

H.V.Jr: You are mixing the two up. You can't use the same set of figures on spending and - what has that got to do --

Blough: The defense spending represents production. It is estimated that the --

H.V.Jr: Now let me ask you the question because this is the most muddle-headed thing I have ever read. What is the total production of all kinds of goods in June, '42?

Blough: Do you have that figure?

Friedman: Yes. About a hundred point five. About a hundred and a half billion dollars.

Blough: One hundred and one half.

H.V.Jr: A hundred and a half. All right, how much of that is for defense?

Blough: Twenty-five and a half.

H.V.Jr: That leaves seventy-five, then.

Blough: It leaves seventy-five exactly for civilians.

H.V.Jr: All right. Now, what do you do with that figure?

Blough: Just let it alone for a minute.

H.V.Jr: All right.

Blough: Then in June, 1941, instead of it being a hundred and a half, it was ninety.

H.V.Jr: Right. The defense was 100"

Blough: And the defense was ten.

Bell: It was eighty-five, wasn't it?

H.M.Jr: No, it said here ten.

Blough: Ten, that is right, at the rate of ninety for June, '41.

H.M.Jr: That brings you down to eighty.

Blough: That brings you down to eighty.

H.M.Jr: Now, that leaves you - there is five billion dollars less goods to go around.

Blough: That is right. Five billion less goods --

H.M.Jr: Five billion less goods to go around. All right, now what do you do then?

Blough: And five and a half more spending.

H.M.Jr: Gives you ten and a half.

Blough: Gives you ten and a half.

H.M.Jr: Do you add the two, is that correct?

Blough: That is the idea.

Shere: That is right.

Friedman: Well, there is one deduction, because in getting the five and a half we have already allowed a three billion dollar reduction, so out of that five billion dollar reduction, we have already allowed for three billion, leaving two more than is needed.

Blough: My error.

H.M.Jr: Do it again.

Blough: I missed that. We have had a five billion dollar reduction in goods here. As you have calculated, seventy-five against eighty. But in our previous calculation of the money, we said that there would be three billion dollars less spent on those goods, so we have taken that three into consideration already.

H.M.Jr: Yes.

Blough: So that three isn't added.

H.M.Jr: So you only add two?

Blough: So you only add two.

H.M.Jr: Two to five, making seven and a half?

Blough: Two to five and a half, making seven and a half.

H.M.Jr: I think anybody that is fair-minded will agree that this thing has got to be done over again. I mean, nobody can understand it.

Barnard: Well, we all agree to that, I think.

Blough: Yes, I am sure everybody agrees.

H.M.Jr: A poor job.

Barnard: Yes, but I think the fundamental difficulty is, we started with differentials instead of totals, and then the differentials appear out of totals, I think, don't you?

H.M.Jr: Yes, but I go back to it again, it has got to be as good as my boss can speak, so the fellow can understand it, and when he reads it he can understand it the first time.

Frank Knox called me up and said, "Henry, all my life I have heard inflation discussed and I never understood it. Now, for the first time in my life, I understand what inflation is." It is the same thing. After all, this is the foundation on which we are going to spring from, and it has got to be written so that if I stop a fifteen-year old boy or girl on the street and read it to them, they will understand it. Now, that is the test. I can't say "my daughter" any more, because she is a freshman at Vassar, but I mean it has got to be so a fifteen or eighteen year old boy or girl could follow it.

- Flough: It will have to be much longer than that, of course, to do it.
- H.M.Jr: Well, it has to be long enough. Now, who is going to do this? This has got to be done very, very carefully.
- Flough: If you wish, I will take the responsibility to see that it is done.
- H.M.Jr: If you would take the responsibility and then let my two teachers (Kuhn and Odegard) back there go over it, see.
- Would you do that?
- Flough: Surely.
- H.M.Jr: But you get the idea.
- Flough: I think so now.
- H.M.Jr: Get it so it flows, see. It has to be in such shape that even an editorial writer of a newspaper can understand it (laughter).
- Flough: That is asking a good deal, but we will try.

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- Paul: He will try not to understand it.
- Blough: There is one more step here, if I might mention it, that may be disturbing.
- H.M.Jr: What is that?
- Blough: We have seven and a half gap, then, or spendable income needing to be mopped up. Then the memorandum goes on to say that six and a half taxes will, through its direct and indirect effects, take care of the seven and a half.
- H.M.Jr: Yes. And there is one billion dollars hanging in the air.
- Blough: The one billion dollars will come through indirect and secondary effects of the six and a half billion.
- H.M.Jr: Well, that will have to be explained.
- Blough: That is why I brought it up. Mr. "A" spends the money. Mr. "B" then takes it and spends it again.
- H.M.Jr: I have got to explain this to Doughton, too. (Laughter).
- Blough: If I might say so, I think this --
- H.M.Jr: Doughton will think that one billion is the economy.
- Sullivan: He will say that that one billion dollars is really three or three and a half, or four. That is the trouble when you have a mop-up factor.
- H.M.Jr: Well, what you ought to do, Roy, is to take plenty of time and go over this thing and if you would have something Monday, then let everybody jump on you so when I come back Tuesday you will really have something.

Blough: If I might say so, Mr. Secretary, this has been extremely helpful in pointing out the spots where we are just going to get into trouble on it in explaining it to anyone. It was done very hurriedly yesterday.

H.M. Jr: Well, I would rather, in the future, if the people would say, "Well, we are not ready," rather than give me a thing like this. I would much rather you would say, "I am not ready."

So much for that. Are we all together on that, I mean as to the needs?

Barnard: Yes, agreed.

Coe: Not as to the amount of that figure.

H.M. Jr: I take it for granted with the twenty-five people in the room they have given me a correct figure.

Blough: That was the minimum.

H.M. Jr: Well, get together, boys.

Blough: We are together as a minimum, aren't we?

Coe: No.

Blough: I thought you had agreed to all these. Weren't you a member of the technical reviewing group on Friday and Saturday?

Coe: No.

Blough: Well, why weren't you? (Laughter) What do you think it is, Frank?

Coe: I will talk to you afterward.

H.M.Jr:

What is the matter, Coe?

Coe:

Well, I think - I have had comparatively recently, I must say, doubts based on this. This whole analysis indicates a change between June and June. What happens from June to June and what we need to make, what happens to prevent price increases from June to June. Well, we have already narrowed that gap. We have already upped defense expenditure from ten to eighteen billion dollars from June to now. If you want to deal with price increases, presumably you want to prevent price increases from now or January first on, and the differences that you should take should be between that time and June thirtieth, so it seems to me.

H.M.Jr:

Well, I don't want to stop you, but for Heaven's sake, get in, because when I begin to use this figure, it has got to be as near right as the technicians can make it and we have got to be just a little bit smarter about it than anybody else. Now, incidentally, Dr. Viner will be in Monday and I want him to get in on this thing with both feet and believe me, if there is anything technically wrong with it, he will find it, so when he arrives here Monday morning, for Heaven's sake put him on that and he will put his finger on anything that is wrong.

Blough:

I might say, in response to --

H.M.Jr:

Give him a chance right from the beginning.

Blough:

Well, we have been looking and waiting for him.

H.M.Jr:

Well, he will be here Monday. If there is something wrong, he will find it. Let him get on it Monday morning.

Blough:

I think we ought to make clear with you, though,

that whatever we agree - if Mr. Coe raises a question I think it can be handled. What we are agreeing on is the minimum. We can't tell how much more it might be.

H.M.Jr: Well, for my sake, I mean, after all, I go up in June with Dan Bell and we ask for how much taxes? We thought we were all right in June. What was it?

Bell: Well, we started at the end of February to ask for three and a half and before we got to June three and a half wasn't enough. I think the same situation will apply to Coe. You can start today, and by the time you get your plan, three months hence, it will be out of date.

H.M.Jr: Then give me a minimum and a maximum. After all, that gives me -- every Secretary of the Treasury, the first thing he needs, is an alibi. (Laughter)

Blough: Might I ask Mr. Coe a question?

H.M.Jr: You have got to always start with an alibi.

Blough: I would like to ask him a question, since I didn't know this was going on in his mind. In terms of policy, do your doubts go to six as a minimum? Is it too low? Is it too high?

Coe: I think six is too high but I agree with what was just said. This thing probably ought to be tied up with this new program they are talking about. If they get on any such level of expenditures as they indicate in the newspapers, then eight would probably be all right, but for the figures you have, I think it is too high.

Blough: Even for the maximum or for the minimum?

Coe: For the maximum.

Blough: Well, that is something we ought to go into. We certainly had no idea you were in that mental state.

H.M. Jr: Well, is this something you have worked out independently of Harry?

Coe: I have not been at these figures, but it is, as you indicated this morning, a very complicated business and you can't work it out very fast.

H.M. Jr: But you are on it now?

Coe: Yes.

H.M. Jr: I won't press you. Anyway, you have doubts?

Coe: That is right.

H.M. Jr: That the minimum figure is too high?

Coe: I think we can get together.

H.M. Jr: All right.

Blough: We might also put it this way, that the amount we are likely to get in taxes and other methods will not be too high even on your minimum.

Bell: That is right.

H.M. Jr: Has Lauch Currie seen these?

Blough: No.

H.M. Jr: He should. I would like to bring him in again beginning with Monday, too.

Blough: Is there any objection to bringing him in before Monday?

H.M. Jr:

Bell: He was in on the luncheon the other day and heard it discussed. That is as far as it has been.

H.M. Jr: I would like him in on it.

Barnard: You told us not to have him in yet.

H.M. Jr: Well, I would like him now. I didn't say not to have him in.

Barnard: You said we had better confine it to the Department now. Then we got permission to get in to the public who have been working on this thing and for two days we had Shoup in, but we did not get Currie.

H.M. Jr: Well, let's bring him in.

Barnard: You see, all the men who were included were men who were working on this particular problem, some with Henderson and so forth.

H.M. Jr: I think we ought to get him in now. He is all right. Can we leave this?

Blough: Well, we have a lot more here if you want it.

H.M. Jr: On the same thing?

Blough: No, this is on the revenue program and a little memorandum you might use on George and Doughton if you wished.

H.M. Jr: All right, but I want to raise one big thing that I have got in my mind. This is one thing that was brought out by a newspaper man yesterday. He asked us this question. He said, "In this program that you are working on, are you going to give consideration the little fellow who is being discriminated against?" And I told a white lie

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HMJr: Hello.

Secretary
Knox: Hello, Henry.

HMJr: Good morning.

K: How are you?

HMJr: I'm all right.

K: Bad news this morning.

HMJr: Oh, yes?

K: They got one of our destroyers and sunk her.

HMJr: Oh, gosh.

K: A crew of about a hundred and twenty-five. We don't know how many lost their lives or whether any lost their lives for that matter. We have no word on the casualties, but we just got the word - the flash - that she was sunk this morning about 5:40 about seven hundred miles south and west of Iceland.

HMJr: Is that just for me?

K: What?

HMJr: Is that information just for me?

K: No, no. I'm just releasing it to the press.

HMJr: Oh, you are.

K: Henry, what I called you up about aside from that was the matter of the Coast Guard.

HMJr: Yeah.

K: I don't know what Harold Smith's interest in it is, but he keeps calling us and wanting us to get that thing straightened out; and - have you any objection now to our going through with the

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thing along the lines which Waesche and Stark have worked out, which leaves all of the shore activity and so forth....

EMJr: No, no. I'm - you can do it today.

K: Do it today.

EMJr: Yeah.

K: Okay.

EMJr: Do it today.

K: That'll be fine.

EMJr: Is that all right?

K: That's all right. It couldn't be better.

EMJr: Well, you can do it today. I don't know - where does Harold Smith get in on this?

K: I don't know whether the President - he must have been talking to the President. He called up Jim yesterday.

EMJr: Oh.

K: And Jim told - I just got a note from Jim this morning which said that Smith asked me if I had talked with you. I told him not to do anything until I had talked with you.

EMJr: No, I'd be - if you fix it up, I'll initial it so that there's no question.

K: All right, fine.

EMJr: If you get it - I hope to - I'm hoping, I don't know whether the President's changing, but I hope to leave when he does on the train.

K: Leave what?

EMJr: I think he's supposed to be leaving around - sometime around early afternoon.

K: I see.

EMJr: So if you want me to initial something, if you could get it over before.

K: Yeah. All right. Fine.

EMJr: What was the spot that this happened?

K: It happened about seven hundred miles southwest of Iceland in a convoy going to England.

EMJr: And everybody was - all the lives were lost?

K: No, no. No, no. I don't know that. I don't know how many lives or any of the lives were lost. There was no word on casualties at all - all the word I got was that she was sunk - torpedoed and sunk.

EMJr: Oh, but you don't know about the lives.

K: I don't know anything about the lives. There were about a hundred and twenty-five men aboard her.

EMJr: I see.

K: And, Henry, this is confidential - we had another one yesterday, but she wasn't sunk. She was hit twice - one of our tankers - one of the Navy tankers was hit twice, and she's coming into port now under her own power; and I'm keeping it quiet until she gets into port so they won't get after her.

EMJr: Well, it's very useful, Frank, for me to know these things promptly, so that if it's something to do to watch the financial market, it helps me, you see.

K: All right. I'll give you the dope, then. I didn't know that.

EMJr: Oh, yes. It's very useful.

K: Well, that won't be released until tomorrow, because she'll get into port tomorrow.

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HMJr: Well, if you told it to your left hand, it would be as secret as that.

K: All right. I'll be careful to remember that.

HMJr: Right.

K: All right, Henry. Good-bye.

(The Secretary held a telephone conversation with Secretary Knox.)

He said he is releasing information there was a destroyer that has been sunk.

Gaston: U.S.?

H.M.Jr: U. S. destroyer with a hundred and twenty-five men on board. They don't know what lives were lost. That was Frank Knox.

Herbert, he asked me whether they could go ahead with the Coast Guard today on the basis of we keeping the shore stations and so forth and so on, and they take over the rest. I told him yes, to go ahead.

Gaston: Would that be the plan we outlined, they take the deep sea stuff, everything above a hundred and twenty-five feet?

H.M.Jr: As we agreed.

Gaston: I don't see any reason why they shouldn't. I think the time has come.

H.M.Jr: I told him to go ahead and he said that for some reason or other Harold Smith has been in on it, and muddied the whole thing up.

Gaston: Should I call somebody?

H.M.Jr: You had better call Waesche and tell him that I agreed to it. I agreed to the plan as it was worked out as between Waesche and Stark. You had better tell Waesche that I agreed to it.

Gaston: You don't want me to call anybody else, Smith or Knox?

H.H.Jr:

I don't see where it is any of Smith's business.

Bell:

I think it is an executive order under the President's regulations. It has to go through the Budget. That is where he gets in to it.

Gaston:

We had probably better draft a formal order, then.

H.H.Jr:

Then will you take it? I agreed to it and said I would initial it before noon today.

Gaston:

Right.

(Mr. Gaston left the conference.)

H.H.Jr:

Now, what I want to ask you gentlemen is this. You take a man like the newspaper reporter or the Government worker or any white collar worker, and his cost of living is going up steadily and you apply the same rate of taxation to him as you do to the man whose earnings may have tripled or quadrupled because he is working in a defense plant. It is just not fair. How can you get around that?

You make the fellow who is a bookkeeper or a Government worker on twenty or twenty-five or thirty dollars a week or a college professor, if you will, with the increased cost of living going up, and he knows that a boy can go into a plant at sixteen years old and after a couple of months earn sixty and seventy-five dollars a week.

Odegard:

As a matter of fact, Mr. Secretary, it is worse than that because many colleges are going to have to cut salaries because of declining income.

H.H.Jr:

Before I get into it any deeper, I would like

to have a little discussion at that level, because you talk in your memorandum to me - I read all this this morning - about morals. Well, isn't there some way that we can equalize that? It isn't fair. Now, as I remember it in your original suggestion, you had something about taking a certain percentage of the increase.

Barnard: Yes, sir.

H.M.Jr: I would like to have somebody lead off either pro or con on that basis because all of this stuff gets back to what is fair. You can jam the stuff down peoples' throats and that is just what we don't want to do.

Sullivan: Well, you talked about not wanting to freeze bigness in corporations. Any differential here freezes bigness in individuals. In other words, you are giving preferred treatment to the fellow who has had a good salary for a long while as against the fellow who hasn't had a good salary and is just making it now.

H.M.Jr: It doesn't ring a bell, John. It doesn't ring a bell with me.

Sullivan: All right. Here is a man earning three thousand dollars. He has been making it for five years. And here is another man who has been in a hospital, has had illness, hasn't been able to earn money, owes a lot of money. He comes back up and he makes three thousand dollars. They are earning the same amount. Why should the fellow who has had tough luck --

H.M.Jr: Well, that is an exceptional case. You are saying that because the fellow was industrious and smart and was able to earn three thousand dollars a year for five years, that you should

just not give him any credit for that.

Sullivan:

No, it isn't entirely due to his own industry or his own smartness. Maybe he was in a particular trade that was doing well at that particular time. Maybe the other fellow was in a trade that wasn't doing very well. How about the selectees that are coming out of camp now? Are we going to base them on twenty-one dollars a month?

H.M.Jr:

Well, I don't know. You are just putting the other side.

Sullivan:

I am.

H.M.Jr:

Do you believe in it?

Sullivan:

I do.

H.M.Jr:

Do you believe in what you are saying?

Sullivan:

Yes, I do. I also believe that you are quite right when you say that the fellow on a fixed salary is the fellow that is going to get it in the neck, but the reason he is going to get it in the neck is because of employing all his talents he can't increase his income by so much as one penny, whereas a fellow out in business or a profession, by working a little harder, working a little longer, being a little smarter, can earn bigger fees or commissions and can increase his income.

Harvard:

There is a good deal in it and something should be done to mitigate it, but when you get in to a regular maelstrom like we are in now, it seems to me you have got to deal with the broad lines of equity and it isn't equitable for this great mass of people that are going to be on the lower incomes here not to get treated

harder than the fellows that don't get any movement at all. You can't change the whole blamed economy just because some people are frozen at a level. I don't think it is practical to try to carry the idea of equity too far, but just as far as it is reasonably convenient to do it but not to take into account these fellows that are going from twenty dollars a week to fifty dollars a week doesn't seem to me to be right, whether you do it by forced savings or an excess profits treatment.

H.M.Jr:

Well, that is the point that I am making.

Barnard:

Yes, sir. I think you are right about it. If you kill it on the basis of fine spun treatment, it is not worth while. But the first thing we are trying to do, Mr. Secretary, the thing that hits the fellow with the fixed income harder than anything else, is inflation. That is a form of taxation which is an injury to the Government and which is a terrible injury to him, more than anything else, and to take ten percent out of him now and save him fifty percent indirect taxation by inflation later would be a benefaction, but I think we have got to get it in the minds of the American people and everybody else that this business of chasing the cost of living up is the thing you can't do.

Everybody has got to sacrifice. They can't live on the same scale. The way to save the cost is to cut out the things that cost the money. We haven't understood that sufficiently yet, it seems to me.

H.M.Jr:

Let me just ask Randolph Paul a question. Whether you believe in it or not, for the moment as a technician, see, and you can tell me after-

ward whether you believe in it, but as a technician can you think of some way that you could differentiate between the fellow who is getting three or four times as much in a munitions industry as against the white collar fellow? Is there some way as a technician that you could recommend? Then we could discuss whether it is good or not.

Paul: I don't see any way that is practicable. It is just like the problem we had in connection with excess profits. It is impossible to work out any practical scheme to differentiate between the man whose increase in income is due to the defense activity and the man whose increase in income is a normal development of his age and the development of his personality in that market.

H.M.Jr: You don't think of any way?

Paul: I wish I could but I can't think of any way.

H.M.Jr: You don't know of any?

Paul: No, I don't.

H.M.Jr: Let me ask you this. I am not a technician. Couldn't you make a difference in the amount you pay back?

Paul: Well, I don't know that I quite understand.

H.M.Jr: Let's put it this way. Supposing we have the fifteen percent tax, to use round figures, on the fellow that is earning a hundred dollars a week. That is making it easy for me. That is fifteen dollars. Last year - disregarding the fact that he was a soldier; you will have to make some provision for that, if he was in the service - he was getting 1000 dollars and he went

from fifty to a hundred. And then the number two man has been earning on the average for the last three years fifty dollars a week and you tax him fifteen percent. Well, that fellow, just using my own figures, of the seven and a half we would set aside half of his money in savings and the other fellow who has gone up double, we won't give him anything back.

Paul: But the difficulty --

H.M.Jr: I mean, I am just - you see? I am just throwing that out. I mean, the fellow who is getting double, we just won't give him anything.

Paul: I think that is a good principle --

H.M.Jr: And in between that you could scale it.

Paul: That is true, Mr. Morgenthau, but our first initial difficulty is to get at and segregate the people whose rise in income is due to the defense activity as distinguished from the people who are normally rising because, say, they are in their twenties and they are going up every year in a perfectly normal way without any relationship to defense. I don't think there is any particular problem about the selectee because you can make a general rule for that case, but I don't know any way of distinguishing millions of people who are going up in a perfectly normal way and who would go up in a perfectly normal way if there were no defense activity whatever. If I did I would certainly like to get at some such method.

H.M.Jr: Well, I am not going to take a licking so easily. It is an awfully big principle and I don't - just because it has never been done that you should demand the necessary and their

on the basis of what you are going to pay them back.

Paul: Well, I will be very glad to direct my thought to that problem.

H.M.Jr: After all, this isn't exactly comparable, but let me tell you what we did in New York State. It is a little bit comparable, you see. I would like everybody to think about it. I mean, just to say, well, the thing is so difficult we can't do it, isn't a satisfactory answer to me.

I just wonder whether we can't group people, possibly. This is the example I was going to give. When Mr. Roosevelt first became Governor of New York State, you who lived in the State might know this, the town of Rye was the richest district in the State of New York on the basis of assessed valuation.

Therefore, the town of Rye got the greatest State aids for schools and roads and we went in and made a study and decided that we just would reverse that process and that the County of Hamilton, which is in the Adirondacks, which has the lowest assessed valuation, would get the most aid for its schools and roads, and that system is still in effect, and I worked on it and had a lot to do with it.

Well, up to that time it was always accepted, take your valuation, the richer the town the

more help it gets, and in Rye, I think, we had something like two thousand dollars per mile to help it and Hamilton County might get two or three hundred dollars. I am just using the example that State aid to schools and roads had always been one way. Mr. Roosevelt came in and let me help him and we reversed the thing. So you can do original thinking on it.

And just because the white collar fellow made the same contribution in taxes during the last war and had to pay exactly as much through the cost of living, I am not satisfied we have got to go through the same process this year.

Do I make myself plain? I mean, if you could do the one thing, which was entirely an original approach --

Barnard:

I want to throw one thing in here which seems to me --

H.M.Jr:

And - excuse me - the other thing we did, we took all State tax on real estate off, too. There is no New York State tax on real estate.

Paul:

Well, I am far from opposed to the original approaches to the subject.

H.M.Jr: I know. That is why I am addressing myself to you. I mean, that is a challenge to everybody in the room. If after two or three days you say it is impossible, all right, but I certainly don't want to take it as impossible after two or three minutes.

Odegard: Mr. Secretary, would it be necessary to think of necessary devices if you had a tax system that was truly progressive?

Blough: Yes.

H.M.Jr: I don't know. But I will leave it here and let everybody think about it. Let people think about it.

Paul: Yes, I will think about it very seriously.

Blough: I wouldn't like to have you think that nobody has thought about it, Mr. Secretary.

H.M.Jr: I don't insult you. (Laughter)

Bell: You haven't found the answer.

Blough: We are all with you on the principle, but we just haven't gotten the answer yet.

H.M.Jr: Maybe you are not smart enough.

Blough: I wouldn't be surprised. (Laughter)

H.M.Jr: Well, smarten yourself up a little bit.

Blough: I just wanted to indicate that I for one believe in the principle, but like Randolph Paul, thus far I haven't found out a way to make the distinction.

H.M.Jr: I am just throwing it out as a challenge to everybody. Maybe there is no answer and

maybe there is.

Now where do we go from here? I am sorry to have taken up so much time, but I thought it was important. What do I read next?

Barnard: Go ahead Roy.

Blough: You have in your hand a memorandum (see Attachment 2), briefly explanatory, which you might wish to use either in talking with Mr. George and Mr. Doughton or in your own--

H.M. Jr: Read it out loud.

Blough: And also two pages in which the program we have been thinking about, the group has been thinking about, is summarized. Everybody has a copy.

H.M. Jr: May I just say one other thing? The very fact that you leave that billion dollars floating, because that is going to stay in the company's treasury, shows that we haven't done a complete job on that either.

Paul: That is right.

H.M. Jr: I mean, there is another loophole. You just say, "Well, we can't reach that billion dollars," and that billion dollars is there because it is going to stay in the treasury, which indicates there is also something left undone.

(Mr. Gaston returned to the conference.)

(Secretary held a telephone conversation with Secretary Knox and Admiral Stark.)

October 31, 1941
9:40 a.m.

Secretary
Knob:

Hello, Henry.

MrJr:

Frank, since you called me, Ingersoll called
Waesche.....

W:

leen.

MrJr:

.....and told him that on orders from
Forrestal.....

W:

That's all right.

MrJr:

.....now wait a minute, please - that you
and I'd come to an agreement that you were
going to take over the entire Coast Guard.

W:

No, no, just the - we'd never take over the
entire Coast Guard, Henry, anyway. If we
take it over, we'd turn it back to you anyway -
the portion we don't use.

MrJr:

Well.

W:

I don't know what the formality is, but it
leaves you in possession of all those shore
activities. We don't want anything to do
with those.

MrJr:

Well, what you told me was - at least as I
understood it - for the moment, you just want
to take over all our sea-going stuff and leave
us.....

W:

Well, I don't know just what the formality is;
but I'm told - Admiral Stark told me this -
we take over the whole damn thing and then
return to you those things that we don't do.

MrJr:

Well, do you mind.....

W:

They'd function just the same - exactly as they
are now. There's no change in their functioning
at all.

MrJr:

Do you mind checking, and - because.....

- K: Well, he's right here with me. Let him talk to you. He's been through this before, and I haven't.
- HMJr: All right.
- Admiral Stark: Mr. Secretary.
- HMJr: Talking.
- S: It - Wessche knows just what that is. The arrangements which we made long ago in case we did this were taken up with him, very much the same as in the last war; and while the Navy takes over the Coast Guard, all those functions which are purely local and Coast Guard functions, they continue under their own administration just as now. They'd hardly notice any difference; and if you'd like, I'll give you a memorandum on it.
- HMJr: Well, that - I mean, it wasn't what Secretary Knox told me this morning, and I'm afraid he didn't understand it; or at least, maybe I didn't understand him. The net result was, I didn't understand - what Secretary Knox told me this morning, he'd like to go ahead and take over our sea-going - whatever we've got left of the ships. The in-shore stuff in the harbors and so forth. That was what he understood. I know about the plan in case we get into war. Hello. And there's no argument about once war is declared, I mean, as far as I'm concerned.
- But in the interim, now, if that isn't what you're to have in mind - I mean, if you're proposing to go the whole way as though we were at war.....
- S: Yes. Well, that's what we were.
- HMJr: Well, Mr. Knox didn't tell me that. I mean, you can check with him.
- S: My feeling about it is this, Mr. Secretary. We don't want to start, if we get in the war - and we may - we don't want to be suddenly

confronted with a whole lot of things to do, where we can get the thing running smoothly and in perfectly harmony beforehand. And that is the reason for getting this; wherever we can we're doing that.

HMJr: Um huh. Well, Admiral, I'm the last one that's going to argue with you. If you'll just tell me what you want, see?

S: Yes, sir.

HMJr: And if that's going to help you, I'm for helping you.

S: Well, that's fine; but we want to take over just as though war had been declared.

HMJr: Well, if that's what you want, all right.

S: Yes, sir.

HMJr: I mean, just so I know.

S: Well, that's it.

HMJr: Well, if that's what you want, all right.

S: All right, fine.

HMJr: I mean, because I want to - the last thing in the world is to be any stumbling block. I want to accelerate your job, see?

S: Yes, sir. Well, that's fine, Mr. Secretary; that's what we want.

HMJr: Well, it wasn't explained to me that way; but if that's what you want, Okay.

S: All right, sir.

HMJr: Thank you.

S: Right. Good-bye.

Gaston: Stark is not frank with Knox.

H.M.Jr: That is a kind word. When a man puts it up to me on that basis, there is only one answer, knowing that Waesche told me he wants to go under the Navy in case of war. So what is the use of quibbling about a few days.

Gaston: And that stuff with Knox, that they didn't want the shore things, they would transfer them back, that just isn't so. There is no way they can transfer them back. We are all right. We understand the whole thing now.

H.M.Jr: You know my memory is pretty good.

Gaston: Of course. I heard what Knox said just now. He didn't understand it, and he didn't tell you what Stark wanted.

H.M.Jr: No.

Gaston: But now we are to go ahead and permit them - agree to--

H.M.Jr: Let them have anything they want.

Gaston: What they want is the entire Coast Guard immediately.

H.M.Jr: O.K. There is no use waitin' until the last second. I believe Knox. Knox wasn't told the facts.

Gaston: No, that is right.

(Mr. Weston left the conference.)

Blough: I don't know how much of this you will want.

H. M. Jr: Go ahead and read it. You have got a half hour and then we will have to stop.

Blough: "When I appeared before the Senate Finance Committee on August 8, 1941, I pointed out that, in the light of rapidly changing conditions, the all-out defense program would necessitate all-out taxation, that much more revenue would be required not only to strengthen the government's fiscal position but especially to maintain economic stability and prevent 'inflationary price rises which threaten to increase the cost of the defense program, unbalance family budgets, and seriously disturb our economic life.'

"Since that time the price rises have been accentuated and cost of living has gone up substantially. The cost of living in the United States has risen over 5½ percent during the last five months. From August to September alone it rose by almost 2 percent. An intensive study of the problem of meeting this inflationary threat has been under way for several months and certain tentative conclusions are now at hand. They have such an important bearing on the immediate fiscal program that I wish to summarize them for you."

And then this material we have already discussed would be inserted here, assuming you were giving this to Doughton and George or the Committee or something like that, so that page 2, page 3, and up to the end of the first paragraph on page 4 is material we have already gone over on the fifteen and a half billion and the ten and a half billion and so on.

H.M.Jr: Go ahead.

Blough: I will not read that unless you wish it.

H.M.Jr: No, don't read it.

Blough: On page 4, beginning the first full paragraph.

"For technical reasons the figures given above were computed as of the month of June 1942. The need for increased tax revenue would not be quite as great in January 1942 but will be very much greater than the revenue to be derived from laws now in effect. Furthermore, beyond June 1942, the needed rate of increased taxes may be even greater than for June 1942.

"It should be very clear that the burden of the taxes necessary to hold down price rises will be no greater than the burden of the price rises themselves. If the cost of living goes up 5 percent, it imposes in effect a 5 percent gross income tax without exemption on the lowest income groups in the country. Inflation imposes burdens as real as taxes but in the case of inflation the money does not go to the government."

H.M.Jr: Instead of using June '42, would you mind using for the calendar year '42?

Blough: The figures are not on that basis.

H.M.Jr: They should be, shouldn't they?

Blough: No, there is a long story to that. I am not going to tell you the story. But the way in which the figures had to be drawn up, it was necessary to take a point in an accelerating program, and they took June 1942, and on

a further examination they may consider that that would be equivalent of the average and we ought to go into that with Mr. Coe.

H.M.Jr: I think that would be more intelligible to people. They will say, "Why June?" I think they will be suspicious that you picked a month which made the thing look the worst, so I would much rather you would say "for the average of the calendar year."

Blough: We will get Mr. Shoup in and have him proceed on that idea, see what he can do.

H.M.Jr: People will be suspicious. "Why just June? It is a trick."

Go ahead.

Blough: "It should not be necessary to mention the very serious evils of inflation and the great importance of preventing it. We are all familiar with the way in which it burdens the great bulk of the population, including the lowest income groups, financially embarrasses State and local governments, increases the cost of defense materials, gives opportunities for profiteering and otherwise harming and demoralizing the people. What I would like to stress is that we have reached the point where vigorous action is needed now - without delay - if we are not to have an accelerated, destructive inflationary price rise.

"The problem of preventing inflation needs to be attacked simultaneously on all fronts. I have repeatedly said that non-defense expenditures should be reduced and that it is important for individuals to increase their purchases of defense bonds. From time to time I have mentioned other methods

that should be adopted to help stave off destructive price rises. But all these plans together will fail if the deficit now estimated at \$12.6 billion for the fiscal year 1942 continues to grow and the Federal Government continues to pour out purchasing power to consumers without at the same time taking back a very substantial part of the increase in the form of taxes. The money is being paid out now. If the taxes are to help prevent price increases they must be imposed at once and collected currently with the income payments."

H.M. Jr:

Ferdie, I want an example, see, something a little picturesque about the fellow with the money bulging in his pockets and the shelves half empty, something to get the thing home, you see. After all, the same store that you go into today that you went into last year and you look at it. Well, twenty percent of the shelves are empty, or thirty percent, you see. I mean, something picturesque. I mean, a man goes in and it isn't there, but, on the other hand, his pocket is ten or fifteen percent fatter, you see.

Kuhn:

Yes.

H.M. Jr:

I mean something like that so that he will get it. He will say, "Well, that is right. I have got more money, but by golly I went in the other day and I couldn't get any nails and I couldn't get any salmon, and I couldn't get this, and I had trouble buying condensed milk, and I couldn't buy any cheese."

I know what he is talking about, but this language is two dollar language.

- Paul: Then, Mr. Morgenthau, you could picture how the people split up the few items there are on the shelves. They are all scrambling in and bidding up the price on them.
- H.M.Jr: And we don't want to have queues in front of the grocery stores the way they have in Oslo.
- Paul: Or world series crowds there.
- H.M.Jr: I think Oslo would be a little better. (Laughter) But we don't want queues in front of our stores. Something like that, Ferdie. You can improve on it undoubtedly.
- Blough: Mr. Kuhn hasn't had a crack at this yet.
- H.M.Jr: But I am just thinking. I want to make it a little picturesque and at the same time drive it home. Just a little color.
- Kuhn: It could be done whenever you mention price rises by changing the rising cost of living. That would drive it home all through this.
- H.M.Jr: Something.
- Go ahead.
- Blough: "For this reason I propose to present to the Congress a major revenue raising program. The program roughly consists of three parts: (1) Taxes to be imposed as soon as possible and to be collected beginning January 1, 1942; (2) other major tax increases and changes to increase revenue and to balance the impact of the anti-inflation program on small incomes;" - you may want that spelled out. It is spelled out later. "... (3) changes to close important loopholes

in the tax system and to remove hardships which have developed under the tax laws.

"1. Anti-inflation taxes which should be imposed immediately.

"The first recommendations relate to taxes which should be imposed at once so that collection may begin January 1, 1942. They are taxes which will withdraw purchasing power from consumers before it is spent.

"The first recommendation for anti-inflationary taxation is the imposition of a new supplementary tax on net income to be withheld at the source on salaries, wages, dividends, bond interest, and similar items and collected quarterly throughout the year on other incomes. These taxes would thus be collected in so far as possible like the payroll taxes. They would, however, have personal exemptions and credits for dependents. It is recommended that the rate of this tax be 15 percent and that existing personal exemptions and credits for dependents be allowed. It is estimated that this tax will yield about \$2.8 billion at present income levels."

We are not all agreed about those exemptions in rates, but we put that in in the light of our discussion.

H.M. Jr: For this purpose it is all right.

Blough: "It is recommended second that the payroll taxes for old-age and survivors' insurance be increased."

H.M. Jr: Excuse me, that means it would be seven fifty and fifteen hundred?

Blough: That is right. Perhaps it should be spelled out in here, but that is what it means.

H.M. Jr: Sure.

Blough: "It is recommended second that the payroll taxes for old-age and survivors' insurance be increased. These taxes are at the present time imposed at a rate of 1 percent on employers and 1 percent on employees and are scheduled to rise on January 1, 1943, to 2 percent on employers and 2 percent on employees. The recommendation is that this increase be made one year sooner than was scheduled. It will be recalled that no increase was made on January 1, 1940, when it was originally scheduled.

"Further, it is recommended that as soon as practicable, the Social Security Board's program relating to the extension of coverage for old-age and survivors' insurance and unemployment insurance and the revision of the unemployment insurance system should be enacted."

Of course I don't know if that will have been publicly presented by that time.

H.M. Jr: Well, this is for the President, George, and Doughton.

Blough: "The change with respect to unemployment insurance involves an additional 1 percent tax on the employees.

"I would like to stress the very great importance of considering and passing these two tax increases at once in order that the money may be taken out of the hands of consumers before it can be spent by them,

thus reducing the inflationary pressure of the increased defense expenditures.

"2. Other changes to increase revenue and to balance the impact of the anti-inflation tax program.

"The additional social security payroll taxes and the new supplementary individual income tax would fall very largely on the low income classes. Substantial increases in other taxes are necessary to balance the burden of these taxes, to restore an equitable distribution of the total tax load and to raise the revenue needed to finance the defense effort.

"It is recommended that the surtax rates in all brackets of the individual income tax above \$2,000 be increased; that the excess profits tax be made more effective; that the corporation income tax be increased; that the estate and gift tax rates be increased and the exemptions lowered; and that the defense excise taxes be extended to important items requiring diversion for defense purposes.

"In circumstances that require the imposition of heavy direct taxes on low incomes, it is especially undesirable to leave under-taxed corporate profits arising from defense expenditures. The present excess profits tax fails to reach a substantial amount of such profits. The excess profits tax could be made more effective in a number of ways. For example, a larger portion of such excess profits would be taxed if the tax were computed using an average of the taxable excess profits under the average earnings method and the invested capital method."

H.M.Jr: No, take that out for the time being.

Blough: That is a compromise between your earlier position and theirs.

H.M.Jr: I am not giving up so easily.

Blough: O.K.

H.M.Jr: Just take that out.

Blough: Or do you want it restored to your original position?

H.M.Jr: No, no.

Blough: Just don't say anything?

H.M.Jr: "... should be made more effective in a number of ways," period. I don't want to lose my nickname with the President. He addresses me now as "Six-Percent" Morgenthau. That is the way my memos come. I don't want to give it up so easily. I like it.

"The present profits tax could be made more effective in a number of ways."

Blough: "Defense excise taxes applied to strategic items can play an important role in diverting consumer demand from goods which can only be produced by using resources required for defense. Selective defense excise taxes alone cannot, however, absorb a sufficient amount of consumer purchasing power to prevent inflation.

"3. Changes to prevent avoidance and promote equity.

"Finally, in an all-out tax program, it is

extremely important that all known avenues of tax avoidance be closed. This is desirable for fiscal reasons, for the promotion of equity and for the maintenance of morale."

H.M.Jr: You have got everything in there except prohibition.

Blough: We can put that in if you wish it. (Laughter)

"It is recommended that the privileges relating to community property income be eliminated; that joint returns of husbands and wives be made mandatory for income tax purposes; that insurance companies be taxed more adequately; that excessive depletion allowances be eliminated; that the undistributed profits of corporations be taxed to the shareholders or, alternatively, some privilege tax for retention be imposed upon the corporation; that tax exemption be eliminated with respect to future issues of State and local obligations and the exemption on outstanding issues be restricted to taxes now prevailing, and possibly to those prevailing before the rate increases under the 1941 Act; that capital gains be more adequately taxed--"

H.M.Jr: Wait a minute, you are inching in on me.

Blough: How about the restricting taxes now prevailing?

H.M.Jr: What is that?

Blough: That means that this supplementary income tax which we are proposing would not allow tax exempt interest as a deduction. They would tax the State and local present interest.

H.M.Jr: I haven't got time for that part which is new in regard to State and municipals. Have it on a separate piece of paper which I could add or not, but I have got to study it more. Have it so I can slap it in if I want to, but it will take me several hours to think it over. You know my position on it now. Where this departs from my position in regard to States and municipals, let's have that on a separate piece of paper.

Blough: Sure. And maybe a little reason for it.

H.M.Jr: Oh, yes, you had better have a reason, pro and con.

Blough: All right. (Laughter) I am afraid we are not inching in very much.

H.M.Jr: I just want to know.

Blough: "... and that other changes and corrections be made in the statute to prevent tax avoidance."

H.M.Jr: Now, what happens to Sullivan's so-called administrative stuff.

Blough: Well, that is Sullivan's administrative bill in that last sentence.

Paul: One of the most important things in that last sentence is the present racket of pension trusts.

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

Paul: That is the greatest new racket we have.

H.M.Jr: I don't know. I want to - well, now, the way I feel is this, always depending upon what the President wants of me. I am going

up with him at two o'clock. He is staying up there to vote. I thought I would get back here around Tuesday noon unless the President changes his plans. What I would like to do is, you see, these gentlemen are coming in Wednesday morning. I would like to start in at three o'clock Tuesday and have as much as you could have for me, you see, in the way of a memo that we will work from with these people Wednesday morning. You are here right along aren't you, Mr. Groves?

Groves: Yes, sir.

H.M.Jr: You are available?

Groves: Yes, sir.

H.M.Jr: This doesn't take too much--

Groves: I am very glad to be in on it. It is a privilege.

H.M.Jr: I would like very much if you could. It is very useful. Is it all right?

Groves: Yes, indeed.

H.M.Jr: Are we using any of your staff down there?

Groves: Mr. Friedman who is with us.

H.M.Jr: Well, now, could we have something a little bit better, maybe, and a little bit simpler?

Blough: Is it along this line you want it, Mr. Secretary?

H.M.Jr: That is perfect.

Blough: We just develop this further, is that the

idea, and work over the program which is on the other sheets there?

H.M.Jr: Yes. If I could have one thing, possibly. Could you have it maybe at the end, a summation, suggestion 1, so much revenue; suggestion 2, so much revenue.

Blough: That is already here, Mr. Secretary, in that attached memorandum, although it doesn't say, "Suggestion one," and it may be a little more elaborate than you like.

H.M.Jr: No, that is all right.

Blough: Part three, however, does not have the revenue items on it, and we will try to see what we can do about adding those.

H.M.Jr: I think we have come along nicely.

Barnard: I think so.

H.M.Jr: I think we are coming along nicely. Certainly between now and three o'clock Tuesday the technicians can get together on just how empty the shelves are going to be and how fat the pocket books are going to be.

Frank, you come in here telling everybody it is too high and Harry White was in here before telling them they were too low.

Coe: He shouldn't have gone away.

H.M.Jr: Well, what do they call it that they drink down there? Cubalibre? Coca-Cola and rum, is that the drink? Is that what it is?

Blough: That is it.

H.M.Jr: Cubalibre, isn't it?

Blough: So I have been told.

H.M.Jr: Do you think you could be back too, Mr. Paul?

Paul: It will be pretty hard for me to be back--

H.M.Jr: Well, you can be back Wednesday, and then we will get the rebound from what these fellows say. If you are back Wednesday, that will be all right.

Paul: That will be all right. I might be able to get back Tuesday afternoon and vote early.

H.M.Jr: Well, if you could be here at three, it would be very useful.

Paul: Well, I will try. It depends on the weather.

H.M.Jr: If it is like today, there will be no flying.

Paul: I think not. I am going to change and go up on the train.

H.M.Jr: You had better because my pilot told me there is a storm moving in, so you had better get your train reservation. He told me this morning there is a definite storm moving in, a bad storm.

Well, thankyou all. I think we are moving somewhere.

Dept

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October 30, 1941

MEMORANDUM FOR THE USE OF THE SECRETARY
IN OUTLINING THE PROPOSED REVENUE PROGRAM

When I appeared before the Senate Finance Committee on August 8, 1941, I pointed out that, in the light of rapidly changing conditions, the all-out defense program would necessitate all-out taxation, that much more revenue would be required not only to strengthen the government's fiscal position but especially to maintain economic stability and prevent "inflationary price rises which threaten to increase the cost of the defense program, unbalance family budgets, and seriously disturb our economic life."

Since that time the price rises have been accentuated and cost of living has gone up substantially. The cost of living in the United States has risen over 5½ percent during the last five months. From August to September alone it rose by almost 2 percent. An intensive study of the problem of meeting this inflationary threat has been under way for several months and certain tentative conclusions are now at hand. They have such an important bearing on the immediate fiscal program that I wish to summarize them for you.

- 2 -

On the basis of these studies it appears that by June, 1942, the defense spending of the Federal Government will be at a rate of about \$15½ billion per year above the rate of defense spending in June, 1941. It appears that revenues will be coming in during June, 1942, at the rate of about \$6 billion above the rate of June, 1941, such increase being due in part to the effects of the rate increases of the Revenue Acts of 1940 and 1941 and in part to the larger flow of income.

Another \$3 billion, at most, of the increased defense expenditure may be counteracted by a reduction in consumer spending on consumption goods and services and by a reduction of business spending on private capital goods. Such reductions will be caused by defense savings bond purchases, by priorities, by the unavailability of goods and by a number of other restrictive factors.

Finally, \$1 billion is likely to be absorbed by an increase in corporate reserves, and will not reach the hands of consumers.

The total offset to the increased government spending is, therefore, about \$10 billion, leaving \$5½ billion of purchasing power that will be pushing prices upward.

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At the same time that this increased purchasing power will be available for expenditure, the flow of goods for civilian use will be at a reduced rate. Defense needs will, as stated above, require about \$15½ billion more by next June than last June. Yet by June, 1942, the total real output of goods and services will probably be no more than \$10½ billion per year higher than in June, 1941. Hence, civilian output must be cut down by about \$5 billion in the same period. As noted above, \$3 billion of this decline may come about as a result of defense savings bonds purchases, priorities, shortages and other factors, but the rest of the decline must be achieved through increased taxation or other expenditure controls if prices are not to rise.

To absorb the excess purchasing power of \$5½ billion and to also reduce private spending at the rate of an additional \$2 billion, a total of \$7½ billion, will require about \$6½ billion in increased taxes withdrawn currently from the incomes of consumers. The apparent discrepancy of \$1 billion here reflects the indirect effects of the additional taxes. If the decline in private spending due to priorities and unavailability

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of goods is less than the \$3 billion mentioned above, an even larger amount of taxes will be needed. Indeed, the total amount of taxes needed to prevent a substantial rise in prices in June, 1942, may be as high as \$9 billion annually.

For technical reasons the figures given above were computed as of the month of June, 1942. The need for increased tax revenue would not be quite as great in January, 1942, but will be very much greater than the revenue to be derived from laws now in effect. Furthermore, beyond June, 1942, the needed rate of increased taxes may be even greater than for June, 1942.

It should be very clear that the burden of the taxes necessary to hold down price rises will be no greater than the burden of the price rises themselves. If the cost of living goes up 5 percent, it imposes in effect a 5 percent gross income tax without exemption on the lowest income groups in the country. Inflation imposes burdens as real as taxes but in the case of inflation the money does not go to the government.

It should not be necessary to mention the very serious evils of inflation and the great importance of preventing it. We are all familiar with the way in which

it burdens the great bulk of the population, including the lowest income groups, financially embarrasses State and local governments, increases the cost of defense materials, gives opportunities for profiteering and otherwise harming and demoralizing the people. What I would like to stress is that we have reached the point where vigorous action is needed now - without delay - if we are not to have an accelerated, destructive inflationary price rise.

The problem of preventing inflation needs to be attacked simultaneously on all fronts. I have repeatedly said that non-defense expenditures should be reduced and that it is important for individuals to increase their purchases of defense bonds. From time to time I have mentioned other methods that should be adopted to help stave off destructive price rises. But all these plans together will fail if the deficit now estimated at \$12.6 billion for the fiscal year 1942 continues to grow and the Federal Government continues to pour out purchasing power to consumers without at the same time taking back a very substantial part of the increase in the form of taxes. The money is being paid out now. If the taxes are to help prevent price increases they must be imposed at once and collected currently with the income payments.

For this reason I propose to present to the Congress a major revenue raising program. The program roughly consists of three parts: (1) Taxes to be imposed as soon as possible and to be collected beginning January 1, 1942; (2) other major tax increases and changes to increase revenue and to balance the impact of the anti-inflation program on small incomes; and (3) changes to close important loopholes in the tax system and to remove hardships which have developed under the tax laws.

1. Anti-inflation taxes which should be imposed immediately.

The first recommendations relate to taxes which should be imposed at once so that collection may begin January 1, 1942. They are taxes which will withdraw purchasing power from consumers before it is spent.

The first recommendation for anti-inflationary taxation is the imposition of a new supplementary tax on net income to be withheld at the source on salaries, wages, dividends, bond interest, and similar items and collected quarterly throughout the year on other incomes. These taxes would thus be collected insofar as possible like the payroll taxes. They would, however, have

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personal exemptions and credits for dependents. It is recommended that the rate of this tax be 15 percent and that existing personal exemptions and credits for dependents be allowed. It is estimated that this tax will yield about \$2.8 billion at present income levels.

It is recommended second that the payroll taxes for old-age and survivors' insurance be increased. These taxes are at the present time imposed at a rate of 1 percent on employers and 1 percent on employees and are scheduled to rise on January 1, 1943 to 2 percent on employers and 2 percent on employees. The recommendation is that this increase be made one year sooner than was scheduled. It will be recalled that no increase was made on January 1, 1940 when it was originally scheduled.

Further, it is recommended that as soon as practicable, the Social Security Board's program relating to the extension of coverage for old-age and survivors' insurance and unemployment insurance and the revision of the unemployment insurance system should be enacted. The change with respect to unemployment insurance involves an additional 1 percent tax on the employees.

I would like to stress the very great importance of considering and passing these two tax increases at once in order that the money may be taken out of the hands of consumers before it can be spent by them, thus reducing the inflationary pressure of the increased defense expenditures.

2. Other changes to increase revenue and to balance the impact of the anti-inflation tax program.

The additional social security payroll taxes and the new supplementary individual income tax would fall very largely on the low income classes. Substantial increases in other taxes are necessary to balance the burden of these taxes, to restore an equitable distribution of the total tax load and to raise the revenue needed to finance the defense effort.

It is recommended that the surtax rates in all brackets of the individual income tax above \$2,000 be increased; that the excess profits tax be made more effective; that the corporation income tax be increased; that the estate and gift tax rates be increased and the exemptions lowered; and that the defense excise taxes be extended to important items requiring diversion for defense purposes.

In circumstances that require the imposition of heavy direct taxes on low incomes, it is especially undesirable to leave undertaxed corporate profits arising from defense expenditures. The present excess profits tax fails to reach a substantial amount of such profits. The excess profits tax could be made more effective in a number of ways. For example, a larger portion of such excess profits would be taxed if the tax were computed using an average of the taxable excess profits under the average earnings method and the invested capital method.

Defense excise taxes applied to strategic items can play an important role in diverting consumer demand from goods which can only be produced by using resources required for defense. Selective defense excise taxes alone cannot, however, absorb a sufficient amount of consumer purchasing power to prevent inflation.

3. Changes to prevent avoidance and promote equity.

Finally, in an all-out tax program, it is extremely important that all known avenues of tax avoidance be closed. This is desirable for fiscal reasons, for the promotion of equity and for the maintenance of morale.

It is recommended that the privileges relating to community property income be eliminated; that joint returns of husbands and wives be made mandatory for income tax purposes; that insurance companies be taxed more adequately; that excessive depletion allowances be eliminated; that the undistributed profits of corporations be taxed to the shareholders or, alternatively, some privilege tax for retention be imposed upon the corporation; that tax exemption be eliminated with respect to future issues of State and local obligations and the exemption on outstanding issues be restricted to taxes now prevailing, and possibly to those prevailing before the rate increases under the 1941 Act; that capital gains be more adequately taxed; and that other changes and corrections be made in the statute to prevent tax avoidance.

Appendix

Revenue program for 1942

I. Anti-inflation taxes
which should be imposed immediately

1. A supplementary individual income tax collected at source: Impose a new supplementary individual income tax based on surtax net income as at present defined, with the same exemptions as in the income tax at a rate of 15 percent, but the tax is to be allowed as a credit against income for income tax computation. The tax is to be imposed on all sources of income reported at the end of the year but is to be withheld at source only with respect to wages and salaries, bond interest, dividends, and royalties. Proprietorships and partnerships would be required to file quarterly returns on an estimated income. \$2,800,000,000

2. Social security payroll taxes:

A) Increase the payroll taxes for old age and survivors' insurance by 2 percent effective January 1942, thus moving up for one year the increase at present scheduled for 1943. 900,000,000

B) Increase the coverage of the old age and survivor insurance and revise the unemployment insurance plan in accordance with the recommendations of the Social Security Board and increase the payroll taxes for unemployment by 1 percent-- additional revenue increase over item 2-A. 1,000,000,000

Total Part I 4,700,000,000

II. Other changes to increase revenue and to balance the impact of the anti-inflation tax program

1. Individual income tax: Increase surtax rates of individual income tax on surtax net incomes in excess of \$2,000 beginning with 1 or 2 percent at the lower levels and ranging up to 5 or 6 percent in the higher brackets. 300,000,000

2. Corporation taxes

A) <u>Excess profits tax</u> : Revise basis and increase rates. For example, if the tax were computed using an average of the taxable excess profits under the average earnings method and the invested capital method.	\$ 500,000,000
B) <u>Surtax</u> : Increase rates 2 percent from 6 and 7 to 8 and 9 respectively.	200,000,000
3. <u>Estate and gift taxes</u> : Increase rates and lower exemptions.	300,000,000
4. <u>Defense excise taxes</u> : Increase rates on a few important items as for example, automobiles, refrigerators, and possibly others which might be suggested by the defense agencies.	400,000,000
Total Part II	1,500,000,000

III. Changes to prevent avoidance and promote equity

1. Mandatory joint returns

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2. Insurance taxation

A) Align the treatment for stock and mutual insurance companies other than life.

B) Revise basis for taxation of life insurance companies to provide more adequate taxation.

3. Eliminate percentage depletion or otherwise revise the present scale of excessive allowances.

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A) Eliminate the exemption with respect to future issues of State and local obligations.

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RE: dmd
10/30/41

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2. <u>Social security payroll taxes:</u>	
A) Increase the payroll taxes for old age and survivors' insurance by 2 percent effective January 1942, thus moving up for one year the increase at present scheduled for 1943.	900,000,000
B) Increase the coverage of the old age and survivor insurance and revise the unemployment insurance plan in accordance with the recommenda- tions of the Social Security Board and increase the payroll taxes for unemployment by 1 percent-- additional revenue increase over item 2-A.	1,000,000,000
Total Part I	4,700,000,000

II. Other changes to increase revenue and to
balance the impact of the anti-inflation tax program

1. <u>Individual income tax:</u> Increase surtax rates of individual income tax on surtax net incomes in ex- cess of \$2,000 beginning with 1 or 2 percent at the lower levels and ranging up to 5 or 6 percent in the higher brackets.	200,000,000
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3. Corporation taxes

A) <u>Excess profits tax</u> : Revise basis and increase rates. For example, if the tax were computed using an average of the taxable excess profits under the average earnings method and the invested capital method.	\$ 800,000,000
B) <u>Surplus</u> : Increase rates 2 percent from 6 and 7 to 8 and 9 respectively.	200,000,000
3. <u>Waste and gift taxes</u> : Increase rates and lower exemptions.	200,000,000
4. <u>Defense excise taxes</u> : Increase rates on a few important items as for example, automobiles, refrigerators, and possibly others which might be suggested by the defense agencies.	400,000,000
Total part II	1,600,000,000

III. Changes to prevent avoidance and promote equity

1. Mandatory joint returns

If mandatory joint returns cannot be enacted then at least a change relating to community property income is recommended.

2. Insurance taxation

A) Align the treatment for stock and mutual insurance companies other than life.

B) Revise basis for taxation of life insurance companies to provide more adequate taxation.

3. Eliminate percentage depletion or otherwise revise the present scale of excessive allowances.

4. Tax the profits of corporations remaining after corporation income and excess profits taxes to the shareholders or impose some additional tax on such profits for the corporate privilege of withholding them from individuals.

5. Exemption securities

A) Eliminate the exemption with respect to future issues of State and local obligations.

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TREASURY DEPARTMENT

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INTER OFFICE COMMUNICATION

DATE October 30, 1941

TO Secretary Morgenthau
FROM Mr. Bernard

In accordance with your request of yesterday, I state below my principal arguments for compulsory saving under present conditions. I conceive a proper program to be one withdrawing in the form of such savings not less than \$2 billion per annum, or about 10% of tax revenues and 20% of deficits.

1. This is a means of giving millions of people a direct definite individual financial property stake in the United States of America. It is important to secure a common interest among all classes which they clearly recognize as identical in character. Though it may never be so expressed, such a definite common interest is fundamental in social organization, cohesion and morale. The country may need it badly, if it does not already.

2. Millions of men and many more millions of their women will be given a sense of security against depression and post-war difficulties available to them in no other way. This also is important for real national morale. Most such people under the pressure of the cost of living, ambitions of one kind or another, lack of unity of opinion within families, or lack of prudence and financial self restraint, will not be able voluntarily to save, and will be grateful in the end to have had compulsion to assist them. It is helpful to most people to have virtue and necessity combined.

3. Substantial direct taxes, except under high emotional patriotism, are an injury to the self-respect of most people. The relation between taxes paid and benefits received is so indefinite that we usually feel that we are not paying for something we get, but for something someone else gets. Compulsory saving clearly mitigates this feeling, perhaps less at the time of imposition or withholding than afterwards. We shall need to impose heavy tax burdens at best. It is well to combine sheer financial sacrifice with some specific benefits in financial rights.

4. The protection of free enterprise and anything like our present social order depends upon the possession of purchasing power and property among small people. Compulsory savings - not available under ordinary conditions - is now logically available to accomplish this. To do it is in accordance with the philosophy of the Administration, as I understand it.

5. The possibility of paying out large sums - \$6, \$8 or \$10 or more billions - to millions of people of limited means under post-defense conditions, will be of great importance. For the payments will be freely available without sense of benefaction or subsidy. I believe they will be far more effective in the hands of individuals as property which they have earned in their own right than the same sums by any other method. Moreover, the sums under this plan must be made available without cavil by any class equally with obligations owed to others. This is exceedingly important in view of the possibility of stringency in

financing and excessive debt after defense. No one could attack distribution in this form without attacking all obligations, public or private. It is fairly certain that distribution of similar sums at that time would be "logically" difficult by any other means.

6. It is now and later may be even more necessary to withdraw income from the lower income classes in order to control excessive demand for consumption that cannot be provided for, i.e., to prevent serious inflation. To do this by straight taxes on the low income groups will be offensive to most people in nearly all classes. I know that most of the demand of higher income classes for direct taxes on the lower income classes is not due to the desire to depress the latter economically, but rather it is due to the belief that the absence of a sense of financial responsibility for the government among the lower income groups breeds impossible long run economic problems to the disadvantages of the whole country.

7. Unless the lower income groups are given the benefit of compulsory savings as a substitute for taxes, it would appear unlikely that any progressive tax scheme would seem to them adequately fair, and they will not easily be able to appreciate the damage to their own interests that excessive limitation of incentives on a national scale may cause.

I should now like to answer some of the financial objections to compulsory savings by the following remarks:

a. In a tax bill of over \$20 billions, the substitution in

the magnitude suggested of savings for taxes is a matter of 10%. It involves a capital cost assuming that the same amount could be secured by taxes, of \$2 billion or only 6% of the Federal expenditure (at the rate of \$30 billion), and about 2% of the national income; and an interest cost of about \$50 million. These seem small to me for the benefits.

b. If the deficit to be financed by bonds should be \$10 billion per year, the increase in debt would in 10 years be \$100 billion, of which some \$20 billion would be compulsory savings obligations (not including interest) or 20%. This seems to me not an excessive proportion of debt of the compulsory savings kind.

c. In the event of excessive debt burden at the end of defense requiring either an anti-deflationary inflation or repudiation of interest charges as against maintenance of excessive taxes, the treatment of the debt would be a common problem of all income classes, if there is a substantial proportion of compulsory saving debt. This seems of first rate potential importance. Such a balancing of interests and of burdens could not, I think, be secured in any other way.

OMB.

October 30, 1941

MEMORANDUM FOR THE SECRETARY

Subject: Distribution of consumption expenditures
by income classes

It is estimated that all families in the United States spent about \$41 billion on consumption items in 1935-36. 1/ As the attached tables indicate, families with an annual income less than \$1,000 accounted for about \$8½ billion, or 21 percent, of total expenditures; families with an income between \$1,000 and \$2,000 for almost \$15 billion, or 36.5 percent, and families with an income over \$2,000, for \$17½ billion, or 42½ percent.

The inflationary pressure on prices is likely to be greatest on durable and semidurable goods, and least on food. Families with an income below \$1,000 account for only 12½ percent of all expenditures on durable goods and 16½ percent of all expenditures on semidurable goods but for 26½ percent of all expenditures on food. Families with an income between \$1,000 and \$2,000, on the other hand, account for about 34 percent of all expenditures on durable and semidurable goods.

Even these figures understate the importance of this middle income group. The figures are for 1935-36, and the increase in the national income and in prices since then has brought many more families into this income group. Moreover, the income figures include income in the form of the services of owned homes, home-produced food, and the like, whereas taxes are assessed almost exclusively on the basis of money income.

1/ This estimate and those that follow are based on data published by the National Resources Planning Board. These data were obtained from a nation-wide study of consumer expenditures made in 1935 and 1936.

To control inflation, it is necessary to withdraw purchasing power that would otherwise be spent on consumer goods and services. To accomplish this by taxation, it is essential that the taxes go far enough down the income scale to reach the families and individuals who account for a substantial part of total expenditures on consumption. The higher the exemption, the more severely must the consumption of the groups taxed be restricted in order to balance increased spending by those not subject to the tax.

The present exemptions exclude from the income tax most families with incomes less than \$2,000. Under these exemptions, about 13,000,000 persons will pay an income tax out of a total of almost 50,000,000 persons receiving an income. These exemptions, therefore, subject only about one quarter of all income receivers to the income tax. In 1935-1936, the quarter of American families who had the highest incomes accounted for less than half of total expenditures on all consumption items and for 56½ percent of the aggregate income of all families. Moreover, the income tax does not affect all these expenditures since personal exemptions and credits for dependents exclude part of the income from taxation.

Even if the exemptions were lowered to \$1,000 for a married person, \$500 for a single person, and \$300 for each dependent, a large part of the families with incomes between \$1,000 and \$2,000 would not be subject to the income tax. Under these exemptions, a tax would be paid by about 20,000,000 persons, or 40 percent of all income receivers. In 1935-36, the 40 percent of American families who had the highest incomes accounted for almost two-thirds of total expenditures on all consumption items and for more than 70 percent of aggregate income.

The study made by Dr. Parran and referred to by you was not available in preparing this memorandum.

Attachments

Milton Friedman

Aggregate expenditures of families for durable, semidurable, and perishable goods, for services and housing, 1935-1936

Income level	Aggregate expenditures (in millions) for --					
	All consumption items	Durable goods	Semi-durable goods	Perishable goods	Services	Housing
Under \$1,000	\$ 8,543	\$ 452	\$ 648	\$ 4,952	\$ 945	\$ 1,546
\$1,000 - 2,000	14,884	1,222	1,316	7,555	2,145	2,646
2,000 - 3,000	7,876	807	797	3,510	1,371	1,391
3,000 - 5,000	4,545	490	503	1,838	910	804
5,000 and over	4,995	630	646	1,525	1,294	900
All levels	40,843	3,601	3,910	19,380	6,665	7,287

Percentage distribution by type of expenditure

Under \$1,000	100.0%	5.3	7.6	58.0	11.1	18.1
\$1,000 - 2,000	100.0	8.2	8.8	50.8	14.4	17.8
2,000 - 3,000	100.0	10.2	10.1	44.6	17.4	17.7
3,000 - 5,000	100.0	10.8	11.1	40.4	20.0	17.7
5,000 and over	100.0	12.6	12.9	30.5	25.9	18.0
All levels	100.0	8.8	9.6	47.4	16.3	17.8

Percentage distribution by income level

Under \$1,000	20.9%	12.6	16.6	25.5	14.2	21.2
\$1,000 - 2,000	36.4	33.9	33.6	39.0	32.2	36.2
2,000 - 3,000	19.3	22.4	20.4	18.1	20.6	19.1
3,000 - 5,000	11.1	13.6	12.9	9.5	13.6	11.1
5,000 and over	12.3	17.5	16.5	7.9	19.4	12.4
All levels	100.0	100.0	100.0	100.0	100.0	100.0

Treasury Department, Division of Tax Research

Source: Family Expenditures in the United States, p. 34.

Aggregate expenditures of families, for main categories of consumption,
1935-1936

Income levels	Aggregate expenditures (in millions) for --					
	Aggregate income (in millions)	All consumption items	Food	Housing	Clothing	All other
Under \$1,000	\$ 7,424	\$ 8,543	\$ 3,654	\$1,546	\$ 691	\$ 2,652
\$1,000 - 2,000	15,503	14,884	5,371	2,646	1,394	5,473
2,000 - 3,000	9,043	7,876	2,429	1,391	844	3,212
3,000 - 5,000	5,780	4,545	1,254	804	537	1,950
5,000 and over	9,930	4,995	1,005	900	671	2,419
All levels	47,680	40,843	13,713	7,287	4,137	15,706
	Aggregate ex- penditures as % of aggregate income	Percentage distribution of expenditures by type of expenditure				
Under \$1,000	115.1%	100.0%	42.8%	18.1%	8.1%	31.0%
\$1,000 - 2,000	96.0	100.0	36.1	17.8	9.4	36.7
2,000 - 3,000	87.1	100.0	30.8	17.7	10.7	40.8
3,000 - 5,000	78.6	100.0	27.6	17.7	11.8	42.9
5,000 and over	50.3	100.0	20.1	18.0	13.4	48.5
All levels	85.7	100.0	33.6	17.8	10.1	38.5
	Percentage distribution of expenditures by income level					
Under \$1,000		20.9%	26.6%	21.2%	16.7%	16.8%
\$1,000 - 2,000		36.4	39.2	36.2	33.7	34.6
2,000 - 3,000		19.3	17.7	19.1	20.4	20.4
3,000 - 5,000		11.1	9.1	11.1	13.0	12.5
5,000 and over		12.3	7.4	12.4	16.2	15.6
All levels		100.0	100.0	100.0	100.0	100.0

Treasury Department, Division of Tax Research

Source: Consumer Expenditures in the United States, p. 86; Family Expenditures in the United States, p. 25.

TREASURY DEPARTMENT

189

INTER OFFICE COMMUNICATION

DATE October 30, 1941

TO Secretary Morgenthau

FROM Mr. Barnard

Herewith a statement which you requested regarding the need for additional taxes from the inflation standpoint. It is in the form of a press statement but we all wish to emphasize that it is not yet written in proper form for public use and that the statement in the first paragraph on page 3 particularly, in our opinion, should not be made public.

JLS
RNB

Secretary Morgenthau today made public a Treasury estimate showing that about \$6½ billion in increased taxes must be withdrawn currently from consumers' incomes if price rises are to be kept in check in the coming year.

This figure represents the goal which, the Treasury believes, must be achieved by new tax legislation in order to offset the inflationary effects of the defense program. The following estimates show how the figure of \$6½ billions was obtained.

I

By June, 1942, the Federal Government will be spending on defense about \$15½ billion per year more than in June, 1941. About \$6 billion of this increase will be drained off by higher tax receipts, approximately half of the increase coming from the larger flow of the national income and the other half from the higher rates enacted in the Revenue Act of 1941.

Another \$3 billion, at most, of the increased defense expenditure may be counteracted by a reduction in consumer spending on consumption goods and services and by a reduction of business spending on private capital goods. Such reductions will be caused by defense savings bond purchases, by

priorities, by the unavailability of goods and by a number of other restrictive factors.

Finally, \$1 billion is likely to be absorbed by an increase in corporate reserves, and will never get into the hands of consumers.

The total offset to the increased Government spending is, therefore, about \$10 billion, leaving \$5½ billion of purchasing power that will be pushing prices upward.

II

This purchasing power cannot be matched by an increased flow of goods for civilian use. Defense needs will, as stated above, require about \$15½ billion more by next June than last June. Yet by June, 1942, the total real output of goods and services for civilians will probably be no more than \$10½ billion per year higher than in June, 1941. Hence, civilian output must be cut down by about \$5 billion in the same period if defense requirements are to be met.

As noted above, \$3 billion of this reduction may come about through factors other than taxes, such as voluntary savings, priorities and shortages. The rest of the reduction, amounting to about \$2 billion, must be achieved by increased taxation.

III

To absorb the excess purchasing power of $\$5\frac{1}{2}$ billion and also to reduce private spending by an additional $\$2$ billion, a total of $\$7\frac{1}{2}$ billion, will require about $\$6\frac{1}{2}$ billion in increased taxes withdrawn currently from the incomes of consumers. The apparent discrepancy of $\$1$ billion here is caused by the fact that taxes drain off more purchasing power than the exact amount of the tax receipts.

If private spending declines by less than $\$3$ billion as a result of voluntary savings, priorities and the like, even more than $\$6\frac{1}{2}$ billion in new taxes will be needed. In this case the total amount of taxes needed to prevent a substantial rise in prices may be as high as $\$9$ billion.

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TREASURY DEPARTMENT

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INTER OFFICE COMMUNICATION

DATE October 29, 1941

TO Secretary Morgenthau
FROM Mr. White

You asked me to leave with you my comments on the Barnard proposal before I left.

I have just spoken to Mr. Barnard and find that as a result of the week's discussion we are very close together in our recommendations. The plan which I, along with others, am in favor of will have been submitted to you. The only difference, I believe, between Mr. Barnard's position and my own is that he would prefer the lower exemptions on the 15 percent withholding tax and I favor the higher (i.e., the present) exemptions.

I am not sure that Mr. Barnard would agree with all the recommendations in Part 3 of the tax program outlined in the memorandum referred to above but I believe he favors most of them. He will doubtless indicate where if at all he disagrees.

TO:

Copies to:

Mr. Randolph Paul
Dr. Harold Groves
Mr. Dave Morris
Dr. Harry White
Mr. Charles Kades
Mr. John Sullivan
Miss Chauncey

MR. FOLEY

From Mr. Foley .

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October 29, 1941

MEMORANDUM FOR MR. BARNARD:

The appended plan is submitted for the Secretary's consideration. It has the endorsement of Messrs. Paul, Groves, Foley, Morris, White, and Kades.

In order to show that the Treasury is contemplating a balanced program not unduly burdensome to the low income groups, we are strongly of the opinion that the separate parts of the plan should be presented to Congress at the same time, with the recommendation that Part I be taken up immediately.

Mr. Groves makes the important reservation that the exemption in Part I A (2) should be lower and that the rate of 15 percent should be reduced to 12-1/2 percent.

Attachment

TREASURY TAX AND ANTI-INFLATION PLAN

Part I - to become effective January 1, 1942.

- A. A 15% withholding tax upon all individuals measured by
1. income from all sources (e.g., wages, salaries, dividends, interest, rents, royalties, etc.)
 2. after personal exemptions now provided for income tax under Revenue Act of 1941 (i.e., single person, \$750; married person, \$1,500, each dependent, \$400),
 3. with provision for repayment in part after emergency to those in lowest brackets.
- B. Net increase in revenue under this part of program estimated to be \$2,700,000,000.00

Part II - to become effective January 1, 1942.

- A. A 3% increase in payroll taxes for extended unemployment insurance and old-age assistance portions of program of Social Security Board as follows:

Type	Employer		Employee	
	Now	After	Now	After
<u>Unemployment Insurance</u>	3	3	0	1
<u>Old-age assistance</u>	1	2	1	2
	4	5	1	3

- B. Net increase in revenue under this part of program estimated to be \$1,900,000,000.00 (consisting of \$700,000,000 from unemployment part and \$1,200,000,000 from old-age part; gross tax increase being \$1,600,000,000 from unemployment part and \$2,000,000,000 from old-age part; difference made up through increased benefits paid out).

Part III - to become effective with Revenue Act of 1942
but to be submitted simultaneously with Part I.

- A. Excess Profits Taxation (Morris-Paul-McKeough Plan of averaging alternative taxes; i.e., adding the tax under invested capital method to the tax under average earnings method and dividing by 2).
- B. Manufacturers' Excise Taxes (imposed or increased to discourage purchase of goods competitive with defense articles).
- C. Estate and gift tax revision in rates and exemptions, along lines of Treasury 1941 proposal, and an additional revision to prevent avoidance by life insurance and powers of appointment.
- D. Elimination of tax-exemption of holders of future state and municipal securities on interest derived from this source.
- E. Elimination of discrimination in favor of community property states.
- F. Reduction in depletion deduction.
- G. Revision of capital gains tax provision.
- H. Taxation of life insurance industry (\$30,000,000,000 in assets and \$8,000,000,000 in tax-exempt income).
- I. Elimination of tax exemption of dividends on stock issued by Federal Reserve Banks, Savings and Loan Associations, Farm Loan Banks, etc.
- J. Equalization of the status of dividends and corporate interest for deduction purposes.
- K. Miscellaneous corrections of the statute to prevent avoidance and promote equitable incidence.

October 31, 1941.

MEMORANDUM FOR THE FILES.

While I was in the Secretary's office at a conference on taxation this morning shortly after nine o'clock the Secretary had a telephone call from Secretary Knox. At the conclusion of the conversation he told me in the presence of the others that he had just agreed with Secretary Knox that we would immediately transfer a part of the Coast Guard to the Navy along the lines of the understanding we had worked out last April. This proposal, which had the President's approval, was for the transfer of the seagoing equipment, including all the heavier cutters and twenty 125-foot cutters, and for the retention by the Treasury Department of the ice breakers, shore stations, lighthouse service and smaller floating equipment.

The Secretary asked me to work it out immediately so that an agreement could be effected before noon. I immediately came to my office and called Admiral Wessche, telling him what had been agreed upon, and he said he would get to work with Harrison, who was with him at the time, to work out the transfer. He said that in view of Executive Order 5895 of September 11, 1941, all that would be necessary would be a memorandum to be signed by Stark and himself and approved by the Secretary of the Treasury. I also called Cairns and he agreed that this would be sufficient. He said he was leaving on the ten o'clock train but would have Feidler look the agreement over to see that it was in proper form as soon as Wessche brought it over, which I had instructed Wessche to do. A few minutes later Wessche called me back and said that Admiral Ingersoll, Assistant Chief, Naval Operations, had just called him and told him that he (Ingersoll) had instructions from Forrestal that arrangements were to be made immediately for the transfer of the entire Coast Guard to the Navy. I told the Admiral that this was not in accordance with Secretary Morgenthau's understanding with Secretary Knox and that I would speak to the Secretary about it immediately. I went into the Secretary's office, where the tax meeting was still continuing, and told the Secretary of this development. He called Knox and, with the loud speaker being on, I could hear the conversation. Knox said his understanding was that they did not want the shore stations and equipment and that even in case of war these would be transferred back to the Treasury Department. But he said that Stark was with him in his office and he would let Stark explain just what was passed. Stark came on the

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phone and explained that what he wanted was the immediate transfer of the entire Coast Guard. He added that it would not do to leave everything to the last moment and he thought that all possible preparations ought to be made in advance of whatever might happen and he considered it necessary to have the transfer made now. Secretary Morgenthau said in reply that he would be the last man to give him (Stark) any argument when it came to the question of what was necessary for defense and that if what he wanted now was the immediate transfer of the Coast Guard to the Navy he (Secretary Morgenthau) would agree, but that this differed from his previous understanding with Secretary Knox. Stark repeated that this was what he wanted, and the Secretary said it would be done. When they hung up, I remarked that Stark had not been entirely frank with Knox and that as a matter of law it would not be possible for the Navy to retransfer shore stations and the lighthouse service back to the Treasury Department in time of war. The Secretary replied that to say that Stark had not been entirely frank was putting it mildly, but at any rate for me to go ahead and see that the transfer was accomplished.

I came back to my office and told Waesche of the new arrangement. He said that Bailey, of the Budget, had called him up and that Bailey was confused as to just what was desired. Bailey also said that if there was to be an executive order, he thought it ought to be prepared in Coast Guard. Waesche said that in view of the new development he would have Harrison prepare an executive order making the transfer and would call Bailey back. I told him that I would take care of calling Bailey and that he could go ahead with the executive order. I called Bailey and told him exactly what had occurred and that we would deliver an executive order to him before noon. I then called Mr. Feidler and told him to take a look at the executive order to see that it was in proper form and that I thought there ought to be with it a letter to the President, through the Budget, to be signed by the Secretary of the Treasury noting his approval of the transfer. Feidler agreed and said that he would see that such a letter was prepared and that he would look over the order to see that it was in form.

Harrison and Gorman came over to Feidler's office a little later with a copy of the suggested executive order drafted by Navy. In their opinion it was not in proper form and they redrafted it, together with a letter to the President for the Secretary's signature. These were delivered to the Secretary's office at 12:15 and after his signature to the Bureau of the Budget at 1:00 P.M. The executive order requires processing also by the Attorney General and the Division of Federal Register which will probably delay the signature until early next week.

OCT 31 1941

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Through the Bureau of the Budget.
Through the Attorney General.
Through the Division of the
Federal Register.

My dear Mr. President:

In accordance with an oral understanding between Secretary of the Navy Knox and myself, there is respectfully transmitted herewith for your signature, if you approve, a proposed Executive Order directing that the United States Coast Guard shall, until further orders from you, operate as a part of the Navy, subject to the orders of the Secretary of the Navy.

Faithfully yours,

(Signed) H. Morgenthau, Jr.

Secretary of the Treasury.

The President,

The White House.

EXECUTIVE ORDER

PROVIDING FOR THE OPERATION OF THE
COAST GUARD AS A PART OF THE NAVY

Pursuant to the authority vested in me by Section 1 of the Act of Congress approved January 28, 1916, 38 Stat. 800, (U.S.C. title 14, sec. 1), as amended by sections 5 and 6 of the Act of July 11, 1941 (Public Law 166, 77th Congress, 1st Session), it is hereby directed that the Coast Guard shall from this date, until further orders, operate as a part of the Navy, subject to the orders of the Secretary of the Navy.

All Coast Guard personnel operating as a part of the Navy, subject to the orders of the Secretary of the Navy, pursuant to this order, shall, while so serving, be subject to the laws enacted for the government of the Navy: Provided, That in the initiation, prosecution, and completion of disciplinary action, including remission or mitigation of punishments for any offense committed by any officer or enlisted man of the Coast Guard, the jurisdiction shall depend upon and be in accordance with the laws and regulations of the Department having jurisdiction of the person of such offender at the various stages

of such action: Provided further, That any punishment imposed and executed in accordance with the provisions of this paragraph shall not exceed that to which the offender was liable at the time of the commission of the offense.

THE WHITE HOUSE,

1941

TREASURY DEPARTMENT

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INTER OFFICE COMMUNICATION

DATE October 31, 1941

TO: Secretary Morgenthau

FROM: Dave H. Morris, Jr.

Subject: Problem of Base of Excess Profits Taxes.

Without unduly trying to boost the "joint base average", I think it is fair to report that Mr. Randolph Paul, entirely independent of any work I have done on the subject, seems to have reached the conclusion that this type of plan has much to commend it. In fact, during my absence in New York at the Federal Reserve Bank at the end of last week, he suggested it to the "Barnard" group on an entirely independent basis. As a result of this, the attached memorandum has, within the last day or two, been generally circulated to the group now working with Mr. Barnard.

While no over-all figures are (to my knowledge) available, nevertheless it is interesting to note that with respect to the fourteen companies chosen as illustrations, the total amount of excess profits available for taxation under the different methods proposed is as follows:

<u>Base</u>	<u>Thousands of Dollars</u>
1. Six percent on invested capital	147,802
2. Proposed joint base average (i.e., average of (a) six percent allowance on invested capital and (b) average earnings credit -- both adjusted under the 1940 law).	141,837
3. Proposed joint base average, but with excess profits limited to a minimum of four percent on invested capital on the one hand and a maximum of twelve percent on the other hand.	152,347

It is also to be noted that the "technicians" say a better average is to take an average of the taxes under the two methods. If this proves to be correct, I would certainly approve it.

Some Thoughts* - for Testing Purposes - with Respect to Proprieties and Practical Results, of Various Excess Profits Taxes and Limitations under War (or Emergency) Conditions

Not many people will deny the basic injustice of requiring one man to risk his life in the army at a dollar a day while letting his neighbor stay at home in comparative safety and comfort and earn from five to fifteen dollars a day. Yet so far no one has found a real answer to this problem, and probably it will remain one of the basic paradoxes of life.

While not directly comparable, it seems there is fundamentally a good deal of an analogy in the problem of a ceiling on profits. Even England has had to modify her 100-percent tax on "excess profits" and now gives a 20-percent credit, repayable at the end of the war. Hence, in spite of the "pure justice" of a 100-percent tax on excess profits in war, we seem to have another paradox, and if we try to do "pure justice" it will look, from all available experience, as if we might do rather severe practical harm to our business system without reaping proportionate benefits.

* The thoughts set forth in this memorandum are given in as simple a form as possible and only attempt to reach those aspects of the subject which seem most basic. As in any such discussion, there is over simplification, and it is realized that any final plan would have to provide for many ramifications, such as "new" corporations; or those, such as railroads, whose rates, etc. have been and are subject to strict governmental regulations. In spite of these limitations, it is believed best in this particular memorandum to over simplify, but this qualification must be kept in mind when considering the subject matter herein.

Another problem, regardless of whether a 100-percent rate or a graded scale of rates is set on excess profits, is that of determining a fair base for normal profits. It seems pretty well agreed that the two major ones are those generally described as "invested capital" on the one hand, and on the other, as "average earnings" or "idea results." This last name is not often used, but probably, in a basic way, is a more accurate description of the second group.

In a capitalistic society it seems that sometimes substantial aggregations of capital with only mediocre management get along in a fair to medium way. At the same time, some rather small capital investments with particularly good management do surprisingly well. Under these conditions it may be asked, on the one hand, why should a corporation with a big capital but a mediocre management, who in a base period could only earn 3 percent, be allowed 6 percent just because of war (or emergency) conditions? And on the other hand, it would seem just, that under war (or emergency) conditions an "idea corporation" should not be allowed 20, 30, 40 percent on its invested capital.

Therefore, as a means both to approach "basic justice" as nearly as possible, by treating the two major components equally, and also as a reasonable means of raising substantial amounts in taxes, it is suggested that a plain arithmetic average of the two bases be used. Under this proposal there would be no options. If such a system were adopted, it is believed that its equal treatment of both major components would appeal to most Americans, both in and out of business.

As respects to the tax raising aspects of this proposal, no extensive studies are known to the writer. However, in June 1941 some preliminary work was done by the Division of Tax Research on fourteen companies, selected as illustrative, of which half were the "invested capital" type, and half the "idea" type. Based on the data presented in this study some figures have been compiled which compare the results of this proposal with that on the basis of 6 percent on invested capital and the 1941 Income Tax Law. These figures are presented in Appendix A, annexed hereto.

In summarizing the totals, it must not be forgotten that there are great variations between individual companies and under any scheme it is inevitable that there are some cases of severe hardship and some cases of inequitable escape from justifiable taxes. However, even with these difficulties, it is believed that some reasonable evaluation can be made of the various schemes if the following major factors are kept in mind:

- (1) Tax raising ability without "killing the goose that lays the golden egg";
- (2) Substantial fairness to both the Treasury and the taxpayer in a vast number of cases;
- (3) The greatest general acceptance by the public of the proposal possible under emergency conditions.

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Although this memorandum was started with the objective of sticking solely to the main issues, nevertheless there are two collateral problems which seem to require at least some mention. Both appear to have a mixed flavor of the paradoxical and the practical.

The first such problem is that of a 100-percent tax on earnings over the base, whatever that may be decided to be. Here we suggest a modification along the lines of the British system.

The second collateral problem is that under any system there is always the problem of extreme cases, such as on the one hand, Coca Cola, and on the other, American Woolen. Under any system probably the nicest way, from a theoretical point of view, to handle such cases would be to insert special provisions in the tax law which would cover these types of problems. However, from a practical point of view this is probably very difficult and if the scheme suggested in this memorandum were adopted it might be better to handle such extremes through the simple medium of placing certain general limits on credits. For instance, it could be provided that regardless of the joint base formula no company would be allowed to earn over 12 percent on its capital, nor would it be penalized by an average earnings credit of 4 percent on its capital.

D.H.M.
10/22/41

(In thousands of dollars)

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	Coors-Cola	Coit's Patent Streams	Carlisle Wright	Chrysler	Goodyear	General Alloys	Indiana Steel Products	Continental Can	International Paper & Power	U.S. Steel	American Cop & Foundry	American Smelting	Stoke New- ington	Leaver Co.	Total
Invested in 1940	88,953	1,039	46,184	18,785	736,628	175,3	582,6	101,580	164,605	1,589,396	66,612	66,594	727.1	732.8	3,574,376
By 1940	43,676	1,107	45,079	18,406	632,529	66.8	100.7	10,236	83,184	136,630	6,579	3,928	147.6	87.0	471,000
Under 10% of 1940	12,250	975	4,055	17,056	25,858	19.4	22.9	3,257	4,445	30,600	179	1,227	35.8	24.1	109,737
10-20% of 1940	4,125	221	4,883	9,708	26,264	3.1	13.3	1,725	7,264	11,063	1,390	1,227	31.4	6.4	117,305
20-30% of 1940	16,545	1,066	24,115	26,736	50,300	22.7	43.0	4,020	12,377	59,663	2,149	1,227	67.2	32.5	223,335
30-40% of 1940	13,600	582	13,377	20,020	31,884	20.7	35.3	3,733	7,487	44,307	2,039	1,227	95.8	37.0	146,000
40-50% of 1940	30,274	2,185	11,036	14,214	77,086	44.1	74.4	6,963	10,077	107,263	4,540	2,731	101.8	60.0	325,400
50-60% of 1940	3,337	242	2,771	11,567	40,440	10.2	15.0	1,475	11,074	30,364	5,117	3,023	43.6	14.0	144,700
60-70% of 1940	31,187	1,829	5,621	11,011	42,382	44.9	25.0	7,364	4,083	42,227	312	719	36.2	30.3	147,000
70-80% of 1940	16,700	1,131	4,133	16,008	44,198	13.7	33.0	7,030	7,561	71,776	2,913	2,356	34.9	47.8	144,000
80-90% of 1940	16,674	1,131	4,133	16,008	44,198	13.7	33.0	7,030	7,561	71,776	2,913	2,356	34.9	47.8	144,000
90-100% of 1940	79,137	1,093	26,187	13,369	70,728	23.6	41.4	1,548	5,400	15,774	-	-	24.7	16.0	147,000
100% of 1940	17,018	1,064	6,908	11,147	33,497	16.4	27.4	1,413	9,173	37,111	1,005	323	32.2	12.8	141,600
Total	17,500	1,094	6,908	11,147	33,497	16.4	27.4	1,413	9,173	37,111	388	69	32.2	12.8	152,340
100% of 1940	36,439	2,027	4,825	11,677	75,110	44.2	75.7	6,041	13,013	44,078	2,039	1,227	116.5	43.0	299,010
100% of 1940	15,414	2,036	4,827	11,677	46,331	13.1	11.7	3,260	15,397	37,840	3,664	1,650	101.0	35.8	233,240
100% of 1940	33,300	2,036	4,827	11,677	46,331	13.1	11.7	3,260	15,397	37,840	3,664	1,650	101.0	35.8	294,510

October 23, 1941

Regraded Unclassified

October 31, 1941.

Secretary Morgenthau

Dave H. Morris, Jr.

Subject: Problem of Base of Excess Profits Taxes.

Without unduly trying to boost the "joint base average", I think it is fair to report that Mr. Randolph Paul, entirely independent of any work I have done on the subject, seems to have reached the conclusion that this type of plan has much to commend it. In fact, during my absence in New York at the Federal Reserve Bank at the end of last week, he suggested it to the "Barnard" group on an entirely independent basis. As a result of this, the attached memorandum has, within the last day or two, been generally circulated to the group now working with Mr. Barnard.

While no over-all figures are (to my knowledge) available, nevertheless it is interesting to note that with respect to the fourteen companies chosen as illustrations, the total amount of excess profits available for taxation under the different methods proposed is as follows:

<u>Base</u>	<u>Thousands of Dollars</u>
1. Six percent on invested capital	147,802
2. Proposed joint base average (i.e., average of (a) six percent allowance on invested capital and (b) average earnings credit -- both adjusted under the 1940 law).	141,837
3. Proposed joint base average, but with excess profits limited to a minimum of four percent on invested capital on the one hand and a maximum of twelve percent on the other hand.	152,347

It is also to be noted that the "technicians" say a better average is to take an average of the taxes under the two methods. If this proves to be correct, I would certainly approve it.

D.H.M.

**Some Thoughts* - for Testing Purposes - with Respect to Proprietary and
Practical Results, of Various Excess Profits Taxes and Limitations under
War (or Emergency) Conditions**

Not many people will deny the basic injustice of requiring one man to risk his life in the army at a dollar a day while letting his neighbor stay at home in comparative safety and comfort and earn from five to fifteen dollars a day. Yet so far no one has found a real answer to this problem, and probably it will remain one of the basic paradoxes of life.

While not directly comparable, it seems there is fundamentally a good deal of an analogy in the problem of a ceiling on profits. Even England has had to modify her 100-percent tax on "excess profits" and now gives a 20-percent credit, repayable at the end of the war. Hence, in spite of the "pure justice" of a 100-percent tax on excess profits in war, we seem to have another paradox, and if we try to do "pure justice" it will look, from all available experience, as if we might do rather severe practical harm to our business system without reaping proportionate benefits.

* The thoughts set forth in this memorandum are given in as simple a form as possible and only attempt to reach those aspects of the subject which seem most basic. As in any such discussion, there is over simplification, and it is realized that any final plan would have to provide for many ramifications, such as "new" corporations; or those, such as railroads, whose rates, etc. have been and are subject to strict governmental regulations. In spite of these limitations, it is believed best in this particular memorandum to over simplify, but this qualification must be kept in mind when considering the subject matter herein.

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Another problem, regardless of whether a 100-percent rate or a graded scale of rates is set on excess profits, is that of determining a fair base for normal profits. It seems pretty well agreed that the two major ones are those generally described as "invested capital" on the one hand, and on the other, as "average earnings" or "idea results." This last name is not often used, but probably, in a basic way, is a more accurate description of the second group.

In a capitalistic society it seems that sometimes substantial aggregations of capital with only mediocre management get along in a fair to medium way. At the same time, some rather small capital investments with particularly good management do surprisingly well. Under these conditions it may be asked, on the one hand, why should a corporation with a big capital but a mediocre management, who in a base period could only earn 5 percent, be allowed 8 percent just because of war (or emergency) conditions? And on the other hand, it would seem just, that under war (or emergency) conditions an "idea corporation" should not be allowed 20, 30, 40 percent on its invested capital.

Therefore, as a means both to approach "basic justice" as nearly as possible, by treating the two major components equally, and also as a reasonable means of raising substantial amounts in taxes, it is suggested that a plain arithmetic average of the two bases be used. Under this proposal there would be no options. If such a system were adopted, it is believed that its equal treatment of both major components would appeal to most Americans, both in and out of business.

With respect to the tax raising aspects of this proposal, no exhaustive studies are known to the writer. However, in June 1941 some interesting work was done by the Division of Tax Research on fourteen companies, selected as illustrative, of which half were the "invested capital" type, and half the "idea" type. Based on the data presented in that study some figures have been compiled which compare the results under this proposal with that on the basis of 6 percent on invested capital and the 1941 Income Tax Law. These figures are presented in Schedule A, annexed hereto.

In comparing the totals, it must not be forgotten that there are great variations between individual companies and under any scheme it is inevitable that there are some cases of severe hardship and some cases of flagrant escape from justifiable taxes. However, even with these difficulties, it is believed that some reasonable evaluation can be made of the various schemes if the following major factors are kept in mind:

- (1) Tax raising ability without "killing the goose that lays the golden egg";
- (2) Substantial fairness to both the Treasury and the taxpayer in the greatest number of cases;
- (3) The greatest general acceptance by the public of the proposal as fair and reasonable under emergency conditions.

Although this memorandum was started with the objective of sticking closely to the main issues, nevertheless there are two collateral problems which seem to require at least some mention. Both appear to have a mixed flavor of the paradoxical and the practical.

The first such problem is that of a 100-percent tax on earnings over the base, whatever that may be decided to be. Here we suggest a modification along the lines of the British system.

The second collateral problem is that under any system there is always the problem of extreme cases, such as on the one hand, Coca Cola, and on the other, American Woolen. Under any system probably the nicest way, from a theoretical point of view, to handle such cases would be to insert special provisions in the tax law which would cover these types of problems. However, from a practical point of view this is probably very difficult and if the scheme suggested in this memorandum were adopted it might be better to handle such extremes through the simple medium of placing certain general limits on credits. For instance, it could be provided that regardless of the joint base formula no company would be allowed to earn over 12 percent on its capital, nor would it be penalized by an average earnings credit below 4 percent on its capital.

B.H.H.
10/22/41

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Comparison of income and excess profits taxes for 14 selected companies under a 100-percent excess profits tax with a credit of 6 percent of invested capital and with an excess profits credit equal to an average of 6 percent of invested capital and the base period earnings credit under the 1960 Revenue Act

(in thousands of dollars)

Company	DuPont	Eastman Kodak	General Electric	General Motors	International Harvester	Johnson & Johnson	McGraw-Hill	Rockwell International	Union Pacific	Walt Disney	Western Union	Weyerhaeuser	Other	Total	
Invested Capital 1960	86,953	16,039	46,184	184,183	796,875	375-3	582.6	101,560	168,609	1,589,396	68,612	66,554	777-1	736.8	3,079,370.8
Net Income 1960	43,874	3,167	45,070	54,406	112,503	68.4	110.7	12,236	23,186	155,830	4,579	3,994	187-6	87.0	471,647.1
Income Tax on basis of 1961 law															
(a) "Base" Income Tax	12,460	675	4,254	17,080	23,438	19.4	29.9	3,257	4,405	30,600	1,300	1,287	35.8	26.1	109,737.8
(b) excess profits Tax	6,325	993	24,609	7,708	36,504	3-3	13-3	1,729	7,954	31,063	159	1,287	32.8	8.4	112,394.4
(c) Total	16,509	1,666	31,345	24,788	60,362	22.7	43.2	4,986	12,359	61,663	1,459	2,574	67.8	34.5	222,132.2
"Base" Income Tax as 111															
(1) + (2)	13,600	902	13,972	20,090	34,880	26.7	34.3	3,733	7,147	46,307	1,034	1,287	45.4	27.0	146,240.6
Excess Profits Credit															
(a) 6% on Invested Capital - 6% of (1)	5,337	964	2,772	11,327	48,410	22.5	35.0	4,073	11,078	25,364	5,337	3,793	43.4	44.0	146,799.1
(b) average earnings under 1960 Act	31,187	1,299	5,615	41,411	45,302	44.9	63.0	7,964	44,227	48,227	512	719	26.2	50.3	147,414.4
(c) Proposed "Joint Base Average" - 10% of (1) + 2	14,262	1,131	4,193	24,569	44,138	33.7	49.0	7,930	7,583	71,796	7,935	2,356	49.9	47.2	146,820.8
(d) after credit of 6% on Invested Capital with limits of 45 minimum and 125 maximum - 10% of (1)	10,674	1,131	4,193	22,654	44,138	33.7	49.0	7,930	7,583	71,796	3,554	2,060	45.9	47.2	135,622.4
Income Tax															
(a) after credit of 6% on Invested Capital (1) + (d)	24,937	1,293	24,307	33,389	35,435	23.6	41.4	2,394	6,406	15,774	-	-	34.7	16.0	147,842.7
(b) after credit on Proposed Joint Base Average - 10% limits (1) + (c)	12,032	1,099	26,305	18,147	33,447	32.4	37.4	1,413	9,170	37,933	1,028	423	55.2	12.8	141,836.8
(c) after credit of 6% on Invested Capital with limits of 45 minimum and 125 maximum - 10% of (1) + (d)	19,400	1,094	26,305	22,062	33,447	32.4	37.4	1,413	9,170	37,933	986	60	55.2	12.8	138,346.8
Total Tax															
(a) on 1961 basis (1) + (12)	34,539	2,205	42,899	53,479	79,133	44.3	75.7	6,141	13,413	64,074	7,028	1,287	110.5	43.0	294,012.5
(b) on Joint Base Average - 10% limits (1) + (13)	25,644	2,036	40,477	38,237	48,231	33.1	41.7	3,204	14,397	45,400	1,400	1,594	20.8	30.8	248,441.4
(c) on Joint Base Average - 10% limits - (1) + (14)	33,200	2,036	40,477	42,150	48,231	33.1	41.7	3,204	14,397	45,400	1,400	1,594	20.8	30.8	254,011.4

October 25, 1964

October 31, 1941

MEMORANDUM FOR THE SECRETARY

In accordance with your request, there are submitted herewith comparative data on taxes in the United States, Great Britain and Canada. Corresponding information for income and profits taxes was submitted in a memorandum of October 21, 1941.

1. Death and gift taxes

(a) Death taxes

In the United States, individuals are subject to one Federal estate tax. This tax comprises two sets of graduated rates and exemptions - the basic estate tax under the Revenue Act of 1926 and the additional estate tax under the Revenue Act of 1932 as amended. The total tax is the amount determined under the basic tax plus the difference between the basic and additional tax. In addition, all States except Nevada impose death taxes (estate, inheritance or both). A credit for State death taxes paid is allowed under the Federal estate tax to the extent of 80 percent of the tax under the basic Federal estate tax. In most cases, the State death taxes are set at levels which are at least 80 percent of the Federal basic tax.

In Great Britain, two death duties are imposed. The estate tax is based on the net value of the estate and is imposed by totality and not by bracket. ^{1/} The legacy and successions duty is based not on the shares of the estate received by each beneficiary, but rather on the basis of consanguinity to the decedent.

^{1/} The bracket rate scale breaks the estate or inheritance up into separate brackets, a greater percentage of tax applying to each successively higher bracket. The totality scale breaks the tax base into brackets, increasing the rate of tax on each successive bracket, the rate so determined being applicable to the entire tax base.

The Dominion of Canada imposes no estate tax, but does impose two taxes on beneficiaries, (1) an initial duty based upon the aggregate value of the estate and (2) an additional duty based upon the share of the estate received by each beneficiary and on the relationship of the beneficiary to the decedent. The total rate of tax payable by a beneficiary on his share in an estate is equal to the rate applicable to the aggregate value of the estate plus the rate applicable under the additional duty. In addition, death duties are imposed by all of the Provinces.

In the United States, there is a \$40,000 specific exemption plus an exclusion for insurance equal to an additional \$40,000. Under British law, all estates in excess of \$400 are taxable; in Canada, an exemption of \$25,000 is allowed under the initial duty. As shown in Table 1, the Federal estate tax is less on small estates than the British but higher on large estates. For example, on net estates of less than \$50,000, no Federal tax is imposed; in Great Britain, the effective rate of tax is 4 percent; on net estates of \$50,000, the Federal tax is one-sixth of the British; on net estates of \$100,000,000, the effective Federal rate of tax is 75.4 percent as against 65.0 percent in Great Britain. Comparison with Canada is not possible because the Canadian tax is imposed upon the beneficiaries and not upon the estate.

(b) Gift taxes

In the United States, a gift tax is imposed at three-fourths of the estate tax rates. In addition, 9 States impose gift taxes.

No gift tax is imposed in Great Britain. However, there is included in the value of the decedent's estate all gifts made within three years of the date of death, except gifts which in the case of any donee do not exceed \$400 in value.

In Canada, the gift tax ranges from 7 percent on taxable gifts in excess of \$4,000 but not in excess of \$5,000 to 25 percent on gifts of more than \$1,000,000. Gift taxes are not imposed by any of the Provinces.

2. General sales taxes

The United States Government does not impose a general sales tax. There is imposed, however, a number of excise taxes on selected commodities. 22 States impose general sales taxes. The most usual rate of tax is 2 percent.

The British impose a sales tax in the form of a "purchase tax." The tax is imposed on the purchase of certain specified goods from registered dealers (generally wholesalers) by unregistered dealers (generally retailers). The rates of tax are as follows:

(a) $33\frac{1}{3}$ percent on the wholesale value (or about 24 percent on the retail price) of certain luxuries such as furs, articles made with real silk, china, and porcelain articles, jewelry, toilet preparations (including cosmetics) and articles not normally requiring immediate replacement.

(b) $16\frac{2}{3}$ percent on the wholesale value (or about 12 percent on the retail price) of certain goods in common use such as clothing, boots and shoes (other than children's), pots, pans and kettles, domestic brooms and brushes, certain medicines and drugs, newspaper periodicals and books.

Food, water, gas, electricity, coal, petrol, tobacco and drinks, children's clothing and boots and shoes, farmers' machinery and equipment, and certain medicines are exempt from the purchase tax.

In Canada, an 8 percent manufacturers' sales tax is imposed. In general, the tax does not apply to staple necessities of life, nor to the implements used in the primary industries of farming, fishing, mining and lumbering. General retail sales taxes are imposed in the Provinces of Alberta, Quebec and Saskatchewan. The rate is 2 percent.

3. Selective excise taxes

The Federal Government and the States, the British National Government and the Dominion and provincial governments of Canada, all impose numerous excises on selected commodities. A comparison of some of the more important rates is shown in Table 2.

Table 1

Comparison of the amount of estate tax liability and effective rate of tax under present United States law (Revenue Act, 1941) and under British Finance (No. 2) Act of 1940, upon net estates (before exemption) of selected sizes

Net estate before exemption (000)	Amount of tax		Effective rate	
	United States: 1/	Great Britain: 2/	United States	Great Britain
\$ 25	-	\$ 1,000	-	4.0%
35	-	1,400	-	4.0
40	-	1,600	-	4.0
50	\$ 500	3,000	1.0%	6.0
60	1,600	4,320	2.7	7.2
80	4,800	7,680	6.0	9.6
100	9,500	10,800	9.5	10.8
200	38,700	33,600	19.4	16.8
400	100,900	98,800	25.2	24.7
600	166,700	171,600	27.8	28.6
800	236,900	249,600	29.6	31.2
1,000	310,900	338,000	31.1	33.8
2,000	735,200	832,000	36.8	41.6
4,000	1,814,600	1,976,000	45.4	49.4
6,000	3,111,400	3,276,000	51.9	54.6
10,000	6,057,800	6,500,000	60.6	65.0
20,000	13,751,400	13,000,000	68.8	65.0
40,000	29,151,400	26,000,000	72.9	65.0
60,000	44,557,400	39,000,000	74.3	65.0
100,000	75,357,400	65,000,000	75.4	65.0

Treasury Department, Division of Tax Research

- 1/ Computations are before allowance of credit for State death taxes which is assumed to be 80 percent of the tax imposed under the 1926 Act.
- 2/ Excludes legacy and succession duties applicable to personal property and real property, respectively. The rates of tax are graduated on the basis of consanguinity and not on the size of the share received by each beneficiary. Under present law the rates, after certain exemptions, in the case of both of these taxes, are as follows:
- On shares passing to husband or wife, child or lineal descendant of child, father or mother or any lineal ancestor 14
 - On shares passing to brother or sister, lineal descendant of brother or sister 5
 - On shares passing to any other person, including any related only by natural ties 10
- In certain cases supplementary rates to a maximum of 14 percent are chargeable excepting as between spouses.

Table 2

British, Canadian and American Tax Rates on Distilled Spirits, Beer and Cigarettes ^{1/}

	British:	Canada: ^{2/}	Federal:	Combined Federal and aver- age State excise tax:	Combined Federal and high- est State excise tax:	Highest State excise tax
Spirits, domestic, per U. S. proof gal.	\$14.23	\$5.11	\$4.00	\$5.08	\$ 6.00	\$2.00
Beer, domestic, per bbl. of 31 U. S. gals.	11.62	9.04	6.00	7.35	12.62	6.62
Cigarettes, per thousand, weighing 3 lbs.	11.70	6.00	3.25	4.56	5.15	2.50

Treasury Department, Division of Tax Research

^{1/} Spirits: The license States, the District of Columbia, and the three monopoly States (Vermont, Ohio, Wyoming) which impose specific excise taxes were included in the determination of the average and highest State excise rates. The 14 monopoly States which do not impose specific excise taxes were not included. The mark-ups in the sales prices in State stores in all the monopoly States include some amounts which are equivalent to a tax. These amounts are, however, not determinable and hence not included in the computation. Retail sales taxes imposed in some States on sales of distilled spirits were not included. On the foregoing basis, the highest State rate is \$2.00 per gallon imposed in Vermont, a monopoly State. The highest rate in the license States is \$1.92 per gallon in South Carolina. Sales of distilled spirits at retail average about 90 proof. If adjustment were made to 100 proof, the average State rate would be equivalent to \$1.20 per gallon and the rate in Vermont \$2.22. The average State rate is weighted by consumption of distilled spirits during the calendar year 1940, as reported by the Distilled Spirits Institute.

Beer: The highest State excise rate on beer is imposed in Mississippi. The alcoholic content of beer sold in Mississippi cannot legally exceed 4 percent by weight. On beer sold in containers, the rate in Georgia is the same as in Mississippi but on draft beer it is \$4.50 per bbl. Retail sales taxes imposed in some States on sales of beer were not included. The average State rate is weighted by consumption for the calendar year 1940, as reported by the United States Brewers' Association.

Cigarettes: For Great Britain, the main duty on unmanufactured tobacco was used instead of the nominal rate on cigarettes. For Canada the rate of tax is on cigarettes weighing not more than 2½ lbs. per M. The Canadian rate of tax on cigarettes weighing more than 2½ lbs. per M is \$11 per M. In the United States the highest State excise rates on cigarettes are imposed by Louisiana, Arkansas and Oklahoma, where the tax is 5¢ per standard package of 20 cigarettes. The average State rate is unweighted since consumption data are not available. Weighting would not, however, greatly affect the average since the largest number of States (18 out of 29) and the most populous (including New York, Pennsylvania, Ohio, Massachusetts, Wisconsin and Connecticut) impose a 2¢ tax per package of 20 cigarettes.

^{2/} Dominion taxes only. Sales of alcoholic beverages are generally provincial monopolies and no specific provincial taxes are imposed. Specific excise taxes on tobacco are not imposed by the Provinces. In the provinces of New Brunswick and Quebec, however, 10 percent retail sales taxes are imposed on tobacco products.

The British pound was converted at \$4.00.

TREASURY DEPARTMENT

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INTER OFFICE COMMUNICATION

DATE October 31, 1941

TO Secretary Morgenthau
FROM Mr. George Buffington

Following your request, Mr. Hampton A. Rabon, Jr., left on October 29 to call on banks to obtain their reaction to the folder "Know Your Taxes". I have arranged his itinerary in such a way that he will communicate with us at intervals making it possible to expand or contract the scope of his investigation.

G.S.

October 31, 1941
9:14 a.m.

Operator: Go ahead.

Doctor Klein: Hello.

EMJr: Yes.

K: Mr. Morgenthau.....

EMJr: Talking.

K: This is Dr. Klein.

EMJr: Yes, doctor.

K: I thought you'd be interested to know that we got Mrs. Cochran safely to Shepard Pratt last night.

EMJr: Oh, good.

K: They had both the police car ambulance and a private ambulance back up to the hotel where she was picked up and gave her the choice of either going to Gallinger or Shepard Pratt, and she chose the latter.

EMJr: I see.

K: And I got word from the ambulance people that she was gotten there safely without any further trouble about nine o'clock last night.

EMJr: Well, I hear you had a repetition of the afternoon.

K: Yes, Mr. Shaw was quite exercised about it, but.....

EMJr: You were called in on that, too.

K: Well, she went over there, you see. She went over to Secretary Hull's office and raised quite a rumpus over there, but we subdued that out

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right and there's no difficulty over there. We just let her go from there and had the police bureau, the women's bureau, take charge of the matter and arrange it so that they'd be available. When she saw that she had no choice but to go to one or the other place, she chose the right place.

HMJr: Well, we accomplished what we set out in the morning.....

K: Yes.

HMJr:to get her into a private institution.

K: Yes. Yes. I don't - I knew that she wouldn't go of her own free will, and I'm sorry that that other plan didn't work out, about having nurses with her; but I think it's just as well that she's over there.

HMJr: Oh, yes.

K: All right, sir. I thought.....

HMJr: No, I'm delighted that you called me, but then I was going to call you.

K: Well, I knew that you'd be interested and that's why I bothered you, sir.

HMJr: It's no bother.

K: All right.

HMJr: Thank you.

K: Yes, sir. Good-bye.

October 31, 1941
10:45 a.m.

HMJr: Hello. Hello.

Postmaster
General
Walker:

Hello.

HMJr: Frank?

W: Hello, there, Henry.

HMJr: How are you?

W: Fine, sir. How are you?

HMJr: I just wanted to tell you that your voice
came over the radio swell the other night.

W: Good.

HMJr: I've never heard it better.

W: That's fine, Henry.

HMJr: And I wanted to thank you for going on.

W: You know on that trip I made fifteen speeches
for your bonds and stamps?

HMJr: That's wonderful.

W: I went down through Missouri, Oklahoma, Texas,
Louisiana and Mississippi, Kentucky and
Tennessee.

HMJr: I'll be darned.

W: And -.....

HMJr: Well.....

W:the sentiment down that way is fine,
Henry.

HMJr: Good. Well, I appreciate all you're doing

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personally and also your department, and I wanted to tell you that.

W: Thanks so much. Say, Henry.....

HMJr: Yeah.

W:why didn't you give us that five or six thousand dollars for those maps?

HMJr: I don't know what you mean.

W: Well, you know about all the maps that we're going to put in all the post offices, don't you?

HMJr: No, I don't.

W: It's going to cost fifty or sixty thousand dollars, but we've gotten down now and we can get them for five or six thousand.

HMJr: Yeah.

W: If you pay the money.

HMJr: Maps?

W: Yes. I showed them to the boss, and he thinks it's a great idea. It shows different points and how long it will take a plane to fly from different points in the United States to.....

HMJr: Have you got a copy of one?

W: Yeah.

HMJr: Would you send it over to me with a little note?

W: I will.

HMJr: And with the five or six thousand, I'll give you an answer.

W: Fine.

HMJr: I have never seen it.

W: Yeah. I'll send it over to you today.

HMJr: Thank you.

W: All right, Henry.

October 31, 1941
11:23 a.m.

HMJr: Hello.

Operator: Go ahead.

HMJr: Hello.

Dr. Randolph
Burgess: Hello, Henry.

HMJr: Randy?

B: How are you?

HMJr: Fine. How are you?

B: Fine.

HMJr: Look. I want to ask you something. I've tried
to get Gordon, but they tell me he's not in.

B: No, he's had a bad throat for a few days.

HMJr: I see. And if you think you can't do this,
forget I asked you, will you?

B: Yeah.

HMJr: What I'd like to get from you if I could would
be a sort of a diary of some manufacturers who
come down here to Washington and have gotten
contracts - defense contracts - as to the troubles
that they went through from one department to
another, and one bureau.

B: Yeah. Yeah.

HMJr: Now, frankly, I want it for the President.

B: Yeah.

HMJr: He's asked me to get it.

B: Yeah.

HMJr: And I know that in the first place, Gordon's
gotten - through his brothers and so forth -

- 2 -

he's in a lot of his own business.

B: Yeah.

HMJr: Then maybe possibly through your trustees. Well, I was thinking, Mr. Jones comes down here and Mr. Smith. And what that fellow had to go through - day by day.

B: Exactly.

HMJr: I mean, and give it day by day.

B: Yeah.

HMJr: Until he was - and from one bureau to another - back and forth - particularly if he needed some facilities.

B: That's right.

HMJr: And this is it, what that fellow's got to go through in order to get a contract and how many days or months elapsed.

B: Yeah.

HMJr: Now, do you think you could get that for me?

B: Absolutely. Yeah.

HMJr: Now, could you get it without anybody knowing it's for me?

B: Yeah, sure.

HMJr: What?

B: Sure, I can.

HMJr: Can you?

B: Yeah. It'd be just our idea.

HMJr: And - I mean, do you think you could get me some nice, good examples?

B: I don't think it would be any trouble at all.

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HMJr: The trouble would be to sort them out.

B: (Laughs) Yeah.

HMJr: Now, would you give me some - you think of some where the people couldn't get the business and had the facilities?

B: Well.....

HMJr: Or would that be more difficult?

B: Where they could not?

HMJr: Where they didn't get it.

B: Yes.

HMJr: I'm not so much interested in that at the moment.

B: Yeah.

HMJr: But you might have that in the back of your head, of some fellow that came down here and had a plant, crazy to get some business, and couldn't.

B: Yeah. Mostly there's a reason on that.

HMJr: Well, what I was asked to get was the conflict and the difficulties that a manufacturer has to go through before he can get a signed contract - his day by day troubles and how long it takes.

B: That's right.

HMJr: See?

Ht: That's right. This is a good fellow who really rates it that we want to have get contracts.

HMJr: That's right.

B: That's right.

- 4 -

HMJr: And on - "I started on such and such a date on such and such an order."

B: Yeah.

HMJr: And if you in some way could identify it so I could tie it up to the particular appropriation, you see.

B: Yes.

HMJr: So I could go back and say - I could say, "On June first Congress passed an appropriation for so many machine guns, or so much this and so much that."

B: Yes.

HMJr: And - I mean if I could get the appropriation numbers he's working under, you see.

B: Yeah.

HMJr: If that's possible.

B: Yeah.

HMJr: If not, if you'd just identify it, then I could look it up.

B: Yeah, that's right.

HMJr: Because I want to show that on such and such a date the appropriation passed. Now, Mr. Jones came down here and he's got such at the factory, and a description of his factory and his facilities, and he wanted the business and this is what this man went through.

B: Yeah.

HMJr: I.....

B: Of course, some fellow may shy off from.....

HMJr: Oh, I.....

- 5 -

B: We'll work it out.

HMJr: If I could get a half a dozen examples.

B: Sure.

HMJr: That oughtn't to be hard.

B: Yeah.

HMJr: You may have them right up there with Pratt and Whitney.

B: Well, their experience might be pretty interesting.

HMJr: I mean, Pratt and Whitney, and then there's the Machine Tool Company that he's interested in out in Ohio.

B: Yeah. General Machinery.

HMJr: I mean, he maybe wouldn't have to go outside of his family.

B: Yeah. Yeah.

HMJr: See?

B: Well, we can work it out all right, Henry.

HMJr: Now, could I get that by Wednesday morning?

B: I think so.

HMJr: Good. How will you get it into my hands?

B: Well, we'll.....

HMJr: Have you got a representative down here?

B: No, we haven't. Well, I'll either get it by special mail or send somebody down with it.

HMJr: Will you?

B: Yeah.

HMJr: All right. I'd like it Wednesday morning.

B: Yeah.

HMJr: And - but they mustn't know it's for me.

B: That's right.

HMJr: See?

B: Yeah. Yeah. No, we'll just be doing it because we think we might be able to use it.

HMJr: Right. And it's going to go from me to the President.

B: Yeah. We'd be very glad to do that, Henry.

HMJr: Don't you think in the interest of the.....

B: Oh, I think that's very useful.

HMJr: Because, you see the President - no one had the nerve to tell him.

B: Yeah. Yeah.

HMJr: Now, if he gets this, then he's going to do something about it.

B: Yeah, that's right. I believe in these chasers. For example, I'm working right now on trying to get some typical cases of the effects of taxes on business.

HMJr: Yeah.

B: I'm going to send you some of those along today.

HMJr: All right.

B: But I'd be glad to go at this.

HMJr: I want the case history.

B: That's right.

HMJr: Good-bye.

B: Good-bye.

HMJr: Thank you.

B: Good.

HMJr: Good-bye.

B: Good-bye.

MEMORANDUM RE THE CONSOLIDATION
IN THE PROCUREMENT DIVISION OF
THE PURCHASING ACTIVITIES OF THE
ENTIRE GOVERNMENT.

10/31/41

Existing law authorizes the consolidation of all Government procurement functions, including those of the Army and Navy, in the Treasury's Procurement Division. This power stems from Executive Order No. 6166 of June 16, 1938, which created the Procurement Division. Executive Order No. 6166 is, in effect, a reorganization plan promulgated under the Reorganization Act of 1933 and as such has the force and effect of law. The pertinent provisions of this Order are as follows:

"The function of determination of policies and methods of procurement, warehousing, and distribution of property, facilities, structures, improvements, machinery, equipment, stores, and supplies exercised by any agency is transferred to a Procurement Division in the Treasury Department, at the head of which shall be a Director of Procurement.

* * * * *

"In respect of any kind of procurement, warehousing, or distribution for any agency the Procurement Division may, with the approval of the President, (a) undertake the performance of such procurement, warehousing, or distribution itself, or (b) permit such agency to perform such procurement, warehousing, or distribution, or (c) entrust such

- 2 -

performance to some other agency, or (d) avail itself in part of any of these recourses, according as it may deem desirable in the interest of economy and efficiency. When the Procurement Division has prescribed the manner of procurement, warehousing, or distribution of any thing, no agency shall thereafter procure, warehouse, or distribute such thing in any manner other than so prescribed.

"The execution of work now performed by the Corps of Engineers of the Army shall remain with said corps, subject to the responsibilities herein vested in the Procurement Division.

"The Procurement Division shall also have control of all property, facilities, structures, machinery, equipment, stores, and supplies not necessary to the work of any agency; may have custody thereof or entrust custody to any other agency; and shall furnish the same to agencies as need therefor may arise."

Under the Executive Order, the Procurement Division not only has the function of determining procurement policies and methods for the entire Government, but also is authorized "with the approval of the President" either to (a) undertake the performance of procurement work of any agency, or (b) permit such agency to perform its own procurement work, or (c) turn the procurement work of any agency over to any other agency, or (d) employ any combination of the foregoing as may be deemed desirable from an economy and efficiency standpoint.

The Procurement Division has not actually taken over the procurement work for the whole Government. It has never taken over Army or Navy procurement work, and there are also many other exceptions. However, these exceptions are on sufferance only and without legislation Procurement could tomorrow take over all procurement functions for the whole Government, including the Army and the Navy.

Furthermore, when Procurement takes over the buying for another agency, a provision in the current Treasury-Post Office Appropriation Act permits the transfer of funds of the other agency to pay Procurement's administrative expenses. This does not, of course, authorize the transfer to Procurement of actual appropriations available for the purchase of defense or other supplies or take away from the agencies their authority to determine what supplies shall be bought.

On June 10, 1939, the President approved Director's Order No. 73, which contemplated the ultimate transfer to the Procurement Division of the purchasing functions of all agencies except the Army, the Navy, and the Marine Corps.

For all practical purposes the authority conferred by Order No. 73 has never been exercised. However, the authority

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still exists and can be extended to cover the purchasing functions of the Service Establishments by means of the attached draft of order for signature by the Director of Procurement and approval by the Secretary of the Treasury and the President. Under this order, the Procurement Division could be made the purchasing agency for all agencies of the Government, except Government corporations. This exception is due to the fact that the old Reorganization Act, under which Executive Order No. 6166 was issued, did not authorize the President to reorganize Government corporations. Since the Reconstruction Finance Corporation and its subsidiaries are included within the exception, it assumes some importance from the standpoint of defense purchasing.

ORDER AMENDING DIRECTOR'S ORDER NO. 73

Pursuant to the authority vested in the Procurement Division of the Treasury Department by Executive Order No. 6166 promulgated by the President under the Act of June 30, 1932, as amended, and transmitted to the Congress June 10, 1933, and in order to promote the national defense by increasing efficiency in Government procurement operations, Director's Order No. 73, issued by the Director of Procurement, and approved by the President on June 10, 1939, is hereby amended as follows:

- (1) By changing the comma after the word "Government" in section 1(a) to a period and deleting the words "except the War and Navy Departments and the Marine Corps.";
- (2) By striking out section 6 in its entirety and renumbering section 7 as section 6.

Director of Procurement

APPROVED:

Secretary of the Treasury

APPROVED:

The White House,

, 1941.

PROCUREMENT DIVISION ORDER PRESCRIBING THE
MANNER OF PROCUREMENT, WAREHOUSING, AND
DISTRIBUTION OF SUPPLIES FOR ALL AGENCIES
OF THE UNITED STATES.

Pursuant to the authority vested in the Procurement Division of the Treasury Department by Executive Order No. 6166 promulgated by the President under the Act of June 30, 1932, as amended, and transmitted to the Congress June 10, 1933, and in order to promote the national defense by increasing efficiency in Government procurement operations, it is hereby prescribed that:

1. As used in this Order

(a) The term "agency" means any department, commission, independent establishment, board, bureau, division, service, or office in the Executive Branch of the Government.

(b) The term "supplies" means materials, supplies, articles, facilities, improvements, machinery, equipment, stores, and all other personal property, including defense articles as defined in section 2(a) of the Act of March 11, 1941 (Public No. 11, 77th Cong., 1st Sess.).

(c) The term "procurement" means the purchase, rental, exchange, distribution, warehousing, and transportation of supplies, and all functions and services relating thereto.

2. The Procurement Division of the Treasury Department shall undertake the procurement of all supplies for all agencies: Provided, That any agency may continue to perform its procurement to the extent now permitted, until such date as the Procurement Division may designate with respect to specific agencies, specific kinds of procurement, or specific supplies.

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3. All records and property pertaining to, or utilized in, the procurement of supplies by any agency, and all personnel engaged in the procurement of supplies for any agency, are hereby transferred to the Procurement Division, such transfer to be effective upon such dates as the Director of Procurement may prescribe with respect to specific agencies, specific kinds of procurement, or specific supplies. Such part of the unexpended balances of appropriations or funds, available to any agency for personal services and other expenses, in connection with the procurement of supplies which the Secretary of the Treasury, with the approval of the Director of the Bureau of the Budget, shall transfer to the Procurement Division pursuant to Treasury and Post Office Departments Appropriation Act, 1942 (Public No. 88, 77th Cong., 1st Sess.), and any other law authorizing such transfer, shall be available for the use of the Procurement Division in performing the functions of procurement undertaken pursuant to this Order.

4. The Director of Procurement may, with the approval of the Secretary of the Treasury, issue such regulations and instructions as may be necessary to make the provisions of this Order effective.

5. The regulations governing the operation of the Branch of Supply, Procurement Division, approved by the President April 12, 1935, are hereby superseded to the extent that they are inconsistent with the provisions of this Order.

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6. This Order shall become effective on the date of its approval by the President and shall supersede Director's Order No. 73, approved by the President on June 10, 1939, which is hereby revoked.

Director of Procurement

APPROVED:

Secretary of the Treasury

APPROVED:

The White House,

, 1941.

October 30, 1941
3:46 p.m.

Guy
Vaughn:

Hello.

HWJr:

How are you?

V:

Well, I'm fine. What's wrong? I haven't heard from you for a long time.

HWJr:

Nothing's wrong. I wanted to talk to you and then if you don't think you can do what I ask, forget it, see?

V:

Yeah.

HWJr:

I am - very, very confidentially - looking into some of the troubles that a manufacturer has in signing up for contracts here in Washington. Hello.

V:

Yeah, I hear you.

HWJr:

It will only go to one place, and that's my superior.

V:

I see.

HWJr:

Now, what I really want is a sort of a diary on any particular contract recently where you went through with an engine, or for planes, from the very time you started - the various troubles that you had.

V:

All right. I'll give you a diary and what happened. See....

HWJr:

I mean, for instance, let's say that there's an appropriation, but if you don't have that, I can't get that; but at least, you can tell me which appropriation it would come under. I mean, if you're working on an appropriation next last July or last - a year ago - and under that appropriation that you've been negotiating to get a contract, do you see?

V:

Yeah.

- 2 -

HMJr: What I want to show him and what he's asked me to get for him in the strictest confidence, I don't want anybody to know it, is.....

V: All right. Of course, you realize we didn't have very much difficulty in making contracts in Washington. As I recollect it - now, I'd have to.....

HMJr: Well, haven't you got some recent ones?

V: What's that?

HMJr: Haven't you made some recent ones for planes?

V: Have we what?

HMJr: Have you made any recent contracts?

V: No, not of any substantial proportions; but I'll - I tell you what I'll do. I'll review the contracts that were made about ten months ago - from ten months ago up, you want, I imagine.

HMJr: Well, from ten months ago down to date, yes.

V: Yeah. All right, I'll do that; and in order to get that together, it'll take me two or three days.

HMJr: Well, do you suppose I could have it by Tuesday?

V: I'll do my best and give you something by next Tuesday.

HMJr: Now, you know what I want?

V: I know. You want really a record of the transactions involved in making contracts of any substantial proportions - that is, our experience - we went to Washington on a certain date.

HMJr: A certain date that you went to the Navy, and the OPM and the RFC and.....

V: And we saw up there General Eccles, or Colonel Smith or anybody you want to mention.

HMJr: Yeah.....

V: We saw so and so. We went then to - back to our plant and changed the setup and changed the bid and all that sort of thing.

HMJr: Yes. And then if after you got started you were delayed because of change of orders or something.

V: Right.

HMJr: In other words, until the time - what - you get the picture. What your troubles were, you see.

V: I understand.

HMJr: And then.....

V: What the delays were and what caused them, if any.

HMJr: If any.

V: Other than normal, or give you the normal setup.

HMJr: I mean, you may think it's normal if it took you three months.

V: Oh, no. No, unless something that couldn't be decided on for three months, it was impossible; I don't remember anything like that though, offhand. So I'll do that for you, Mr. Secretary, right away.

HMJr: Yes. Now, how will you get it into my hands?

V: I'll send it by a messenger, if you say.

HMJr: I think you'd better.

V: I'll put a man right on a plane and send him down and have them handed to you direct.

HMJr: Yeah. Have them ask for me and put it into my own hands.

V: All right, I'll do that.

HMJr: And I'll appreciate it, and so will my boss.

V: All right, sir.

HMJr: And then.....

V: And we'll try and please you both.

HMJr: And I'm not going around and asking many people, because there are not many people I've got the confidence in to ask.

V: I am sure that it is not misplaced in this case.

HMJr: Because you do planes as well as engines, don't you?

V: Engines, propellers and airplanes.

HMJr: That's right.

V: All three.

HMJr: That's right.

V: And better than United. (Laughs)

HMJr: What do you mean?

V: I mean we make better ones than United Aircraft do. They make the same thing.

HMJr: (Laughs) In other words, just a little plug for your side.

V: That's right.

HMJr: Okay.

V: All right, sir.

HMJr: Thank you.

V: Good-bye.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE October 31, 1941

TO Secretary Morgenthau
FROM Mr. Coe vFC

Subject: Triangular Lend-Lease transactions

The proposition is that in return for \$1 billion of food which the British Government gets under Lend-Lease from the United States and which it sells to its people for £ 250 million, the British Government should, say, purchase £ 250 million of wool from Australia and give it to the United States, either now or later.

Pros of this transaction

1. The British Treasury would have to pay out on wool all that it received from selling food. This would eliminate the criticism that the British Government was "making money" out of Lend-Lease food. This is probably Hopkins main purpose.
2. It would be a true Lend-Lease transaction--return of goods for goods. Most Americans, expecting nothing to be returned, would be surprised and delighted.
3. The United States is a large wool importer. There would be no loud protests from domestic producers, as with other commodities. Most Americans would consider that "useful" return had been made.
4. The United States Treasury would stand to regain \$1 billion, and the budgetary and debt picture would be brightened.
5. If a single large-scale "return" were negotiated, the pressure for an over-all agreement would be diminished, and it would be easier to get the February (?) Lend-Lease appropriation through.
6. Government stockpiles of goods are excellent aids to stabilizing prices and combating foreign or domestic monopoly control.

Cons

1. The prospects for transfer of \$1 billion of wool or other commodities within a year are poor. The British are either (a) using the commodities or (b) selling them for dollars or other foreign exchange.

On the basis of their figures about their foreign exchange position, they could not now afford to give us goods which bring in \$1 billion unless they sold some foreign investments. Perhaps in a year they could.

2. Where the sterling area is storing goods in surplus, transfer to the United States would cost no foreign exchange. But the surplus of wool is probably not great, and we have just begun to buy \$60 million of Empire wool for a stockpile.

The British are accumulating some surpluses inside and outside the Empire, but most of these are agricultural products.

3. One billion dollars of wool is 4 years' imports into the United States at the exceptionally high level of this year. If the deal is for \$1 billion, it might better include tin, rubber, and wool. However it was made up the British would probably need more Lend-Lease aid if they made early transfers.

4. Even delivery at later dates--unless the goods represent additions to what we would otherwise buy--will raise a foreign exchange problem for the British, since it will reduce their foreign exchange income.

Conclusions

1. The only way to effect a present return of \$1 billion of goods is for the British to

(a) transfer title to various surplus Empire goods (cocoa, tea, cotton, wheat), many of which we would not want;

(b) sell investments in order to give us the Empire goods we now buy for dollars;

(c) get still more Lend-Lease aid, so that they need less dollars and other foreign exchange.

Of these, only (a) seems likely, and we might find out what surpluses the British have inside and outside the Empire.

2. The British could arrange to transfer wool and other goods in the future, either for United States consumption or for stockpiles.

Lend-Lease may make their foreign exchange position favorable enough for transfers in the next 6 or 9 months.

The determination of whether (or when) such transfers to the United States can be made without reducing British imports should be made upon the basis of the whole British foreign exchange position (which we do not know) and not simply upon the dollar position of the British.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

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DATE October 31, 1941

TO Secretary Morgenthau
FROM Mr. White

Subject: Great Britain - Criticisms of Production

The development of a bitter controversy in England over the British war effort on the production front is reflected in the English press in September and early October. Your attention is called to the following indications of this controversy:

1. The resignation of four members of Parliament from the Air Services Sub-Committee of the Select Committee on National Expenditures was announced early in October.

The resignations were said to be caused by the suppression of a report which these four members wanted to publish to the House of Commons. The report apparently contained charges of wasteful and inefficient administration by the Ministry of Aircraft Production in factory work.

2. Charges have been widely made that the Government is taking from industry too many skilled workers for the armed forces.

The policy of the Government is not entirely clear, although Mr. Bevin says that

- (a) the Government is attempting to give due consideration to the needs of both industry and the armed forces for skilled men, and indicates that
- (b) more women will be called up for industrial service.

3. Other criticisms of the war effort in industry are revealed by demands for

- (a) better mobilization of small firms,
- (b) decentralization of Government administration, through giving greater power to Regional Boards,
- (c) more consultation with workers' representatives by management.

(Clippings from the British press, Sept. 2 - Oct. 10, 1941, received from Casaday, London.)



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EMBASSY OF THE
UNITED STATES OF AMERICA

LONDON, September 27, 1941.

Dear Mr. Secretary:

Enclosed are some clippings dealing with the subject of "War Production."

In the past week or so there seems to have been a definite revival of criticism and self examination with respect to the war effort, comparable with that which was in evidence some months ago. In the interim there seems to have been a lull in such criticism, partly due, no doubt, to the strong statements made on the subject by the Prime Minister and other government officials. The current "Thanks for Russia Week" appears to have stimulated a great deal of enthusiasm and an unusually high level of efficiency on the part of the workers. But it may also have led critics to see shortcomings in general organization and in the government controls which were not noticed before.

There have been several types of criticism recently. The Daily Mail for example, has discovered what it calls a "Valley of Chaos" somewhere in Western England. It is charged that various industrial supply facilities as well as many public services are completely inadequate to care for the needs of the industries and the workers which have settled there since the outbreak of the war and that the resulting disorganization has brought about a 30% cut in efficiency.

The Financial News calls for a greater concentration in industrial organization as vital to the war effort. At the same time this and other financial papers are asking whether the present controls of profits and wages are affording enough "incentive" to bring out the best efficiency.

/The

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

The recent meeting here of the Engineering Industrial Association has also given voice to much criticism, most of it being directed against the "dead hand of Treasury control", which, it is alleged, shackles industry and kills efficiency. Other charges have also been made such as lack of coordination among the various government departments and similar matters. These will be apparent from the enclosed clippings.

Sincerely yours,

L. R. Friday

LWC/RF





EMBASSY OF THE
UNITED STATES OF AMERICA

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London, October 11, 1941.

Dear Mr. Secretary:

The critical attitude toward the rate and efficiency of War Production, on which I enclosed a number of clippings in my letter of September 27, is continuing. Enclosed herewith are some further clippings and a copy of Hansard for October 8, containing the debate on Manpower.

In fact the controversy over War Production has shifted its emphasis and now seems to center largely on the issue of Manpower. With the worsening situation on the Eastern Front the familiar argument of the past few months, "production will win the war" has been greatly weakened. It is beginning to be realized that while production must indeed be constantly stepped up, there is now or may be soon an imperative need for a larger and better trained armed force. This means the Army must have skilled men to operate, service and repair the mechanical equipment which War Production presumably will continue to supply.

How much Manpower and of what skills are available? Ditto for Woman power. In what ratio should this force be allocated to the Armed Services as against War Production? Above all, is there really a Plan, a Higher Strategy for the conduct of the war which has taken the whole problem of Manpower into account?

These are some of the questions being asked. The general feeling seemed to be that the House debate did not adequately answer any of them.

The controversy has been sharpened by the conflict between Bevin and Citrine. The fighting word "Quisling" has been hurled and there is considerable confusion as to the position which organized labor as a whole takes on

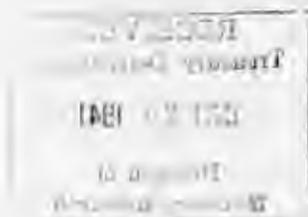
The Honorable
Henry Morgenthau, Jr.,
Secretary of the Treasury,
Washington.

on this question. For example the T.U.C. has in general favored the policy of reserving skilled men from military service for key jobs in war industry but at the same time the Daily Herald, (referred to as a "Quisling" by Bevin) has been extremely outspoken in agitating for more positive aid to Russia, the compulsory calling up and allocation of people in non-essential occupations and for an improved military. Even invasion has been suggested.

Meanwhile the Financial News continues its campaign re "Incentive", the E.P.T. and "The dead hand of Treasury control." I say the campaign is continuing, although I believe it has decreased somewhat in intensity and in some respects assumed a more subtle form, since the Chancellor of the Exchequer's speech in which he stood firm on the established policy followed thus far.

Sincerely yours,

W. L. L. L.



TREASURY DEPARTMENT

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INTER-OFFICE COMMUNICATION

DATE OCT 31 1941

TO Secretary Morgenthau

FROM Mr. Foley

In accordance with the request contained in Mr. Thompson's memorandum of December 26, 1939, there is attached a summary report of studies or projects carried on in the Office of the General Counsel for the month of September, 1941.

Attachment

Smith

SUMMARY REPORT ON STUDIES AND PROJECTS IN
THE OFFICE OF THE GENERAL COUNSEL -
SEPTEMBER 1941

The following work was done under the supervision of
Assistant General Counsel Cairns:

1. Legislation. Two pending bills, H. R. 2628 and S. 413, would make it an offense to bring into the United States matter of an obscene nature and also to carry such matter in interstate commerce. The bills specifically place investigative jurisdiction of violations in the Federal Bureau of Investigation, although investigations of such violations under existing law, insofar as foreign commerce is concerned, have been, and should be, in the Treasury Department. A conference was held by Mr. Spingarn and Mr. Chambers with Alexander Holtzoff of the Department of Justice and it was pointed out to him that jurisdiction over violations involving foreign commerce should be in this Department rather than in the Federal Bureau of Investigation, and that the portions of the proposed bills which involve foreign commerce were unnecessary, inasmuch as they were fully covered by existing laws. Mr. Holtzoff stated that the Department of Justice is agreeable to the elimination of the portions dealing with foreign commerce, and Mr. Spingarn is now taking up with the appropriate House and Senate Committees the question of eliminating those portions of the bills.

2. Neutrality. On September 16, 1941, all collectors were instructed that, in accordance with a recent opinion of the Attorney General, the term "United Kingdom" as used in the President's proclamation declaring certain countries to be belligerent includes only England, Wales, Scotland, and Northern Ireland, and, therefore, the Neutrality Act does not apply to shipments to overseas colonies and possessions of Great Britain which are not in combat areas and are not specifically enumerated in the proclamation.

3. Currency Conversion. On September 4 a conference was held by Mr. Cairns regarding the Barr case, in which the importer is protesting in customs court against the use of the official rate for the pound sterling, rather than the free rate, in determining the duty due on certain merchandise. The conference was attended by Mr. Agee, Mr. Feidler, Mr. Everett Smith, and Mr. Donohue, of the office of the Assistant Attorney General in New York, who will represent the Government at the trial. Mr. Wolf and Mr. Chambers also participated in the conference.

4. Exclusion of colored reproductions of foreign postage stamps under section 161 of the Criminal Code. An opinion, which was prepared by Mr. Collins for the Commissioner of Customs and approved on September 2, 1941, concludes that

foreign postage stamps are "obligations" or "securities" of a foreign government and colored reproductions thereof may be excluded from the United States under section 161 of the Criminal Code (U.S.C. title 18, sec. 275).

5. Local tax on Philadelphia Mint employees. An opinion, which was prepared by Mr. Collins for the Director of the Mint and approved on September 20, 1941, concludes that employees who were residents of Philadelphia were subject to the local tax on salaries. However, prior to January 1, 1941, non-residents of Philadelphia could not be taxed on income received from the Mint since the Mint was a Federal area and permission by the Federal Government to tax income earned in that area was not given prior to January 1, 1941.

6. Study of Treasury Criminal Cases. A preliminary confidential report with statistical analysis of the contents of comparative tables, based on statistics received each month on Treasury criminal cases, for the fiscal years 1937, 1938, 1939, and 1940, has been completed.

The following matters received attention in the Office of the Chief Counsel for the Bureau of Internal Revenue:

7. Report on legislation relating to unemployment insurance for maritime industry. A report has been prepared on H. R. 5446 (77th Congress) at the request of Chairman Sland

of the House Committee on Merchant Marine and Fisheries. This bill, which would establish a system of unemployment insurance for the maritime industry, provides for two systems. The first, a completely Federal system under which unemployment benefits would be paid and employers would be required to pay "contributions", covers the so-called "deep-sea" portion of the industry. That system would be administered by the Railroad Retirement Board. The second system, covering maritime services on inland waters, including the Great Lakes, rivers, and ports, would be fitted into the existing Federal-State unemployment insurance program. Under the new Federal system, relating to "deep-sea" maritime services, the "contributions" required of employers would be collected not by the Commissioner of Internal Revenue but by the Railroad Retirement Board. The bill would implement the Board with all powers now conferred upon the Secretary of the Treasury, the Commissioner of Internal Revenue, and Collectors in connection with similar tax collections.

The following work was done under the supervision of Assistant General Counsel Bernard:

8. Fidelity Bond Bill (formerly identified as "Bond Survey")

(for description see original report, Item 10). The legislative section is still canvassing ways and means of securing the most effective sponsorship for this proposed legislation in Congress.

9. Federal Depository System (for description see original report, Item 6). This bill was sent to the Bureau of the Budget on July 24, 1941, for clearance, and is still being considered by that Bureau.
10. Law Committee of Defense Communications Board (for description see November report, Item 23). Mr. Spingarn in conjunction with the other members of the Law Committee of the Defense Communications Board assisted in the drafting of legislation which would give the President power to act with respect to wire services and other desirable features which are not now covered by section 606(c) of the Communications Act. He prepared a letter for the Secretary's signature to Mr. Fly, Chairman of the Defense Communications Board, commenting on this proposed legislation.
11. Administrative procedure bills. (for description see April report, Item 8). After clearance with all bureaus and branches of the Department, the letter to the Senate Judiciary subcommittee considering these three bills (which also transmits a lengthy memorandum detailing the impact of these bills on each of the principal activities of the Treasury), prepared by the Legislative Section, was signed by Mr. Bell as Acting Secretary on September 3 and sent forward.

11. Proposed legislation to regulate production of opium poppies. (for description see May report, Item 9). The Legislative Section is rewriting the draft of the opium poppy seed bill, which was submitted to Commissioner Anslinger, in the light of the conference on this subject in Mr. Gaston's office on September 11, 1941.
12. Board of Legal Examiners (for description see August report, Item 7). Mr. Bernard, as the representative for Mr. Foley, is continuing his work on the Board of Legal Examiners.
13. Un-American Activities Committee (for description see September report, Item 8). Mr. Spingarn, as a member of the Treasury Committee considering charges of un-American activities on the part of Treasury employees, is continuing the study of the background and legislative history of acts prohibiting salary payments to employees advocating or belonging to organizations advocating the overthrow of government, with the purpose of preparing a memorandum thereon to assist in the formulation of standards for action by the Department committee.
14. Equalizing privileges of Government obligations. The Legislative Section is engaged in a study of the problems inherent in equalizing privileges of direct and guaranteed governmental obligations with the purpose of drafting a bill to effect such equalization.

The following matters were worked on under the direction of Mr. Bernard Bernstein, Assistant General Counsel, through October 19, 1941:

15. Foreign Funds Control.

- a. Educational Program: This phase of freezing control received special attention with particular emphasis on enlisting the cooperation and understanding of those groups in key positions in assist in the enforcement of the Order. Mr. Foley addressed the committee on insurance law of the American Bar Association on the subject "Freezing Control as a Weapon of Economic Defense". This office worked on this speech. Several meetings with bankers were held in the states of New York and New Jersey. A representative of this office (Murphy) and representatives of the Administrative office spoke at such meetings. This office also sent several representatives to the Foreign Trade Convention in New York City (Luxford, Reeves and Arnold). They participated in a panel discussion of trade problems and freezing control and also discussed the individual freezing problems of those attending the convention. Other similar meetings were arranged and attended. These matters were worked on by Messrs. Bernstein, Luxford, Reeves, Murphy and Arnold.

The over-all picture of an integrated educational program was also the subject of study and conferences both within the Treasury and also with the interested groups outside the Department. In the furtherance of such program letters were sent to the presidents of all the banks in the United States, telegrams were sent to the secretary of each state bankers' association, and the active cooperation of the American Bankers Association, including the magazine Banking, was obtained. The assistance of the Federal Reserve Banks was also enlisted. This office participated fully in this project. These matters were worked on by Messrs. Bernstein and Luxford.

Intensive educational work was carried on in the field of reports on TFR-300. Conferences with all of the interested groups were held by Reeves and Arnold and the issuance of question and answer pamphlets for the various groups was continued. These matters were worked on by Messrs. Bernstein, Reeves and Arnold.

- b. Decentralization of Administration: In cooperation with representatives of the Federal Reserve Bank of New York steps have been taken to decrease, where desirable, the volume of license applications referred by the Federal Reserve Bank of New York to this office

for consideration. It is expected that the steps taken to assure decentralization of administration will permit the personnel of Foreign Funds Control to devote a greater amount of time to the analysis of reports with respect to transactions and persons. These matters were worked on by Messrs. Bernstein, Luxford and Golding.

- c. General Licenses: General licenses were issued relating to transfers of securities to blocked accounts, for the payment of necessary living expenses within the United States of American citizens residing abroad, and, at the request of the Chinese Ambassador, conferring upon certain Chinese partnerships the status of generally licensed nationals. General License No. 53 was amended to bring within the scope of the generally licensed trade area territories now under British or free French domination. Consideration was also given to the amendment of General License Nos. 32, 38, 42, and 72. Messrs. Bernstein, Luxford and Golding worked on these matters.
- d. The Proclaimed List of Certain Blocked Nationals: This office, in conjunction with members of the State Department, prepared a memorandum outlining a standard of conduct for all American citizens and American

concerns in Latin America in their dealings with Proclaimed List nationals. Such memorandum was sent by the State Department to all diplomatic and consular offices as a circular instruction on September 20, 1941. It is thought that such instructions will go far toward helping to achieve the objective sought to be attained by the promulgation of The Proclaimed List of Certain Blocked Nationals. This office has worked with members of the State Department in formulating plans for lessening the impact of The Proclaimed List on the economies of the Central American Republics under appropriate safeguards to our interests. One of the men in this office (DuBois), together with a State Department representative, is in Central America studying this problem. Messrs. Bernstein, DuBois and Mann worked on these matters.

- e. Reporting of Foreign-Owned Property: The latest date upon which reports on Form TFR-300 may be filed was extended to October 31, 1941.
- f. Business Enterprises: In cooperation with the Securities and Exchange Commission and the Federal Bureau of Investigation, this Department began an investigation of the Sofina Corporation. Plans are now under consideration for handling the entire problem of Japanese trade.

The methods adopted by this Department in handling the problems of foreign-owned insurance companies were extensively considered. The problem of dealing effectively with a number of enterprises was given particular study. Messrs. Bernstein, Lawler, Kehl and Linville worked on these matters.

- g. Economic Defense: A memorandum was prepared for the Vice President outlining the economic defense activities in which the Treasury Department participates. Messrs. Bernstein and Luxford handled this.
- h. Program for Japan: During the month members of this office, in conjunction with representatives of the Administrative office of Foreign Funds Control and the office of Monetary Research, studied a program for stronger political and economic action in respect to Japan. Messrs. Bernstein, Lawler and Kehl worked on this.
- i. Program for China: Work has continued on a program to coordinate freezing control with stabilization operations in order to improve the economic position of China. There have been further exchanges of cables on the subject, as well as some work on the question of drafting licenses necessary to effect any such program. Messrs. Bernstein and Luxford worked on this matter.

j. Freezing Problems Relating to Insurance Companies:

A number of conferences were held with representatives of the various insurance companies on the subject of answering their questions relating to freezing control. These involve both the question of interpreting the Executive Order and the procedure to be followed in executing Form TFR-300. A pamphlet of questions and answers dealing with insurance matters is in the process of preparation. Also under consideration is the problem of the relation of insurance companies to persons whose names appear on the Proclaimed List. These involve a consideration of the free insurance practices of British firms and the extent to which the Latin American insurance companies will cooperate with the United States in any program of this kind. Messrs. Bernstein, Reeves, Arnold and Golding worked on this matter.

16. Mixed Claims. This office cooperated with the Division of Accounts in the preparation of a new distribution of Class 3 awards (i.e. awards in excess of \$100,000) of the Mixed Claims Commission. Mr. Bernstein and Miss Hodel worked on this.

17. Mexico. This office worked with the Under Secretary and the Division of Monetary Research and with the Mexican representatives in drafting the new stabilization agreement with Mexico and an agreement for the purchase of silver from Mexico. A press release was also prepared and assistance was rendered on the over-all press release to be issued by the State Department in connection with this matter. Mr. Bernstein handled this matter.

18. Iceland. This office cooperated with the Under Secretary and the Division of Monetary Research in the preparation of a stabilization agreement with Iceland, and participated in conference with the State Department and Icelandic officials in this connection. Mr. Bernstein worked on this matter.

19. Russian Agreement. This office prepared an agreement for the purchase of \$30 million of Russian gold to be delivered in 180 days and also worked on matters relating to the delivery of gold under the first gold agreement with Russia. Mr. Bernstein worked on this matter.

20. Certifications Under Section 25(b) of the Federal Reserve Act. Licenses were issued and papers prepared in connection with certifications under Section 25(b) of the Federal Reserve Act with authority to operate the following accounts:

- (a) Royal Norwegian Government account with the Federal Reserve Bank of New York.

- (b) Danmarks Nationalbank account with the Federal Reserve Bank of New York. This was a very important matter which was worked out in detail by this office and gives to the Danish Minister in Washington control over the Danmarks Nationalbank account in the Federal Reserve Bank of New York. \$200,000 was transferred out of the account to the credit of the Danish Minister and used by him, among other things, in the attempted purchase of legation property owned by the German Government and now leased by the Danish Legation.
- (c) Bank Polski account with the Federal Reserve Bank of New York.
- (d) Yugoslav National Bank accounts at four banks in New York which enabled transfer of these accounts to the Federal Reserve Bank of New York for credit to the account of the Government of Yugoslavia.
- (e) Banque Nationale de Belgique account with the Federal Reserve Bank of New York.
- (f) The office also worked on the certification of the Bank of Greece account with the Guaranty Trust Company which has presented considerable difficulty in view of the fact that there is no Greek representative in this country with authority to deal over the account. Mr. Bernstein and Mr. DuBois worked on these matters.

21. Pioneer Import Case. In conjunction with Customs officials in New York City and the United States District Attorney's office in New York City the office has been making a careful study of Mr. Werner von Clemm and his two companies, Pioneer Import Corporation and Bridge Import Company. Customs is holding between \$300,000 and \$400,000 worth of diamonds and synthetic stones imported by these two companies. A grand jury investigation with respect to the diamonds is now in progress to determine whether any of the diamond shipments involve a violation of the freezing legislation. This study has involved conferences in New York City and in Washington. Mr. Bernstein and Mr. Sherbondy worked on this matter.

22. Additional Freezing Control Legislation. The office has been working on drafts of legislation which will serve to increase our statutory authority to deal with freezing control problems and other related problems of economic defense, with a view to being ready, should an appropriate occasion arise and, in particular, should a war situation develop, to strengthen the executive control over foreign-owned property in this country. Mr. Bernstein and Mr. Friedman worked on this matter.

TREASURY DEPARTMENT

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INTER-OFFICE COMMUNICATION

DATE October 31, 1941

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

You may be interested in reading the attached memorandum of the work done in the Legal Division during September and the first half of October on freezing control matters. The memorandum will give you a brief idea of what has been done in the freezing control field during that period.

In addition to the attached memorandum, you might like to read the minutes of the Interdepartmental Committee meetings during the same period.

E. H. F. L.

*Continue to send
me these kind
of reports
etc.*

Studies or Projects Worked on During September 1941

The following matters pertaining to Foreign Funds Control were worked on through October 19, 1941:

FOREIGN FUNDS CONTROL

Educational Program: This phase of freezing control received special attention with particular emphasis on enlisting the cooperation and understanding of those groups in key positions to assist in the enforcement of the Order. Mr. Foley addressed the committee on insurance law of the American Bar Association on the subject, "Freezing Control as a Weapon of Economic Defense". This office worked on this speech. Several meetings with bankers were held in the states of New York and New Jersey. A representative of this office and representatives of the Administrative office spoke at such meetings. This office also sent several representatives to the Foreign Trade Convention in New York City. They participated in a panel discussion of trade problems and freezing control and also discussed the individual freezing problems of those attending the convention. Other similar meetings were arranged and attended.

The over-all picture of an integrated educational program was also the subject of study and conferences both within the Treasury and also with the interested groups outside the Department. In the furtherance of such program letters were sent to the presidents of all the banks in the United States, telegrams were sent to the secretary of each state bankers' association, and the active cooperation of the American Bankers Association, including the magazine Banking, was obtained. The assistance of the Federal Reserve Bank was also enlisted. This office participated fully in this project.

Intensive educational work was carried on in the field of reports on Form TFR-300. Conferences with all of the interested groups were held by representatives of this office and the issuance of question and answer pamphlets for the various groups was continued.

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Decentralization of Administration: In cooperation with representatives of the Federal Reserve Bank of New York steps have been taken to decrease, where desirable, the volume of license applications referred by the Federal Reserve Bank of New York to this office for consideration. It is expected that the steps taken to assure decentralization of administration will permit the personnel of Foreign Funds Control to devote a greater amount of time to the analysis of reports with respect to transactions and persons.

General Licenses: General licenses were issued relating to transfers of securities to blocked accounts, for the payment of necessary living expenses within the United States of American citizens residing abroad, and, at the request of the Chinese Ambassador, conferring upon certain Chinese partnerships the status of generally licensed nationals. General License No. 53 was amended to bring within the scope of the generally licensed trade area territories now under British or free French domination. Consideration was also given to the amendment of General Licenses Nos. 32, 33, 42, and 72.

The Proclaimed List of Certain Blocked Nationals:
This office, in conjunction with members of the State Department, prepared a memorandum outlining a standard of conduct for all American citizens and American concerns in Latin America in their dealings with Proclaimed List nationals. Such memorandum was sent by the State Department to all diplomatic and consular offices as a circular instruction on September 20, 1941. It is thought that such instructions will go far toward helping to achieve the objective sought to be attained by the promulgation of The Proclaimed List of Certain Blocked Nationals. This office has worked with members of the State Department in formulating plans for lessening the impact of The Proclaimed List on the economies of the Central American Republics under appropriate safeguards to our interests. One of the men in this office, together with a State Department representative, is in Central America studying this problem.

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Reporting of Foreign-Owned Property: The latest date upon which reports on Form TFR-300 may be filed was extended to October 31, 1941. Other activities in this area are discussed under "Educational Program".

Business Enterprises: In cooperation with the Securities and Exchange Commission and the Federal Bureau of Investigation, this Department began an investigation of the Sofina Corporation. Plans are now under consideration for handling the entire problem of Japanese trade. The methods adopted by this Department in handling problems of foreign-owned insurance companies were extensively considered. The problem of dealing effectively with a number of enterprises was given particular study.

Economic Defense: A memorandum was prepared for the Vice President outlining the economic defense activities in which the Treasury Department participates.

Program for Japan: During the month members of this office, in conjunction with representatives of the Administrative office of Foreign Funds Control and the office of Monetary and Research, studied a program for stronger political and economic action in respect to Japan.

Program for China: Work has continued on a program to coordinate freezing control with stabilization operations in order to improve the economic position of China. There have been further exchanges of cables on the subject, as well as some work on the question of drafting licenses necessary to effect any such program.

Freezing Problems Relating to Insurance Companies:

A number of conferences were held with representatives of the various insurance companies on the subject of answering their questions relating to freezing control. These involve both the question of interpreting the Executive Order and the procedure to be followed in executing Form TFR-300. A pamphlet of questions and answers dealing with insurance matters is in the process of preparation. Also under consideration is the problem of the relation of insurance companies to persons whose names appear on The Proclaimed List. These involve a consideration of the free insurance practices of British firms and the extent to which the Latin American insurance companies will cooperate with the United States in any program of this kind.

PIONEER IMPORT CASE

In conjunction with Customs officials in New York City and the United States District Attorney's office in New York City we have been making a careful study of Mr. Werner von Clemm and his two companies, Pioneer Import Corporation and Bridge Import Company. Customs is holding between \$300,000 and \$400,000 worth of diamonds and synthetic stones imported by these two companies. A grand jury investigation with respect to the diamonds is now in progress to determine whether any of the diamond shipments involve a violation of the freezing legislation. This study has involved conferences in New York City and in Washington.

ADDITIONAL FREEZING CONTROL LEGISLATION

We have been working on drafts of legislation which will serve to increase our statutory authority to deal with freezing control problems and other related problems of economic defense. Legislation has been prepared with a view to being ready, should an appropriate occasion arise and, in particular, should a war situation develop, to strengthen the executive control over foreign-owned property in this country.

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October 31, 1941

MEMORANDUM FOR THE SECRETARY'S FILES

A meeting relative to the administration of Executive Order 8388 was held in Mr. Foley's office at 4:00 P.M. on October 30, 1941, attended from time to time by the following:

Messrs. Foley (Chairman), Pehle, B. Bernstein, Morris, Coe, E. M. Bernstein, Dietrich, Carre, DuBois, Lawler, and Timmons for the Treasury; Messrs. Acheson, Luthringer, and Miller for State; Messrs. Shea, Kreeger, Jurenev, and Rosenwald for Justice; and Mr. Knapp for the Board of Governors of the Federal Reserve System.

Reference was made to two transactions proposed by the Banque Nationale Suisse. The Swiss Minister, in a letter to Under Secretary of State Welles, has requested permission to export approximately \$10,000,000 in gold from the United States to Switzerland. It is claimed by the Swiss Government that the National Bank is required by law to maintain in Switzerland a gold coverage of 40% of the paper money in circulation. In addition it is stated that the Bank must provide gold for use in domestic industries. It is claimed that the gold coverage is now less than the required 40% and that Switzerland must repatriate gold to cover this shortage. While the first proposed shipment would amount to only \$10,000,000, two other shipments of \$10,000,000 each are contemplated. Further, a pending application seeks to transfer approximately \$11,500,000 in gold to Portugal under earmark in the United States. Recently this application was discussed with Mr. B. Bernstein by Mr. Feer of the Swiss Legation, who said that Mr. Bernstein had suggested this procedure in connection with a previous application which the Swiss had filed to ship \$2,000,000 in gold from Switzerland to Portugal. Mr. Bernstein indicated that he had at no time suggested this procedure but had merely asked why Portugal was not willing to take gold under earmark, but rather preferred to have the gold shipped to Portugal. Mr. Dietrich also referred to a cable received from Ambassador Caffery in Brazil stating that the Central Banks of Portugal and Switzerland were planning to ship gold to Brazil. Mr. Pehle pointed out that the Swiss reluctance to accept dollars in New York against Swiss franc payments in third countries, notably Germany and Italy, should be somewhat relieved by the recent amendment to General License No. 32, which prohibits payments to blocked countries through third countries. Mr. Pehle also

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stated that another application is pending to ship \$100,000 in gold held under earmark with the Federal Reserve Bank of New York for the account of the Central Reserve Bank of Peru to Buenos Aires, to be held there under earmark for Swiss account. Mr. B. Bernstein suggested that the Swiss Minister be called in for a frank discussion of these recent maneuvers on the part of Switzerland with respect to her assets in this country. It could be pointed out to the Swiss Minister that the future of an independent Switzerland is linked to the policy of this Government and that all suspicious financial transactions should be strictly avoided. Mr. Acheson stated that he had talked to Under Secretary Welles on the Swiss gold question. Mr. Welles had agreed that shipment of gold out of the country was definitely out of the question, but had inquired as to whether Switzerland could be permitted to transfer gold under earmark to Portugal. Mr. Acheson had told Mr. Welles that this was a somewhat different question. Mr. Pehle stated that it was the present feeling of the Treasury Department that the application to transfer gold to Portugal should be denied, for upon receipt of gold under earmark Portugal could proceed to release gold held in Portugal to Switzerland. It was agreed that Mr. E. M. Bernstein of the Division of Monetary Research would prepare a memorandum discussing the three pending applications and the considerations involved therein.

Mr. Acheson said that Mr. Iguchi had recently stated to him that the fares paid by the Japanese returning to Japan would be deposited in the blocked account of the Japanese Consul General in San Francisco. Such funds could be used to defray expenses in connection with the fueling and provisioning of the "Tatuta Maru", and any surplus could be used to cover Japanese diplomatic expenses in the United States when an agreement is arrived at. Mr. Acheson said he also expected to be able to arrange for \$70,000 owing to Japan from the United States under a fur seal treaty to be deposited to Japanese account in this country. Mr. Iguchi also raised with Mr. Acheson the question of past expenses for Japanese diplomatic and consular personnel in this country. Mr. Pehle suggested that it would be helpful if Mr. Iguchi would submit in a single statement all of the past expenses the Japanese Embassy desires to cover by the release of blocked funds.

Mr. Pehle referred to a report received by the Bureau of Customs to the effect that several Japanese desiring to board the "Tatuta Maru" were in possession of excessive amounts of food supplies.

The Committee agreed that Customs should be informed that passengers of the Japanese vessel should be allowed to take with them only reasonable amounts.

Mr. Foley reported that Mr. Nishiyama had recently called upon him and had inquired as to the status of the oil question. Mr. Nishiyama had pointed out that if the two tankers now on the West Coast return to Japan empty it will create a very bad impression. Mr. Foley told Mr. Nishiyama that the question of the use of South American funds to purchase the oil was still under consideration by this Committee.

Mr. Bernstein referred to State Department despatches indicating that Japanese boats have been bringing cargoes of gold to Peru and Argentina and inquired how such boats were being fueled. If American oil companies or other Latin American subsidiaries are supplying fuel to such vessels, the situation could be controlled by ruling that such companies cannot supply oil to any blocked country or person acting on behalf thereof, except pursuant to license. Once this action is made known to the Japanese, they would in all probability hesitate to send any more boats into Western Hemisphere waters. Mr. Acheson stated that the British had approached the State Department on this question sometime ago, but that Secretary Hull was not then willing to take action. Mr. Acheson suggested to Mr. Bernstein that they examine information received by the State Department as to the number of Japanese vessels that have visited the Western Hemisphere in recent months and that if the problem seemed to warrant action, Secretary Hull could again be approached on the matter. Mr. Bernstein pointed out that there are two breaches in our control, the "Lati" Airline and the Japanese vessels, and that the Standard Oil Company has already been informed that no further sales of fuel to "Lati" or "Condor" may be effected except under license.

Mr. Pehle discussed with the Committee approximately 250 applications involving remittances to Portugal and Switzerland for the purchase of food packages to be sent into occupied countries. Mr. Pehle said that a large number of these applications have been held up for over four months and that we have experienced very little pressure to secure their approval. The Treasury recommended denial of these applications on the ground that dollars should not be used to finance the movement of food between neutral countries and occupied countries; and it was pointed out that if individuals are allowed to send food packages into invaded areas, such a practice may be used as a wedge for

American relief work behind the British blockade, or an attempt to break the blockade with food shipments from the United States. Several of the firms engaged in this business in the United States are frankly German in composition and sympathy; others are firms of dubious reputation. Mr. Bernstein pointed out the denial of these applications was a logical corollary of our recent action in amending General License No. 32 so as to prohibit the Axis countries from realizing free dollars or other valuable foreign exchange. It was agreed that such applications should be denied.

Mr. Pehle also referred to a group of applications involving the German Standstill Agreement. There is presently pending an application to pay \$1,300,000 to various American banks out of blocked German accounts as interest on the Standstill obligations. This application has previously been denied by this Committee. It was agreed that this action should be reaffirmed. Another group of applications involves the calling up by Standstill creditor banks of registered marks; a procedure which enables American creditor banks to convert the part of the Standstill credits they hold. The Committee agreed that such applications should be approved, provided that such marks are licensed only for sale for use in effecting remittances to Germany where otherwise free dollars would be credited, as under General License No. 33, General License No. 72, and specific licenses containing similar provisions.

Reference was made to a group of applications to pay interest on German dollar obligations. It was agreed that in the case of banks whose coupon dates or maturities were before June 14, 1941, and for whose payment funds have been set aside in the hands of the respective paying agents, we would allow interest and principal to be paid in such cases. With respect to all applications to effect payments of interest and principal on German bonds falling due after June 14, 1941, it was agreed that such applications should be denied.

TREASURY DEPARTMENT

INTER-OFFICE COMMUNICATION

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DATE OCT 31 1941

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

Re your memorandum of October 30 concerning the Quakers buying milk in Switzerland.

Walter Stewart has not as yet spoken to me about the matter. Attached is a memorandum prepared in Foreign Funds Control showing applications to transfer French funds to the Quakers to buy food supplies in Switzerland and Portugal for shipment to France.

You correctly recalled that at the beginning of 1941, you authorized the transfer of \$50,000 of French funds to the Quakers to buy Swiss milk. Towards the end of February the Quakers told you that they had not as yet been able to buy the milk. We were advised from time to time that the Quakers were able in April and May to export in small amounts the \$50,000 worth of milk from Switzerland to France.

In March and April of this year, the Quakers again asked that French funds be released to purchase food in Portugal and Switzerland to be shipped to France and after taking up the matter with the State Department, we did not grant the licenses. On October 15, we denied the most recent application by the French to transfer \$200,000 to the Quakers for the purchase of Swiss milk. This was done after clearance with the State Department and in line with the policy followed with respect to other countries.

E. H. Fh

October 30, 1941.

Applications to transfer funds from the French Government to the American Friends Service Committee for the purchase of food supplies in Switzerland and Portugal for shipment to France.

(1) Application No. NY 84497 filed by the French Government to transfer \$50,000 to the American Friends Service Committee for the purchase of Swiss milk was raised by Mr. Pehle with Secretary Morgenthau at the 9:30 meeting on December 13, 1940. It later developed that the Friends Service Committee had considerable difficulty in securing export permits from the Swiss Government for the milk purchased. The French Government approached the Treasury Department on the question of further release of funds. This matter was discussed with Secretary Morgenthau by Mr. Pehle at the 9:30 meeting on January 10, 1941. The Secretary indicated that no action should be taken on the release of further French funds until the milk already purchased in Switzerland had been sent to France. It was also indicated that before the approval of any further release of French funds, we should ascertain the attitude of the Department of State, and also check with the French as to whether they have any amounts of Swiss francs available.

(2) On February 26, 1941, Secretary Morgenthau saw Mr. Clarence E. Pickett and Mr. John P. Rich of the American Friends Service Committee. Mrs. Klots and Mr. Pehle were present. Secretary Morgenthau referred to the fact that the Friends Service Committee had not been able to obtain much of the milk purchased in Switzerland, which fact was confirmed by Mr. Pickett. At that time Secretary Morgenthau indicated that the release of further funds for the purchase of milk in Switzerland would have to be taken up with Secretary Hull and that before the Treasury Department would be in a position to discuss the matter further he would have to have a letter from Secretary Hull indicating that the State Department wanted the Friends to work in the occupied areas.

(3) Another application, NY 103767, was filed by the French Government to transfer \$50,000 from the French account to the American Friends Service Committee. On March 11, 1941, the Committee requested the Treasury Department to allow this release of funds, which they indicated would be sent to Portugal for the purchase of food stuffs and clothing to be sent to France. This application was referred to the Department of State by letter on March 21, 1941, and the State Department replied as follows:

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"Inasmuch as the French Government has available in Portugal deposits amounting to a minimum of \$600,000 and inasmuch as the French Purchasing Commission is at present in Lisbon endeavoring to raise transportation of supplies to France, the Friends Service Committee has been informed that they should, in the first instance, communicate with this Commission to determine whether it would be possible to make use of its facilities in connection with the purchase of these supplies. It is further understood from the British Embassy that the British authorities are reluctant to grant navicerts if these supplies are to be purchased from blocked accounts in this country as long as ample funds exist in Portugal for this purpose. Under these circumstances, this Department is not at the present time prepared to recommend this transfer."

This letter was signed by Under Secretary Welles. Accordingly, application No. NY 103767 was denied. It was brought to the attention of Secretary Morgenthau by a memorandum from Mr. Pehle dated April 11, 1941.

(4) On April 14, 1941, the American Friends Service Committee requested by letter that the dollar equivalent of 1,792,650 Swiss francs (approximately \$417,000) be released from French funds to purchase food in Switzerland for shipment to France. The Treasury Department referred this request to the Department of State on April 22, 1941, stating:

"This transaction is being referred to you in view of the important foreign policy considerations involved therein. Should an application be filed to transfer the above-mentioned amount from French Government funds to the American Friends Service Committee, this Department is not prepared to approve such application unless requested to do so by your Department."

The State Department replied in a letter from Under Secretary Welles dated April 30, 1941, stating:

"The American Friends Service Committee, which has also communicated with this Department in this matter, has been informed that the situation has developed in such a way that this Government must recommend that the distribution of supplies in the unoccupied areas of France be undertaken through cooperation with the American Red Cross which has obtained funds from the American Government to supply milk to French children and that this Department is not in a position to recommend the unblocking of funds as requested by the American Friends Service Committee."

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(5) A letter was received from the State Department dated May 20, 1941, stating that it had been ascertained from the American Ambassador at Vichy that approximately 60 tons of milk had already been purchased by the American Friends Service Committee in Switzerland and had arrived at Marseille. The State Department stated that it perceived no objection to the release of funds in payment of this specific amount of milk provided that distribution was coordinated with the American Red Cross efforts. This coordination was arranged between the Friends and the Red Cross.

(6) A further application, NY 266162, was filed by the French Government to transfer \$200,000 to the Friends Service Committee for the purchase of Swiss milk. This application was discussed by the Treasury Department with Assistant Secretary of State Dean Acheson. It was agreed that the application should be denied in view of the general policy being followed by the Interdepartmental Foreign Funds Control Committee in similar cases. Applications have been filed to transfer funds to Sweden for the purchase of foods to be sent to Norway, and the transfer of funds to Switzerland for food to be sent to Greece and Belgium. The Committee has unanimously agreed that all such applications should be denied.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

281

DATE October 31, 1941.

TO Mr. White

FROM Mr. Friedman

SUBJECT: Exports from the Port of Manila, Philippine Islands, to China, Hong Kong, Burma, Japan and Russia for the two weeks ending October 23, 1941.

1. Exports to China from the Port of Manila, Philippine Islands, during the two weeks ending October 23, 1941, amounted to \$60,000, of which practically all went to Occupied China. (See Appendices A, B and C.)
2. Exports to Hong Kong during the two weeks under review exceeded exports to any of the other countries discussed, amounting to \$186,000. Cement, salt and rayon and cotton textiles and manufactures were the principal items shipped. (See Appendix D.)
3. Exports to Burma were valued at only \$11,000, consisting of rubber manufactures and automobiles. (See Appendix E.)
4. No exports to Japan were recorded. However, much of the exports to Occupied China may be ultimately destined for Japanese use and even some of the goods shipped to Hong Kong may be obtained finally by the Japanese via Shanghai.
5. No exports to Russia were recorded.

Appendix A.

Total Exports from the Port of Manila, Philippine Islands, to Russia
Japan, Free and Occupied China, Hong Kong and Burma for the
period September 19, 1941 - October 23, 1941

(in thousands of dollars)

	Russia	Japan	Total	China		Hong Kong	Burma
				Free China	Occupied China		
Sept. 19 - Sept. 25	--	--	6 1/2			34	1
Sept. 26 - Oct. 2	60	--	7 1/2			23	10
Oct. 3 - Oct. 9	--	--	113 1/2			48*	--
Oct. 10 - Oct. 16	--	--	59	--	59	70	--
Oct. 17 - Oct. 23	--	--	1	1	--	116	11
Total	60	--	186			291	22

1/2 Figures for these weeks were not broken down as to Free and Occupied China.

* This figure listed in radiogram as \$418,000, presumably a typographical error.

Treasury Department, Division of Monetary Research

October 30, 1941.

282

Exports from the Port of Manila, Philippine Islands,
to Free China for the period October 10 - October 23,
1941.

(in thousands)

Total Exports	\$ 1
Principal Items	
Automobile and parts	1

Treasury Department, Division of Monetary Research Oct. 30, 1941

Exports from the Port of Manila, Philippine Islands to
Occupied China, for the period October 10 - October 23,
1941

(in thousands)

Total Exports	\$ 59
Principal Items	
Sawn lumber	51
Woolen suiting	3
Machinery and parts	3
Otegraphic and motion picture films and materials	1

Treasury Department, Division of Monetary Research Oct. 30, 1941.

APPENDIX D.

285

Exports from the Port of Manila, Philippine Islands to
Hong Kong for the period October 10 - October 23, 1941.

(in thousands)

Total Exports	\$ 186
Principal Items	
Rizal cement	66
Common sea salt	45
Rayon and cotton textiles and manu- factures	32
Fibers and manufactures	13
Chemical products dyestuffs	9
Sawn lumber	6
Electrical appliances, parts and accessories	6
Machinery, apparatus, parts and accessories	3
Iron and steel manufactures	2
Automobile engines	1
Alimentary substances	1
Automobile	1

Treasury Department, Division of Monetary Research Oct. 30, 1941.

Exports from the Port of Manila, Philippine Islands
to Burma for the period October 10 - October 23, 1941.

(in thousands)

Total Exports	\$ 11
Principal Items	
Rubber manufactures, tires and tubes	8
Automobiles	3

Treasury Department, Division of Monetary Research Oct. 30, 1941.

October 31, 1941.

287

*... about progress to ...
... 11/10 & would be done ...*

TO: HAROLD E. GRAVES

SUBJECT: PROGRESS REPORT FROM DEFENSE SAVINGS STAFF

SALE OF BONDS

Actual cash receipts from the sale of Series E, F, and G Bonds from October 1st through October 29th were \$250,842,000, which is an increase of 8 per cent over the same period in September. Sales from September 1st through September 29th were \$222,683,000. Sales from August 1st through August 29th were \$255,822,000.

SALE OF SERIES E AND D BONDS

Sale of Series E Bonds to date shows a decided recent increase over the sale of Series D Bond in the corresponding period of 1940. (See graph attached.)

DIRECT MAIL

In 47 days of pulling the industrial mailing has brought sales of \$2,689,314. In 37 days of pulling the customer mailing brought sales of \$2,416,990. Though the latter mailing is beginning to taper off, it is still drawing about \$70,000 daily.

The following has been prepared for November mailing:

Series IV tests - 14 tests to 147,000 names;
second industrial mailing to 397,000 names offering
F and G bonds and, and special Christmas order form,

Bonds for employee bonuses and gifts; to 2,000,000 prospects of over \$5,000 income, offering E, F and G Bonds; customer mailing to 600,000 names which have become available since the first customer mailing.

TOLEDO DEFENSE DAY

Toledo, Ohio will stage an elaborate Defense Day Celebration on Tuesday, November 4, and arrangements have been made for the participation of the Army, Navy and Coast Guard.

EXHIBITS

Arrangements have been made for a Defense Savings Booth at the Arizona State Fair in Phoenix November 8th, with the Army and Navy participating. There will be a Defense Savings Booth in the Automobile and Home Defense Show, Denver, Colorado, November 3 to 8. Treasury Houses will be opened in Los Angeles and Oklahoma City about December 1st, and in San Francisco December 15th. After running thirty days, each of these stations will be moved to other locations.

TREASURY BOOTHS

Through October 29th the following amount of Defense Bonds and Stamps and Tax Notes have been sold at Washington Booths which were opened when indicated:

<u>Garfinckels</u>	10/3/41	<u>Willard Hotel</u>	10/15/41
Bonds	\$762.50	Bonds	\$112.50
Tax Notes	25.00	Tax Notes	----
Stamps	347.40	Stamps	96.40
	<u>\$1,134.90</u>		<u>\$208.90</u>
<u>Woodward & Lothrop</u>	10/6/41		
Bonds	\$5,306.25		
Tax Notes	100.00		
Stamps	1,559.40	Total Sales to Date:	
	<u>\$6,965.65</u>		\$9,770.90
<u>Lansburghs</u>	10/10/41		
Bonds	\$918.75		
Tax Notes	-----		
Stamps	542.70		
	<u>\$1,461.45</u>		

RADIO

Muzak, a wire music system which furnishes transcribed music to hotels, night clubs and restaurants in large cities, reports that a special recording of "Any Bonds Today" has been released to all subscribers.

At a meeting in the Treasury with representatives of General Foods, Proctor & Gamble, General Mills, Colgate-Palmolive-Peet Company and Lever Brothers, arrangements were made for definite routine promotion on the daytime programs of these companies.

Transcriptions of "Ballad of the Leatherneck Corps" were furnished to the Marine Corps to be sent to Shanghai, China, together with additional material to be placed on the English station in Shanghai.

Special material for labor stations, labor broadcasts,

and meetings, has been placed at the disposal of the Field Office through Mr. Hyatt.

Starting this week Rudy Vallee's Sealtest program will include Bond promotion each week. National Dairy Products Company also is using the Minute Man emblem in its publication distributed to three quarters of a million homes each month.

Amos 'n' Andy are working out a complete set of programs for December promoting the giving of Bonds and Stamps for Christmas.

Special labels to be carried on all transcriptions have been prepared. (Copies attached).

PRESS

Cooperation in preparation of posters and other promotion has been extended to the Washington Star in connection with the newspaper's winter bowling tournament, for which prizes are to be Bonds and Stamps. The first prize will be \$1,000. Last season 17,000 bowlers participated in the tournament.

A series of three editorials on the Defense Savings Program has been distributed to the labor press, together with a release, and a letter explaining the special information service set up for these publications. Returns show that the Negro newspapers are using material regularly. A new set of mats of the Minute Man emblem in various sizes for replacement of the stereotypes used widely by newspapers, and suggestions for additional uses, has been sent to all daily and weekly papers.

Figures by States on Bond sales and Stamps sales for five

months were released.

FIELD OFFICE

During the past week the following Deputy State Administrators were in the office for conferences: Wilkerson, Arizona; Churchill, Idaho; Swayzee, Mississippi; Shackelford, Missouri; Miles, North Carolina; Quinn, Ohio; Parks and Adams, New York. Several other administrators and deputies are scheduled to be in Washington next Monday.

Nine field representatives are now on active duty in the field.

Virginia had its initial State Committee meeting on Thursday, October 30th. All but eight of the forty members were present. Governor Price, State Chairman Gaines, Mr. Graves, and Mr. Blyth spoke.

National status of State organizations is shown by the accompanying map.

October 31, 1941.

212

TO: HAROLD N. GRAVES

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Treasury Department
DEFENSE SAVINGS STAFF
RADIO RECORDING
E.T. ANNOUNCEMENTS INCLUDED

START OUTSIDE
33 $\frac{1}{3}$ R.P.M.

USE STYLUS PRESSURE
NOT IN EXCESS OF 2 OZ.

THIS RECORDING CONTAINS ONLY MUSIC AND OTHER COPYRIGHTED MATERIAL THAT MAY BE PERFORMED IN THE U.S. WITHOUT ANY FURTHER LICENSE.



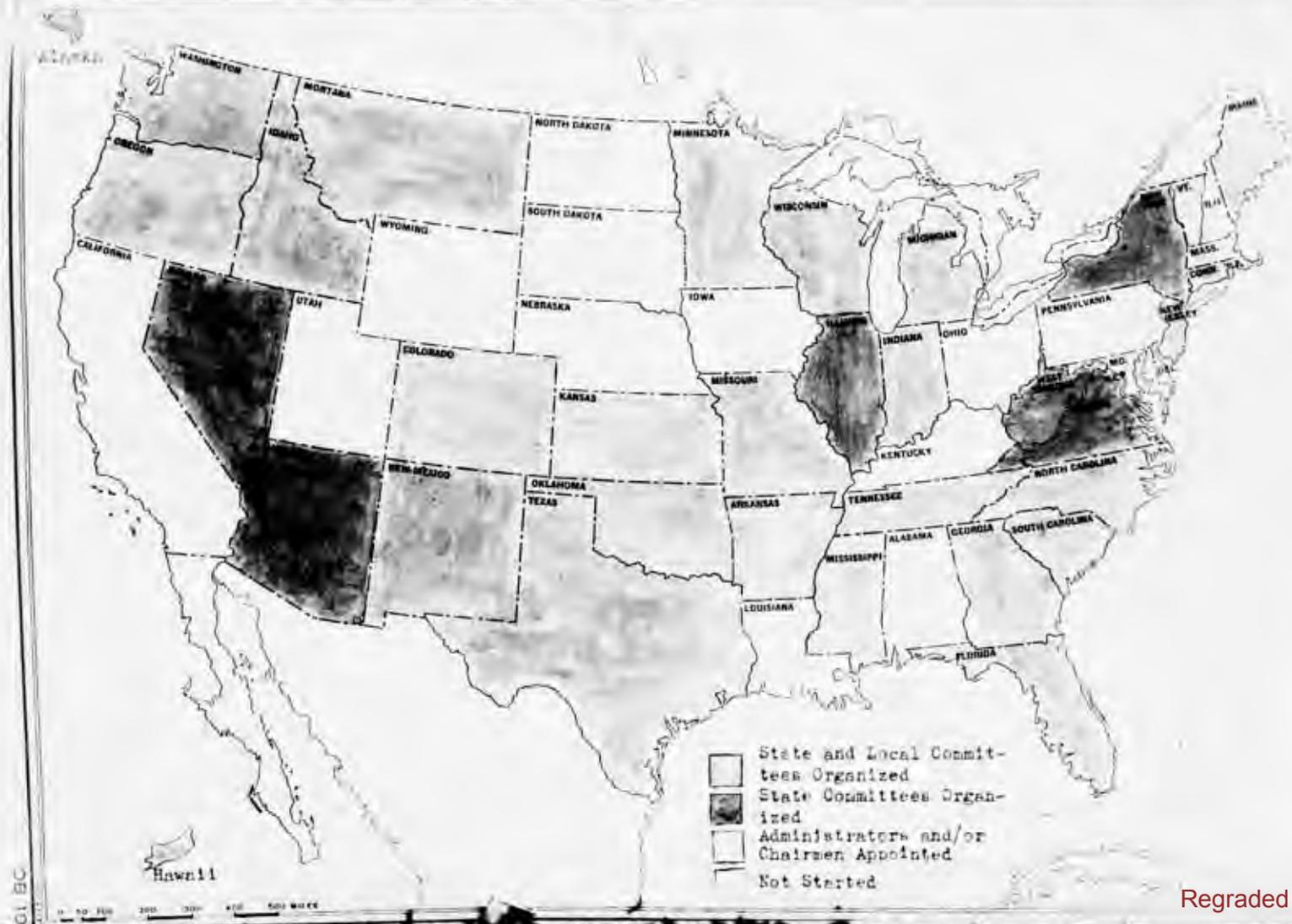
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As of October 24, 1941



SALES OF "E" BONDS 1941 COMPARED WITH SALES OF "D" BONDS FOR SAME PERIOD 1940

Millions
of
Dollars

75
70
65
60
55
50
45
40
35
30
25
20
15
10
5

SERIES E

SERIES D

SERIES E	May 2-3	5-10	12-17	19-24	26-31	2-7 (June)	9-14	16-21	23-28	30-5 (July)	7-12	14-19	21-26	28-2 (Aug)	4-9	11-16	18-23	25-30	1-6 (Sept.)	8-13	15-20	22-27	29-4 (Oct.)	6-11	13-18	20-25
SERIES D	May 3-4	6-11	13-18	20-25	29-1	3-8	10-15	17-22	24-29	1-6	8-13	15-20	22-27	29-3	5-10	12-17	19-24	26-31	2-7	9-14	16-21	21-28	30-5	7-12	14-18	21-25

SALES OF "E" BONDS 1941 COMPARED WITH SALES OF "D" BONDS FOR SAME PERIOD 1940

Millions of Dollars

75
70
65
60
55
50
45
40
35
30
25
20
15
10
5

Series E May 2-3 5-10 12-17 19-24 26-31 2-7 (June) 9-14 16-21 23-28 30-5 (July) 7-12 14-19 21-26 28-2 (Aug) 4-9 11-16 18-23 25-30 1-6 (Sept.) 8-13 15-20 22-27 29-4 (Oct) 6-11 13-18 20-25
Series D May 3-4 6-11 13-18 20-25 29-1 3-8 10-15 17-22 24-29 1-6 8-13 15-20 22-27 29-3 5-10 12-17 19-24 26-31 2-7 9-14 16-21 21-28 30-5

SERIES E

SERIES D

TREASURY DEPARTMENT

299

INTER OFFICE COMMUNICATION

DATE October 31, 1941

TO Secretary Morgenthau
FROM Mr. Thompson

With reference to the mail survey, I am having this done by W. Harold Lane of Mr. Ireys's staff. Mr. Lane is an experienced office procedure man, who assisted Harold Graves in some of his investigations, including that of the Personnel Division. He has made a preliminary review of the mail situation, and he reports to me that in the aggregate the mail of the Secretary's Office is handled efficiently, but that in recent months it appears that the volume has become so great, exceeding 2,000 separate pieces per week in the Secretary's Office, that delays have occurred, for the most part in the newly organized units of the Treasury.

I am convinced that there is room for improvement in our mail handling operations and have on occasion brought to the attention of bureau heads irregularities typical of which will be noted from the attached memorandum to Mr. Pehle and his reply to me. Irregularities such as these do not arise in your immediate office as a general rule, but are apt to arise in the Foreign Funds Unit, the Defense Savings Staff, and in other less sizable units where mail is concentrated in volume, and here it develops that complaints are negligible in comparison with the volume of mail handled.

Secretary Morgenthau - 2

In order to answer specifically the request which you made of me that I run through five or six sample cases of letters received addressed to you to see if they were properly handled, I asked Mrs. Forbush to give me a list of some thirty cases picked at random and had Mr. Lane, also picking at random, run through some of these cases, the results of which are indicated on the attached sheets.

It is evident that there are delays in handling some cases and that it would be desirable where a complete reply cannot be made due to the lack of readily available subject matter to so advise the correspondent.

It has also been noted in the course of this review that, due to the pressure of defense and emergency activity, existing instructions requiring the prompt acknowledgment of letters, followed by prompt and adequate replies, are not being observed as fully as would be the case in normal times. To meet this situation arrangements are being made to have a more forceful circular of instructions on the subject prepared and issued, and appropriate follow-up controls maintained.

For

TREASURY DEPARTMENT

301

INTER OFFICE COMMUNICATION

DATE October 10, 1941

TO Mr. Pehle
FROM Mr. Thompson

There have been received in the Office of the Secretary letters complaining about delays occurring with respect to appropriate replies to letters written in connection with Foreign Funds transactions. This office appreciates fully the mammoth job that is being accomplished by the staff under your supervision at the Park Road offices and is convinced that these delays are justifiable. On the other hand, it is felt that something should be done to hold to a minimum, if not eliminate entirely, letters criticizing such delays, particularly from members of Congress.

In this connection might I suggest that all mail coming into the Foreign Funds Unit, whether coming direct or referred thereto by this or any of the other offices of the Secretary, be recorded at one central desk, properly assigned, and a system of follow-up check maintained so that too long a period might not elapse before final reply is made. Oftentimes, a pending case will take two or three months before appropriate reply can be made. In such cases a letter to the person making the inquiry stating that the matter is being given consideration and reply will be made in the very near future keeps the correspondent satisfied temporarily at least, for he feels that his letter has not been mislaid or indefinitely pigeonholed.

Designating some person at a central desk to follow up on all correspondence would unquestionably serve to expedite inquiries both from your office and from the offices in the Main Treasury Building. As matters now stand, this office generally calls Mr. Evans' office to find out who is handling a particular transaction. When this information has been developed, we are then put in the position of having to call direct your staff man to obtain from him some light on the particular inquiry, whereas it would be far more simple if we were to call a central desk which would be charged with the responsibility of getting back to us an answer to our inquiry.

Typical of this kind of situation is the attached letter dated October 3, 1941, from Congressman James J. Hefferman, concerning gift food packages, which matter was before your unit last summer and a reply prepared there for my signature on August 14, 1941. In tracing this inquiry it developed that Mr. Timmons was handling this case. I called Mr. Timmons' office on this matter yesterday and found that he was in conference. I left word with Miss Heller to have him call me as soon as he returned to his desk, but did not receive a return call from him until

Mr. Pehle - 2

this morning. Meanwhile a call came in from the Congressman to inquire as to his next move, and I hesitated to refer him to Mr. Timmons until I had been assured that he was handling the case.

In view of the Secretary's interest in having correspondence promptly handled, I believe that it would be to our mutual interest to consider any plan that will assure the elimination of complaint letters.

TREASURY DEPARTMENT

303

INTER OFFICE COMMUNICATION

DATE October 14, 1941

TO Mr. Thompson
FROM Mr. J. W. Pehle

I have received your memorandum of October 10, 1941, relative to the handling of correspondence of the Foreign Funds Control.

All correspondence received by the Control is recorded in the Correspondence Unit. I suggest that all routine inquiries as to the status of letters be directed to Mrs. Andrews, who is chief of such unit, and that inquiries concerning Congressional mail and other important letters should be directed to Mr. Timmons. We fully realize the necessity of handling Congressional mail as promptly as possible; in this connection there is attached a copy of the report of pending Congressional mail for Monday, October 13, 1941. You will note that all but one of our pending letters are awaiting signature, and the remaining letter has been acknowledged and will receive a further answer when the difficult policy question to which it relates has been resolved. We are making every effort to reply to every letter received by the Foreign Funds Control as promptly as possible, and in those cases in which replies cannot be made immediately, a prompt acknowledgment is given.



FOREIGN FUNDS CONTROL Section

REPORT ON CONGRESSIONAL MAIL FOR PERIOD October 6 to October 13, 1941.

Subject	From	Date of Letter	Received	Acknowledged	Date of final reply and by whom signed	Reason for Delay (If in office more than 24 hours)
Food packages	L.W.Hall, M.C.	8-9-41	8-12-41	8-12-41	10-9	await. signature
" "	E.J.Keogh, M.C.	8-11-41	8-13-41	8-18-41	10-9	" "
" "	J.J.Heffernan	8-12-41	8-14-41	8-14-41	10-9	" "
" "	L. Lewis, M.C.	8-20-41	8-20-41	8-28-41	10-10	" "
Far East trade	A.G.Klein, M.C.	by telephone		8-26-41	10-13	E.H.Foley
NY 168192	Sol Bloom, M.C.	8-23-41	8-27-41	9-2-41	- - - - -	- policy decision
Sile sian	J.A.Danaher	8-27-41	8-29-41	9-8-41	10-10	E.H.Foley
NY 227732	Sol Bloom, M.C.	9-2-41	9-3-41	9-8-41	10-11	await. signature
Tulsa Coffee	W.E.Disney, M.C.	9-8-41	9-9-41	9-11-41		" "
operating lic.	E.C.Michener, M.C.	9-10	9-11-41		9-13	by telephone
SL 737	J.J.Cochran, M.C.	9-11	9-12-41		10-13	E.H.Foley
NY 153356	L.W.Hall, M.C.	9-15	9-18-41		10-4	E.H.Foley
NY 200808	C.L.McNary	9-17	9-19-41		10-13	await. signature
reg. property	R.M.LaPollett	9-23	9-24-41		9-29	direct to constituent
Estate	J.J.Cochran, M.C.	10-2	10-4-41	10-7-41	10-14	E.H.Foley
Fees in Calif.	L.M.Ford, M.C.	9-26	9-29-41	9-30-41	10-10	E.H.Foley
NY 88904	A.P.Beiter, M.C.	10-1	10-2-41		10-10	E.H.Foley
Sile sian	F.Maloney	9-30	10-3-41	10-4-41	10-10	E.H.Foley
S.Nakahara	L.E.Geyer, M.C.	9-30	10-3-41	10-4	10-13	E.H.Foley
Est.C.Clark	J.J.Cochran, M.C.	10-2	10-4-41	10-4	10-13	E.H.Foley
inheritance	S.Downey	10-3	10-6-41		10-13	E.H.Foley
ben. of will	O.Canfield, M.C.	10-4	10-6-41	10-9	10-9	E.H.Foley
Super. Pow. Corp.	G.W.Gillette	10-6	10-8-41	10-8	10-10	E.H.Foley
cases of china	C.W.Brooks	10-6	10-9-41	10-11		await sig. 10-13
Clev. 1988	Virgil Chapman, M.C.	10-4	10-6-41	10-7	10-11	E.H.Foley

MOVEMENT OF CORRESPONDENCE ADDRESSED TO
SECRETARY MORGENTHAU

Letter from Congressman Charles H. Leavy.

Subject: German Government Bonds.

Date of letter:	August 18, 1941
Received in Treasury Correspondence Division on:	August 19, 1941
Referred by Treasury Correspondence Division to Mr. Parker, Foreign Funds Control, on:	August 19, 1941 9:25 a.m.
Received by Foreign Funds Control on: (No record on letter or in file showing when letter was received).	
Final reply dictated by Mr. Glenn, Foreign Funds Control, on:	August 22, 1941
Final reply signed by Acting Secretary Foley on:	August 26, 1941

Comment:

The total elapsed time from the date this letter was received in the Treasury Department until the reply was seven days. Three days of this time the letter was in the Foreign Funds Control, during which time it received the attention of Mr. O'Flaherty and Mr. Glenn. There is no record of any acknowledgement being sent to the Congressman informing him that there would be a delay in sending him a final reply. It seems that this could have been done. The final reply appears to be adequate.

MOVEMENT OF CORRESPONDENCE ADDRESSED TO
SECRETARY MORGENTHAU

Letter from Senator John A. Danaher.

Subject matter: Foreign Funds Control license for the Silesian-American Corporation.

Date of letter:	August 27, 1941	
Received in Treasury Correspondence Division	August 28, 1941	9:48 a.m.
Referred by Treasury Correspondence Division to Foreign Funds Control on:	August 28, 1941	11:00 a.m.
Received by Foreign Funds Control on:	August 29, 1941	1:34 p.m.
Acknowledgement dictated by Mr. Timmons, Foreign Funds Control on:	September 4, 1941	
Acknowledgement signed by Acting Administrative Assistant to C. R. Schoeneman on:	September 8, 1941	
Further acknowledgement dictated by Mr. Timmons on:	October 4, 1941	
Acknowledgement signed by Acting Secretary Foley on:	October 10, 1941	

Previous Correspondence:

Letter from Mr. D. A. Crawford to Vice President Wallace dated:	August 4, 1941
Received by Vice President Wallace on:	August 5, 1941
Acknowledged by Harold Young, Assistant to Vice President Wallace on:	August 30, 1941
Original letter received in Surplus Marketing Administration on: (Referred to Treasury Department)	September 4, 1941
Received in the Treasury Correspondence Division on:	October 1, 1941
Referred by Treasury Correspondence Division to Foreign Funds Control on:	

Acknowledgement dictated by J. J. Lawler, Foreign Funds Control on:	October 4, 1941
Acknowledgement signed by Acting Secretary Foley on:	October 10, 1941
<u>Other Previous Correspondence:</u>	
Letter from Senator Maloney to Acting Secretary Foley dated	August 8, 1941
Received in Treasury Correspondence Division on:	August 12, 1941 8:55 a.m.
Referred by Treasury Correspondence Division to Foreign Funds Control	August 12, 1941 10:30 a.m.
Letter time stamped (Stamp does not show who placed it on the letter, however, it is believed the record was put there by the Foreign Funds Control.. No record on the letter in the file of who received this letter in Foreign Fund Control)	August 12, 1941 2:24 p.m.
Acknowledgement dictated by Mr. Timmons, Foreign Fund Control on:	August 13, 1941
Acknowledgement signed by Administrative Assistant to the Secretary, Thompson on:	August 14, 1941
Memorandum from Mr. Timmons, Foreign Fund Control to Mr. Lawler, Foreign Funds Control on:	September 6, 1941
Letter from Senator Maloney to Administrative Assistant to the Secretary, Thompson regarding the reply of August 14, 1941, letter dated	September 30, 1941
Received in Administrative Assistant to the Secretary Thompson's office on: (Referred directly to Foreign Funds Control)	October 1, 1941
Received Foreign Funds Control	October 3, 1941

Acknowledgement dictated by Mr. Timmons
Foreign Funds Control on:

October 4, 1941

Acknowledgement signed by Acting Secretary
Foley on:

October 10, 1941

MOVEMENT OF CORRESPONDENCE ADDRESSED TO
SECRETARY MORGENTHAU

Letter from Wilma K. McFarland, Editor Child Life, Chicago, Illinois.

Subject Matter: Desired Defense Bond material that carries a message to children.

Date of letter:	September 22, 1941
Received in Treasury Correspondence Division:	September 24, 1941 9:07 a.m.
Referred by Treasury Correspondence Division to Miss Chauncey on:	September 24, 1941 10:35 a.m.
Recharged by Miss Chauncey to Assistant Secretary Graves on:	September 24, 1941
Referred by Assistant Secretary Graves to Mr. George F. Milton, Defense Savings Staff on:	September 24, 1941
(No acknowledgement of this letter was made by Mr. Graves as there had been previous correspondence)	
Received by Mr. Milton on:	No record.
(Inquiry in the mail and files room of the Defense Savings Staff disclosed there was no record there of the McFarland matter. The letter and other correspondence was finally located in a file cabinet in Mr. Milton's office. There was no record of when or by whom the McFarland letter was received in the Defense Savings Staff.)	
Final reply by Assistant Secretary Graves to Wilma K. McFarland on:	September 25, 1941
(This letter, found in Mr. Milton's file, had a notation in ink that the letter was sent by air mail by Mr. Graves on:	September 26, 1941 9:15 a.m.
Other records in the file showed the following <u>previous correspondence with Wilma K. McFarland:</u>	
Original letter from Wilma K. McFarland to P. Hartford Povel on:	August 11, 1941
(Notation in ink on the letter, "Rec'd. 8/12/41, H.P.")	
Acknowledged by Hartford Povel on:	August 19, 1941

Memorandum by Hartford Powel transmitting McFarland letter to Ferdinand Kuhn on:	August 19, 1941
Memorandum by Ferdinand Kuhn Transmitting McFarland letter to George F. Milton on:	September 3, 1941
Memorandum by Mr. Milton transmitting the McFarland letter to Mr. Kuhn on: (Notation, "O.K.")	No date
Memorandum by Mr. Kuhn transmitting the McFarland letter to Mr. Graves on:	No date
Memorandum by Mr. Graves transmitting the McFarland letter to Mr. Milton on:	September 9, 1941
Letter from Wilma K. McFarland to Hartford Powel on: (Letter bears stamp date September 13, 1941, there is nothing to show what that stamp represents)	September 3, 1941
Enclosures: Submitted herewith are copies of the following letters: Original letter from Wilma K. McFarland, August 11, 1941 Acknowledgement by Hartford Powel, August 19, 1941 Letter from Wilma K. McFarland to Mr. Powel, September 3, 1941. Letter from Wilma K. McFarland to Secretary Morgenthau, September 22, 1941. Letter from Assistant Secretary Graves to Wilma K. McFarland submitting article she desired, September 25, 1941.	

Comment:

The total elapsed time from the receipt of letter dated September 22, 1941 until its final answer to it was four days, which does not seem unreasonable considering the previous correspondence and that an article was prepared to accompany the final letter. The final reply is apparently an adequate response to Miss McFarland's inquiry. The question arises whether the central mail and files room of the Defense Savings Staff should not have a record of the McFarland matter which has been retained in the files in the office of Mr. Milton.

CHILD LIFE

536 S. Clark Street.

CHICAGO

Rec'd
8/12/41
H.P.

Office of the Editor
Miss K. McFarland

August 11, 1941

My dear Mr. Powell:

You may remember that we had some correspondence a little while ago about an article on The Treasury Department that Child Life ran late in the spring. You were pleased with the article and thought you might care to quote from it in one of the Treasury Educational leaflets.

We have been eager to help in any way that we could in the sale of Defense Stamps. I'm sure our many readers would take up the task with enthusiasm if they were properly instructed. We are working on our October issue and I am wondering whether it would be possible for us to get from Mr. Morgenthau a brief statement in regard to this whole matter, that we might feature, perhaps on an inside cover page -- the place that seems to command most immediate attention. We should want to print this in rather large type so I should think 250 or 300 words should be about the right length if the article is to be illustrated. And if you have pictures in your file that might be used as illustrations or some decorative emblem to go at the top of the page this too might be effective. Otherwise we would have a decoration drawn.

The circulation of the magazine is around 175,000, but 30,000 of the subscriptions go to schools, and a great many more than this to libraries, so we have no idea just how large our real reading public is. We have a Teachers Edition going to schools and in the Teachers Edition in connection with such an article, I would call attention to the sale of the Defense Stamps suggesting it as a school project.

I thought of the October issue for this project because by this time all the children will be back in school. But the time is rather short and if we are to have material from you it should reach us by August 25th or earlier, and we should know at once whether we may expect it.

I should be grateful therefore for an early reply to my letter.

With cordial good wishes,

Sincerely,

(signed) Wilma McFarland

Mr. Harford Powell
Information Director
Treasury Department
Washington, D. C.
WKM:AN

August 19, 1941

Dear Miss McFarland:

It was impossible to refer your letter of August 11 to the Secretary of the Treasury before he left Washington the other day. I would suggest that you consider an article by him for your November issue, and I believe it would be very helpful in spreading knowledge of Defense Stamps, in which the Secretary is very much interested at this time.

I am accordingly referring your letter to Mr. Ferdinand Kuhn, Jr., who will answer in behalf of the Secretary, on his return.

I appreciate very much your kindness in wishing to give such important space to Defense Savings Stamps.

With best wishes,

Very sincerely,

Harford Powl,
Director of Information.

Miss Wilma K. McFarland,
Editor,
Child Life Magazine
536 South Clark Street,
Chicago, Illinois

W/P/RLM

COPI

CHILD LIFE
536 S. Clark Street
CHICAGO

Office of the Editor
Wilma K. McFarland

September 3, 1941

Dear Mr. Powell:

Reporting further on my request for material on the defense savings program to be featured in Child Life:

I received a telephone call from Washington from someone to whom you evidently referred my request just before you went on vacation. He said that Mr. Morgenthau was still away but he would send me what he had in the office that might do. I do not remember his name but he said that he was leaving on vacation also. Then the material did not arrive for a week and when it came it was purely adult material--leaflets and the like. I could find nothing there that I could rewrite with the proper approach for the boys and girls who read our magazine. So I had to give up the idea for our October issue. But I'd like very much to feature this program of yours in our November issue which is now in work. Do you suppose now we could get some sort of statement from Mr. Morgenthau or some member of his staff which would start our readers working and would link up with the school program which I assume is now under way? I should be ever so grateful if you would let me hear from you at an early date so that we may save space for the material if it is coming. I hope that I am not burdening you with something entirely out of your province, but the man to whom you referred the question would not give me his name and you are the one with whom we have had the helpful contacts.

With cordial good wishes,

Sincerely,

(signed)

Wilma McFarland
Wilma K. McFarland

WKM:NS

Mr. Harford Powell
Information Director
Treasury Department
Washington, D. C.

SEP 13 1941

COPY

CHILD LIFE

314

536 S. Clark Street

CHICAGO

Office of the Editor
Lina K. McFarland

September 22, 1941

My dear Secretary Morgenthau:

I am the Editor of Child Life, a national magazine for children with a circulation of about 175,000. Recent surveys seem to indicate that the magazine is read by at least one half million children; by many teachers who use it for supplementary purposes in their schools, by librarians, and by most of the parents.

We have been very eager to help the Government in spreading information about the National Defense Stamps and Bonds. During your absence I have been in touch with two members of your staff who seem to have sent me all of the material on hand for publicity purposes. In that material I do not find one sentence that carries a message to children. There are general suggestions to teachers and I have used these in my teachers' supplement, but I had saved one of my November cover pages to devote to the National Defense Stamps. And for over six weeks I have been attempting to get some sort of material from your staff that would be directed to children and would tell them simply and clearly that your plan is for their cooperation. Last week I telegraphed your office again calling their attention to my need and have received no reply. Because you are a busy man I do not want to bother you, but I do honestly feel that a message in Child Life, particularly one signed by you, would be of value. But if it cannot bear your signature, there must be something in your files addressed to the youth of the country which we could at least quote.

As far as I can see the youngsters who read our magazine are eager and patriotic. A personal message from you would set them on their toes. This six weeks' delay on the part of your department has brought us right up against publication date. If there is available material on hand addressed to children, I should be very grateful to receive it. If there is no available material on hand, then, truly, I think there ought to be! And perhaps Child Life is just as good a place to start as your department could find. May we not have some word from you or whoever on your staff is responsible for a direct appeal to children? We only need 200 or 300 words at the most. We

are using a copy of the Minute Man and a patriotic design for decoration. I should greatly appreciate the assistance of your department in this matter and if we are to make publication date I shall need the material by air mail, special delivery.

Cordially,

(signed) Wilma K. McFarland

Mr. Henry Morgenthau
Secretary of the Treasury
Washington, D. C.
WKM:AK

C
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P
Y

September 25, 1941

Dear Miss McFarland:

Your letter of September 22, addressed to Secretary Morgenthau, has come to my attention. Your request for a brief article of not more than three hundred words, signed by him, has been complied with.

I take pleasure in enclosing the copy for it herewith.

Thank you very much for your interest in, and cooperation with, the Defense Savings Program.

Sincerely,

(signed) Harold N. Graves

Harold N. Graves
Assistant to the Secretary

Miss Wilma K. McFarland,
Editor, "Child Life",
536 South Clark Street,
Chicago, Illinois

Sent airmail from Mr. Graves office 9/26 - 9:15 A. M.

COPY

MOVEMENT OF CORRESPONDENCE ADDRESSED TO
SECRETARY MORGENTHAU

Letter from Congressman George D. O'Brien.

Subject: Release of frozen funds for stipend-massés.

Date of letter:	August 18, 1941
Received in Treasury Correspondence Division on: (This letter was sent direct to Mr. A. F. Peden, Foreign Funds Control, and did not go to the Treasury Correspondence Division).	Not received
Received in Foreign Funds Control on: (No record on letter or in file showing when received. Records in Treasury Correspondence Division show this letter was received by Foreign Funds Control on August 20, 1941).	
Final reply dictated by Mr. H. W. Glenn on:	August 21, 1941
Referred by Mr. Luxford, Foreign Funds Control, to Mr. Timmons, Foreign Funds Control, on: (No record on letter or in file showing how or when Mr. Luxford acquired the letter).	August 27, 1941
Acknowledgement dictated by Mr. Timmons on:	September 2, 1941
Acknowledgement signed by Acting Administrative Assistant to the Secretary, C. H. Schoeneman on:	September 8, 1941
Foreign Funds Control office memorandum from Mr. Luxford to Mr. Timmons on:	September 24, 1941
Final reply signed by Acting Secretary Foley on:	October 2, 1941.

Comment:

The lapse of time between the date this letter was received in the Foreign Funds Control and the date it was answered was one month and twelve days. The lapse of time from the date the letter was received until it was acknowledged was thirteen days. It would seem that the letter should have been acknowledged sooner. Apparently after final reply was dictated by Mr. Glenn it was referred to several officials in the Foreign Funds Control, which was no doubt necessitated by the decision to be made as a result of this letter. It is believed that the delay was due to inadequate and unsatisfactory information.

MOVEMENT OF CORRESPONDENCE ADDRESSED TO
SECRETARY MORGENTHAU

Letter from Charles L. Jackman, President, Capital Fire Insurance Company, Concord, New Hampshire.

Subject: Previous Internal Revenue claim and bond matter.

Date of letter:	September 2, 1941
Received in Treasury Correspondence Division:	September 4, 1941
Referred by Treasury Correspondence Division to Assistant Secretary Sullivan on:	September 4, 1941 3:45 p.m.
Received by Assistant Secretary Sullivan on:	
Referred by Assistant Secretary Sullivan to Mr. Broughton on:	
Returned by Mr. Broughton to Assistant Secretary Sullivan on:	
Final reply relative to the bond matter by Assistant Secretary Sullivan on: (Evidently to a prior communication which also answered the inquiry in this letter)	September 2, 1941
Referred by Assistant Secretary Sullivan to Mr. Helvering relative to tax claim on:	
Received by Mr. Helvering on:	September 8, 1941
Referred by Mr. Helvering to Mr. George Schoeneman, Accounts and Collections Unit on:	September 8, 1941
Final draft of reply dictated by Mr. A. B. Niess, Unemployment Tax Section, Accounts and Collections Unit, dated September 22, 1941, received by the Internal Revenue Bureau Correspondence Control Section on:	September 20, 1941
Referred by the Bureau Correspondence Control Section to Commissioner Helvering on:	September 20, 1941 (Saturday)
Returned by Commissioner Helvering to the Bureau Correspondence Control Section on:	September 23, 1941
Sent by Bureau Correspondence Control Section to General Counsel Foley on:	September 23, 1941

Received by General Counsel Foley on:

Sent by General Counsel Foley to Assistant Secretary Gaston on:

Received by Assistant Secretary Gaston on:

Signed by Assistant Secretary Gaston on: September 26, 1941

Returned by Assistant Secretary Gaston to Internal Revenue Bureau (to whom? on:

Received by Bureau Correspondence Control Section on: September 27, 1941

Sent by Bureau Correspondence Control Section to Unemployment Tax Section, Accounts and Collections Unit, 1331 U. St., NW, on: September 27, 1941

Final reply to Mr. Jacinman's letter mailed on:

Comment:

The total elapsed time from receipt of letter in the Treasury Department until answered was twenty-three days. During this period the letter was in Assistant Secretary Sullivan's office four days where it apparently was referred to Mr. Broughton. The letter was in the Accounts and Collections Unit of the Bureau of Internal Revenue for twelve days where the draft for final reply was prepared. From the time the final draft was prepared until the answer was mailed, seventeen days elapsed, two of which were Saturday and Sunday. The final reply seems an adequate answer and probably involved considerable research.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

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DATE October 31, 1941

TO Ferdinand Kuhn, Jr.

FROM Alan Barth

EDITORIAL OPINION
ON FOREIGN AFFAIRS:
THE CHANGING ATMOSPHERE

Emphasis

The press showed a tendency to interpret the President's Navy Day address as a defiance of John L. Lewis, rather than as a defiance of Adolf Hitler. Indeed, The Cleveland Plain Dealer, one of the country's most vigorously interventionist newspapers, concluded a long editorial titled "Enemies Abroad, And At Home" with the observation: "Mr. President, your immediate task is not that of defeating Adolf Hitler but of putting John L. Lewis in his place."

The applause which resounded over the radio for that brief two-paragraph section of the speech dealing with Labor was echoed and re-echoed in editorial pages all over the country. Some newspapers treated it as a speech about Labor; in many of them, the leading editorial was given over to the Labor angle, with scant, or at least only subsidiary, consideration for the Battle of the Atlantic.

All of these editorials, of course, upbraided John L. Lewis. In part, they may be said to reflect a genuine editorial concern for the maintenance of defense production. But the extreme intemperance of many of them suggests that they also represent, in part, a strong editorial bias against the militant organization of Labor. The thesis common to most of them is that strikes in defense industries are the result of the Administration's "coddling" of Labor. The jubilation of the editorial writers stems from an assumption that President Roosevelt has at last been won over to a sharp crack-down on the unions -- perhaps even to the acceptance of a legislative ban on strikes. Numerous news stories from Washington have given encouragement to this view.

Endorsement

Because of the emphasis which they placed upon its Labor aspects, commentators apparently did not regard the address as a major pronouncement on foreign policy. Many of them called it the most vigorous statement yet made of the American position. But they considered the position essentially the same as before the President spoke.

There continues to be overwhelming press support for this position. It is generally agreed -- to quote The Christian Science Monitor -- that "the United States cannot tolerate Axis control

of the seas," and that the Neutrality Act must be amended "not only to permit merchant ships to defend themselves, but to carry supplies 'into the harbors of our friends.'"

There is also general agreement with the President's observation that "the shooting has started." Editorial discussion is full of dialectics as to whether or not this means that the United States is in the war. Commentators with a feeling for the dramatic have been prone to assert that the war is on. But it is doubtful that they genuinely believe it. There is expectation of a vital change in America's relation to the conflict, but no real sense that the change has taken place.

Enmity

The press took scarcely more than a formal or polite interest in the secret Nazi plans revealed by the President for the obliteration of religion in Europe or the remaking of Latin America. It has taken such designs for granted for a long time past and needs no new evidence to persuade it of the menace of Nazism. What has genuinely shocked the sensibilities of editorial writers, and of all Americans, has been the day-to-day reports of Nazi brutality in the occupied countries.

It seems significant that the guilt for this brutality is no longer fastened exclusively upon Hitler or upon the Nazi

hierarchy. The German people, or at least the German Army, are regarded more and more widely as accomplices in the current disregard of civilized values.

As the President himself remarked, a powerful demand for retribution is growing out of this frightfulness. It appears to be having a twofold effect in the United States: (1) there is a diminished patience with apologists for the Nazis in this country; (2) there is a lessening of the American tolerance which might have exercised a strong influence for the extension of a generous peace to Germany.

There was a time when Americans believed that peace could be made with Germany simply by the removal of Hitler from power. It seems less likely now that they would countenance dealings with any of the elements in the Reich who have been responsible for the mass killing and uprooting of civilians. And editorial commentators now assume that the desire for vengeance among the victims of Nazi frightfulness will demand nothing less than the complete defeat and humiliation of the German nation.

The thinking of the American people, as the press reflects it, appears to be undergoing a change from the negative atmosphere of self-interest to the more positive level of active moral indignation. There is, as yet, no general realization that a state of war exists between Germany and the United States. But the background for war, the enmity and anger, is developing.

TREASURY DEPARTMENT

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INTER-OFFICE COMMUNICATION

STRICTLY CONFIDENTIAL

DATE October 31, 1941

TO Secretary Morgenthau
FROM Mr. Klaus

FBI reports that Nelson Courtlandt Brown has explained away the photographs which were sent up to you some time ago. They were taken by a German forestry expert who came to this country with the idea of establishing an international academy of forestry for purposes best known to the Germans who sent him. This man, whose name is Ebner, visited at the Forestry School in Syracuse and the Forestry School in Ann Arbor, Michigan, but left the country on May 17, 1941, bound for Japan. He had arrived here on August 13, 1940, on a visitor's visa and carried letters to the German Embassy.

Samuel Klaus

CHINESE EMBASSY
WASHINGTON

October 31, 1941

My dear Mr. Secretary:

I am very grateful for your letter of October 30th in which you informed me that the Department of the Treasury has no objection to the proposed appointment of Mr. A. Manuel Fox as Adviser to the Ministry of Finance. I have communicated by cable the contents of your letter to Dr. M. H. Kung.

With reference to the question of the Federal Reserve Bank appointing an expert to assist the Central Bank of China, I shall get in touch with the honorable Marrison S. Eccles personally, as you kindly suggested in your letter.

Sincerely yours,

(Signed) Hu Shih

Hu Shih

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

Copy:lc:11/6/41

C
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326

DEPARTMENT OF STATE
Washington

October 31, 1941

reply refer to
611.59 A 31/61

CONFIDENTIAL

My dear Mr. Bell:

With reference to Assistant Secretary Berle's letter dated October 9, 1941 enclosing a copy of a memorandum which had been sent to the British Embassy regarding the United States economic relations with Iceland, there is enclosed for your information a copy of a memorandum dated October 20, 1941, of a conversation between a representative of the British Embassy and an officer of the Division of European Affairs, together with copies of its attachments constituting the British reply to the State Department's above-mentioned memorandum.

The Department has been informed that the proposals outlined in memorandum numbered 2 have now been presented to the Icelandic Government by the British Government. The

American

The Honorable

Daniel W. Bell,

Under Secretary of the Treasury.

- 2 -

American Minister in Reykjavik has been instructed to inform the Icelandic Government that in the opinion of this Government the British proposals are fair and reasonable and that it is recommended that the Icelandic Government accept the proposals as a basis for negotiations.

Sincerely yours,

For the Secretary of State:

Signed. Breckinridge Long

Assistant Secretary

Enclosure:

Memorandum of conversation,
October 20, 1941, with
attachments.

copy:ka:11/3/41

DEPARTMENT OF STATE
MEMORANDUM OF CONVERSATION

DATE: October 20, 1941

SUBJECT: Economic relations of the United States and Great Britain with Iceland.

PARTICIPANTS: Mr. Wyndham White, First Secretary, British Embassy;
Mr. Cumming, Eu.

Mr. Wyndham White called this afternoon at his request accompanied by a British Treasury representative whose name I did not get. Mr. White left with me the attached informal memoranda which he said constituted the British Government's reply to the points raised by Assistant Secretary Berle in his conversation with Sir Ronald Campbell on October 7, 1941 and in the Department's memorandum addressed to the British Embassy on the same date, as well as the point which I put to Mr. White in my conversation with him on October 13.

Mr. White called my attention to the fact that his memorandum marked "II" contained proposals which the British Government was considering making to the Icelandic Government but which would not be made until the Embassy had received an expression of the State Department's views.

Mr. White also said that he had received the following figures, converted into dollars, regarding the value of Icelandic trade:

Icelandic imports from all sources during 1941 are expected to amount to \$16,000,000 of which sum \$10,000,000 will have been furnished from the United Kingdom;

Icelandic exports to the United States during 1941 are expected to amount to some \$4,000,000 and to the United Kingdom to some \$18,000,000 to \$18,000,000;

Icelandic

Icelandic revenue from the British occupying forces during 1941 estimated to be about \$12,000,000.

With respect to Icelandic dollar holdings and commitments, Mr. White gave the following figures:

Dollar balances at the end of August amounted to about \$500,000 (this probably included a United States Treasury deposit of \$300,000, together with various dollar deposits made by the Army disbursing officers in Iceland).

Dollar bills receivable at the end of August - \$265,000.

Against the foregoing holdings Iceland's import permits outstanding at the end of August amounted to about \$1,700,000.

I thanked Mr. White for the memoranda and statistics and told him that I would bring them to the attention of Assistant Secretary Berle as soon as possible.

With reference to the Department's memorandum of October 7th regarding the cooperation between the United States and British Governments in fulfilling their obligations to Iceland, we are authorized to state that the British Government agree in principle to the following proposals made by the Department in the afore-mentioned memorandum.

(a) That the fish agreement shall be included in the proposed Lease Lend arrangements.

(b) That in order that it may fulfill its broad obligations under the exchange of letters between the President and the Prime Minister of Iceland, the United States Government should purchase, until further notice, all imports from Iceland into the United Kingdom, these to be supplied to the British Government and charged to the British account as defense aid.

(c) That the United States Government should take over all of the unexpired contracts by which Iceland is obligated to supply goods to Britain. It is understood that goods which are not under contract will be the subject of arrangements to be made between the Lease Lend representative and the British representatives in Reykjavik, and further, that as unexpired contracts run out the United States Government will confer with the British Government.

The British authorities are communicating to the British Food Mission in Washington details of the working of the fish contract in order that discussions may take place with the United States authorities in order to ascertain how the proposals referred to above may be put into effect. Details of other outstanding contracts will also be transmitted to Washington.

As regards the question whether the British Government would require the Icelandic Government in accordance with the financial agreement between the two Governments to repay out of the dollars accruing under the present arrangements some two million dollars of Canadian and United States exchange advanced to Iceland by Great Britain last summer, we are instructed to say that the British Government would wish the Icelandic Government to admit their obligation to resell foreign exchange, but we are authorized to assure the United States Government that the British Government

would

-2-

would not press the Icelanders to resell until they have substantial dollar balances.

Finally, in reply to the Department's suggestion that the Icelanders should be allowed to utilize sterling funds for re-purchase of Icelandic debts held in Britain, we are authorized to state that the British Government would raise no objection to a suggestion of this kind provided that the transaction were effected through paying agents.

October 20th, 1941.

Copy:ec:11-41

Reference is made to the Embassy's memorandum of even date about arrangements for cooperation between the British and United States Governments in fulfilling parallel obligations to Iceland. The new situation brought about by the Department's memorandum of October 7th compels the British Government to reconsider its general financial relations with Iceland which hitherto have been based on the agreement of March 14th, 1941. We are asked, therefore, to obtain the Department's views on the following proposals which the British Government are considering making to the Icelandic Government:-

(a) His Majesty's Government to renounce their right to control over Iceland's expenditure of foreign exchange and to agree to abolish committee of 2.

(b) His Majesty's Government to renounce their right to control Iceland's import programme.

(c) His Majesty's Government to agree that Iceland's sterling accrued and to accrue shall remain available for any payments to residents of sterling area.

(d) Icelandic Government to renounce the right to call on His Majesty's Government to meet any deficit of foreign exchange (not only United States dollars but all other currencies than sterling and in particular Canadian dollars) including any deficit arising from service of export import bank credit.

(e) Icelandic Government to adhere to their obligation to resell to His Majesty's Government out of eventual surplus sums made available in foreign exchange by His Majesty's Government since beginning of British occupation.

(f) His Majesty's Government to agree to relinquish control of Krone - sterling rate provided that Icelandic Government agrees to make available without limit and at present rate the Krone required by His Majesty's Government for British forces in Iceland.

The above proposals are not being communicated to the Icelandic Government until the views of the United States Government are known.

October 20th, 1941.

Copy: 11-2-41

TREASURY DEPARTMENT

333

INTER-OFFICE COMMUNICATION

DATE October 31, 1941.

TO Secretary Morgenthau

FROM Mr. Dietrich

CONFIDENTIAL

Registered sterling transactions of the reporting banks were as follows:

Sold to commercial concerns	£123,000
Purchased from commercial concerns	£ 4,000

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

The Canadian dollar discount continued to widen. The final quotation was 11-1/4%, as compared with the current high of 10-5/8% reached two days ago.

The Venezuelan bolivar declined 40 points to close at .2580.

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

Argentine peso (free)	.2378
Brazilian milreia (free)	.0505
Colombian peso	.5775
Mexican peso	.2070
Uruguayan peso (free)	.4625
Cuban peso	1/8% discount

We sold \$10,000,000 in gold to the Bank of Java, which was added to its earmarked account.

We purchased \$350,000 in gold from the earmarked account of the Central Bank of Chile.

The State Department forwarded a cable to us stating that the Chartered Bank of India, Australia, and China, Bombay, shipped \$65,000 in gold from India to its New York office, for sale to the New York Assay Office.

In London, spot and forward silver remained at 23-1/2d, equivalent to 42.67¢.

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

- 2 -

We purchased 300,000 ounces of silver from the Bank of Canada. Today's purchase raises the total amount of silver bought from that source during October to 700,000 ounces, as compared with the agreed monthly limit of 1,200,000 ounces.

During the month of October, our purchases of silver under the Silver Purchase Act amounted to 1,450,500 ounces, a new monthly low since September 1939. The sources of this month's purchases were as follows:

<u>Type of Silver</u>	<u>Ounces</u>
New Production	
1. From various countries.....	750,500
2. From Canada under agreement.....	<u>700,000</u>
Total.....	1,450,500

CONFIDENTIAL

BRITISH EMBASSY
WASHINGTON, D.C.

Personal
and Secret

October 31st, 1941

Dear Mr. Secretary,

I enclose herein for your personal and secret information a copy of the latest report received from London on the military situation.

Believe me,

Dear Mr. Secretary,

Very sincerely yours,

Halifax

The Honourable

Henry Morgenthau, Jr.,

United States Treasury,

Washington, D.C.

TELEGRAM FROM LONDON DATED
OCTOBER 30th, 1941

EMPIRE GUILLOT, British, 6720 tons,
sailing independently Malta to Gibraltar is
overdue, probably sunk by torpedo from aircraft
off Gellie Island.

Russian Shuka (Destroyer) torpedoed and
sunk 4,000 ton Merchant Ship on 17th 80 miles
South-West of North Cape.

At 1400 2 B-24 Hudson aircraft off Aalesund
attacked Merchant Vessel estimated 3,300 tons
and another about 1500 tons. Heavy explosion
in one vessel both left on fire and believed
destroyed.

Another Hudson claimed one hit on enemy
S. S. in same area at 1930/lat. Hudson aircraft
attacked from low level two ships along side at
Aalesund claiming two hits.

At 2318 30th a Bearport attacked Merchant
Ship estimated 4,000 tons Bergen. Intense flak
and strong searchlights prevented observation of
result.

On 28th 8 Wellingtons carried out nuisance
raid on Tripoli; raid lasted 3 hours; 74-250 pounds
bombs dropped.

Last night 61 aircraft despatched from United
Kingdom majority to attack Schipol remainder to
Brest.

RUSSIA.

In reply to an inquiry concerning the fate of
the Soviet Ship at Nikolayev Volchov recently in-
quired His Majesty's Ambassador that all unfinished

ships which had been launched were removed together with all equipment in them and material required for completing construction; there remained on stocks a number of ships in early stages of construction but material for completing them had been removed and their hulls destroyed.

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MILITARY INTELLIGENCE DIVISION
WAR DEPARTMENT
Washington, October 31, 1941

TENTATIVE LESSONS BULLETIN
No. 168
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NOTICE

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TRAINING RESPONSIBILITIES OF YOUNG
GERMAN OFFICERSSOURCE

This bulletin, which is based upon a report submitted on July 7, 1941, by an American official observer in Berlin, comprises a translation of an article appearing in the Militär Wochenblatt, semi-official publication of the German Army, and comments by the observer. Other information on the subject of German military leadership is contained in Tentative Lessons Bulletins Nos. 145, 149, 155, and 157.

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RESTRICTEDTRAINING RESPONSIBILITIES OF YOUNG
GERMAN OFFICERS1. INTRODUCTION

This bulletin will attempt, first, to outline the method of continuing the training of the officer after he has been commissioned and second, to give some idea of the standards of knowledge, performance, and conduct required of the German officer.

The German military expert considers army officers as belonging to three general classes: lower, intermediate, and higher. These correspond in general to company officers, field officers, and general officers. In evaluating the efficiency of enemy forces, the German General Staff analyzes the opposing leadership from the point of view of these three general classifications.

It is interesting to note that although the subject of the translated articles is the continued training of officers in general, the greater part of the text deals with the younger officers only. The purpose of this emphasis, however, is not the creation of an effective army sometime in the future, but the maintenance of the effectiveness of the modern and highly efficient force already in existence.

The German believes that the company officer group is the most important in the officer classification, since the company officers are the ones who actually train the enlisted personnel and lead them in combat; they are the ones who in fact execute the decisions of the high command. Their importance extends upward as well as downward, for they are the men who will advance to the next higher classifications of officers and will establish the standard for the group of company officers who will succeed them.

This bulletin is believed to be of importance at this time because of the large number of new and inexperienced officers in the lower grades in our own army as well as that group of officers in the intermediate and higher grades who have not been able to devote their full time toward their development as military leaders.

The bible of the German Army is Truppenführung - Troop Leadership. This text is continually referred to in the instruction at the German Command and General Staff School, and it is the basis for all officer instruction in the German Army.

The articles translated in this bulletin are valuable in that they deal with the training of officers in time of war. By the end of 1941 the German Army will have expanded to approximately six times its

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peacetime size, and the supply of leaders in this expansion is one of the greatest problems that has been solved. It has been met by the large scale development of young leaders, by the commissioning of many reserve officers from the ranks and from veterans of the World War, and by the appointment of many specialists as civilian administrators. The older officers and the civilian specialists have taken over the administrative work, leaving the line officer to concentrate on the main task, leadership of troops in combat.

The standards for officers in the German Army are high, and discipline is strict. If an officer does not meet the required standards, he is eliminated without delay, before he can have a harmful effect on his juniors.

2. TRANSLATION

a. Necessity for Training of Officers

"The progressive training of the officer corps and the development of a solid and efficient nucleus of officers belong among the most urgent missions of all commanders, especially in time of war. Regimental, battalion, or detachment commanders should be most competent for this mission.

"Relatively few regimental officers today have had the full benefit of normal peacetime training. The emergency conditions which have existed since 1933 have entailed the use of emergency training plans, which have applied to officers as well as enlisted personnel. That these emergency measures have been successful is shown by the results attained by the German troops on the battlefield, for only high-grade troops with good training and under superior leadership could achieve such decisive success within such a brief period. We should not blind ourselves, however, to the fact that, as far as the training of our officers - and particularly of those young officers with war promotions - is concerned, many a gap still remains to be filled. This statement, of course, constitutes no criticism either of these young officers themselves or of their instructors. If, indeed, one could become the perfect lieutenant in as short a time as the present brief period, then we officers of former times have had superfluous preparation. This is not the case by any means.

"We do not know what missions are in store for us, but the sword must be kept sharp for any purpose. The surest foundation for this is thorough and all-round training of the corps of officers and the development of satisfactory successors to them. Whether peace is to come soon or whether war is to last a long time is immaterial in this respect; under any circumstances, training in military leadership and the care for its development remain a mission for the commanders concerned, a task

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which is as magnificent as it is urgent.

"In the first place, let us outline the requirements for the development of our officers. The strength of the German Army has lain, and still lies, in the platoon commander at the front. This will remain so in the future, and the example of our lieutenant as he stands and fights at the front cannot be emulated by any nation on earth, according to a well-known saying of Bismarck.

"One would misjudge the lieutenant's mission entirely, however, if one would have him conform exclusively to the services of, and requirements for, a platoon commander. Actual conditions require much more of the lieutenant than mere service as such. Any lieutenant may, at any time, have to educate, train, and lead a company, battery, or other similar unit, and any lieutenant may suddenly have to serve as a staff officer or even as an adjutant or aide-de-camp. We have already witnessed such surprising changes of personnel at different times, and for the most varied reasons, that there is no need to supplement our statement by examples. The progressive training of the officer corps, then, must be carried out with this eventuality in mind.

"How can a lieutenant carry out the duties of a company commander if he is unfamiliar with those duties? How can a young officer fill the desirable position of a staff officer or adjutant if he has never studied the requirements for these assignments? War demands increased effort of every individual and requires that the positions just named be capably filled, even if the new occupant is given but a short time to prepare himself. In peacetime, one may say of shortcomings that improvement will come in due course, but in wartime this cannot be. Mistakes made today have their consequences, and no God, no time, can obliterate them. It is clear, then, that peacetime preparations must further full acceptance of any and all new duties facing a young officer. One may also quote in this connection: 'Time is yours; what you make of it depends on you.' This saying of a gifted soldier had, and still has, great meaning. It is as true for a large group as well as a small, for the life of the individual as well as for that of nations, for military life as well as for civil. In this article we offer some suggestions for the progressive training of younger officers."

b. Tactics

"The first requirement is adequate training of the officer commanding troops, that is, training in tactics. The word tactics causes many a young officer to shudder unnecessarily, but only common sense is needed in order to learn the most elementary fundamentals of tactics. A copy of the regulations - Truppenführung - and a few hours of quiet meditation is all that is normally required, and in case of need, one may ask a senior comrade for information and assistance. The limited

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equipment required is obtainable everywhere.

"A great many young officers have no knowledge of the fundamentals of tactics, and because of this lack of understanding, the discussion during lessons is often vague. Lack of indoctrination is a most serious defect and necessitates many unnecessary commands. Here is an example: Our unit is an infantry battalion, and in an engagement the situation becomes critical; commands and reports come into the battalion commander from all sides. The adjutant and the commander of a machine-gun company become casualties. The battalion commander, an especially energetic man, has made an important decision and is just about to give orders to carry it out. What if the new adjutant, totally ignorant of tactics, transmits the orders to the new commander of the machine-gun company who is just as ignorant? Of course we have selected as an example a particularly gross case, but one can hardly pretend that it is outside the sphere of possibility. One must insist, therefore, that all officers be thoroughly indoctrinated with tactical principles. Young officers must be thoroughly familiar with the tactics of all units up to and including the battalion, and in this field much remains to be done. Older officers must work to teach and the younger ones must work to learn. It is an open but immaterial question as to which task is the more difficult; the important thing is to attain the clearly defined objective.

"Tactics were taught in peacetime according to the so-called method of application: that is, they were taught and learned by example and execution. Present training also utilizes this tactical schooling, and map exercises and map problems are used extensively; there are, however, two fundamental drawbacks to this method. In the first place, the formulation and conduct of these map exercises requires skill which is not always available. In the second place, only those actually participating benefit from the instruction, and if there is a large group of participants, only a few officers will have a chance for discussion. Most of the others remain silent in order to conceal their ignorance. Human nature is that way, in spite of claims to the contrary, and therefore methods must be used which insure that every officer take an active part in the study. Officers must write out their solutions to tactical situations and stick to their decisions - there is no other choice. Every officer must work out the situation and arrive at a decision; it does not matter that solutions will not always be original - the important thing is that every officer take a definite stand one way or another concerning the problem. The books, Truppenführung and Infantry Training Regulations, are referred to concerning each problem, and thus each young officer constantly reviews the application of the important principles and doctrines. Let us be honest: self discipline at times is of advantage everywhere in life and especially in the army. It stands to reason that the young officers will have to sacrifice many an evening hour, but it is a worthy sacrifice. The officer who has to review and correct the written work usually has a far more onerous job, but he must

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accomplish this important work in one way or another in spite of his other pressing tasks. It should hardly be necessary to mention that an oral discussion of the individual solutions is useful.

"Extraordinary times demand extraordinary measures, and although we must work fast, we must be thorough. Even under present conditions formal tactical instruction must be resumed. The scope of the instruction should cover formal, or normal, tactics in order to give the individual a general background of the subject. The instructing officer will present a situation, ask tactical questions of the individuals, and then discuss them in detail, letting each man present his own views. This teaches the students to speak clearly and with military phraseology. An officer must know how to express himself, even though many older officers are not too adept at this. He needs this faculty as an educator, trainer and commander. Formulation of ideas by extemporaneous speaking is, therefore, vital.

"To stand still is to go backward, and no officer can ever know all there is to know about handling men. Even experienced tacticians always find new problems in the vast field of tactics. That is what makes the subject so interesting, and proves it to be the foundation of the art of war."

c. Military Terminology

"The proper use of military terminology is the first essential, and one day devoted to the correction of faulty language would be well spent. Repeated effort should be made to correct defects and to learn to use military terms and definitions fluently in order to convey ideas quickly, correctly, and accurately. It is a matter of record that numerous and sometimes disastrous errors are traceable to careless or loose expressions in commands or orders. Accuracy, even in the smallest details, has been advocated and demanded by all great soldiers of the last two centuries. We need mention only Frederick the Great, Gnaeus, Clausewitz, Moltke, Schlieffen, and Seeckt. This uniform teaching of these masters of the art of war is food for thought to officers who are interested in the military character of the great.

"When selecting subjects for discussion, nothing should be taken for granted. In discussions, improper use of terminology can be corrected and false ideas pertaining to the organization and employment of the other arms may also be clarified. It is our problem to put an end to errors and misconceptions, for mutual dislikes and faulty ideas often result from them. Apart from various combat methods, such as assault with or without preparation, defense, avoiding contact, breaking off an engagement, etc., there are other tactical themes available. These include problems in connection with scouting, reconnaissance, observation, liaison, communications, commands, armored protection, air defense,

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defense against gas attacks, and other things."

d. Personnel Training

(1) General

"After combat leadership, the second most important objective is increasing the young officer's capacity to train personnel. In order to be successful in training other people, two things are necessary: first, the officer conducting the training must himself have mastered the subject which he proposes to teach; secondly, he must be thoroughly familiar with the methods by which he is to convey his own ability and knowledge to others. One is just as important as the other."

.....

(2) Importance of Manuals

"No branch of military training is of secondary importance. Opinions may vary as to whether or not one branch is more important than another; but one thing is certain; all training has combat efficiency as its ultimate aim. This is true of the manual of arms, the facings, saluting, etc. Let us illustrate our meaning by choosing an example out of the wealth of material found in the target practice regulations. These firing regulations outline the training in the most minute detail. The small arms regulations apply to all branches of the service, troops as well as staff: in short, to every German soldier. But our excellent regulations have simply not penetrated as far as they should have. One knows that these regulations exist; one has come across them at one time or another - perhaps even read over a few of them. But this does not suffice to establish them as a basis for training, for we do not apply ourselves assiduously enough to the details of the regulations. We should demand complete and thorough knowledge of them. As an older officer, one must stress application to regulations.

"It is immaterial whether the young officers desire to pursue this study of regulations or not. If an officer wishes to acquire a thorough training, the only thing for him to do is to plunge into the secrets of our regulations - the earlier the effort is made, the easier it will be for him. We do not mean by this that German officers should concentrate all their energies on studying abstract regulations, but young and old officers alike should master the regulations of all training branches down to the most minute details. Here are three of the most obvious deficiencies of instructors:

"(a) Many instructors themselves do not know the correct, regulation method. It is quite obvious that such an instructor can neither explain nor demonstrate correctly.

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"(b) Many instructors have no eye for the shortcomings of their men or for the mistakes that they themselves make. Before mistakes can be corrected, they must first be seen and recognized. If the instructor does not notice such mistakes, they go uncorrected and become habitual, causing considerable harm later,

"(c) Many instructors notice the mistakes which their men make, but do not know how to correct them. To correct a man, it is not enough to tell him what is wrong; he must actually be shown how to do the job properly.

"Officers today often lack knowledge of time-tested instructional practices, whereas the old-time N.C.O. was usually an absolute master of the regulations.

"It is not the purpose of this article to go into great detail on the subject of training. It is sufficient to point out the difficulties which face instructors. The present situation can be improved by simple, thorough study of the regulations, by improving the efficiency of the individual officers, by increasing their powers of observation with regard to shortcomings and mistakes of their juniors, and by finding adequate means for correcting them.

"The complete military education of the soldier is more important than any specific phase of his training. Quite naturally, some young officers will be more proficient in one field than in another, and this condition usually produces satisfactory results, for because of their varied interests and aptitudes, several officers are often able to supplement one another in training and instruction. It is imperative, however, that a certain minimum of efficiency in each task be demanded of every officer."

(3) General Teaching Ability

"Let us return to the officer's duty as an instructor or teacher. Only an educated man can educate others. Who may claim to be educated? Only he whose natural adaptability, training, self-discipline, and mental and physical effort have made him superior to the average can be a true leader. A teacher bears an enormous responsibility, but it often appears that many officers are conscious enough of their uniforms and shoulder straps without realizing, however, their great responsibility of setting a correct example. Officers, especially the younger ones, cannot be reminded often enough of their obligations in this respect. There are too many misconceptions concerning the personal life of an officer. For instance, there is the question of civilian clothing. An officer, of course, is allowed to wear civilian clothes under certain circumstances, but he must always remember that he is still an officer, and he must conduct himself accordingly.

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"We need no classroom psychologists to instruct our men. What we do need are officers with a knowledge of human nature, officers who know the souls of the men, who know how to handle them. It is said that the art of handling men is born, not made, and that there is no way to acquire it. This is an incorrect, though common, belief and the whole subject deserves to be treated in great detail. In order not to go beyond the scope of this article, however, we must be content with pointing out the fact that much can be done in this respect by regimental commanders. Punishment and complaint records often show that discipline is either too lax or too severe, but philosophical and psychological doctrines on this subject will not help young officers. Study of actual cases of different methods of handling men, however, will help them and should be encouraged. The correct and incorrect methods actually explain themselves in the course of ensuing discussions and these may then be confidently applied by the young officer. It is hardly necessary to mention that the application of the discipline-punishment regulations, the court martial regulations and the regulations concerning complaints, should be mastered as early as possible."

(4) Instructional Methods

"Instructional methods have an important bearing on both training and discipline. Many officers are unable to make problems clear to the relatively simple minded soldier, for the essential difference between mentally superior people and those not so gifted is the ability to think in the abstract. It is useless to instruct the German soldier in terms of the abstract. Our men are better able to understand and to carry out what is required of them or what is essential if one explains the attributes of a good soldier to them in simple terms, using concrete examples. Such instruction must connect their duties with life as they understand it, and must never go beyond their powers of comprehension. Too many officers' courses fail to stress the value of simplicity in instruction, often approaching the problem of simplicity and clarity on a highly theoretical basis.

"The officer must understand that it is not merely a question of his thorough knowledge of the subject matter, but also of the adequacy of his teaching methods. Clarity, lucidity, enunciation, formation of sentences - in short, mental discipline in expressing oneself - are indispensable requisites for successful instruction. Questions should be answered with a complete sentence; monosyllabic answering is a bad habit and should be eradicated.

"The standard of training in the German Army is certainly high, but it could be much higher if no time were wasted. In order to save time, every lieutenant must learn to conduct the training of the company in case his company commander should be absent. A young lieutenant who becomes the leader of the subordinate staff when acting as a company

commander or as an adjutant should know how to assign daily tasks and how to utilize fully the time available for training. To accomplish this our lieutenants require methodical training by the company commander.

"Young officers usually have the most difficulty in planning, leading, and discussing tactical exercises. It is really not so difficult as the beginner usually thinks. Knowledge of details is not acquired by reading books and magazines, but by practical experience in the field. A clearly defined, definitely limited objective is the first requisite of a battle exercise. He who attempts to accomplish too much, ends by achieving nothing. It is better to learn a little, but that little thoroughly.

"The choice of the terrain is the next problem. In this respect, one is usually limited in one's choice, being forced to take whatever is within easy marching distance. Variety is essential. If one is lucky enough to be able to choose, one should begin with terrain which is suited to the maneuver, advancing later to less favorable terrain.

"The situation is outlined as simply as possible. One begins with the next larger unit - that is, in the case of a company exercise, with the battalion. People have often wracked their brains wondering how the battalion got into this or that situation! How many different situations have been created in this war, in former wars! Every situation has already existed somewhere or other before, and may therefore occur again.

"Objectives must be clearly defined. It is wrong to complicate the problem with artificial difficulties; enough natural ones will appear. Brief estimates of the situation of all units down to and including the battalion must be oral only and simplicity and clarity of expression are highly important in these explanations.

"In all such exercises mistakes are made and shortcomings in the instruction methods become evident. If this were not so, there would be no need for practices. The important thing is to recognize and eradicate these defects, and for this reason an umpire is essential. Umpires must be fully acquainted with their mission; they must be able to think quickly; they must know the purpose of the exercise, its expected development, etc. They must be able to act energetically and with a sense of responsibility of leadership. They must see and report defects, for this is the only way to secure improvement. Critiques are customary and necessary, but the training is far more valuable if the exercise is repeated on the same or on the following day. As a rule one does not learn simply by being told how things should be done correctly, but by being required to do those things correctly. One should, therefore, not hesitate to repeat an exercise, although slight variations are always permissible.

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"Some young officers will show more imaginative ability than others, but every officer can at least learn how to plan, lead, and discuss small exercises and to impart his knowledge to his men. Properly conducted tactical exercises are also important in that they help arouse and build up esprit de corps, which in turn makes learning enjoyable. It is only by working together under competent leadership that a unit acquires pride in itself as a group and a collective willingness to profit by instruction."

c. Administrative Responsibilities

"Besides the training and instruction of the troops, there is the question of administration, an indispensable ingredient of either military or civilian life. Officers must become acquainted with the most important problems in this sphere of activity as early as possible, for if a young lieutenant has not learned how to handle administration, when the time comes for him to take over the command of the company, he is completely dependent on his first sergeant, his supply and mess sergeants, and his other noncommissioned administrative officers. To be sure, most of these N.C.O.'s fulfill their obligations most satisfactorily, but a company commander must be capable of supervising intelligently all of the administrative operations.

"The most essential part of the education of an officer is the so-called garrison duty. Probably there are certain young lieutenants who, because of a limited amount of time, have never experienced regular barracks' life as it is in time of peace. Discipline, attention to detail, appearance, in other words the standard of military training, is absolutely dependent upon training in garrison duty. We could dispense with a great deal of drilling if more attention were paid to garrison duty, which includes such matters as living quarters, clothing, pay, furloughs, bugle calls, cleanliness, messing arrangements - in short - the soldier's day. Even our first sergeants are sometimes young and untrained, and there is always trouble when an inexperienced officer and an inexperienced first sergeant meet. For this reason, the officer himself must be familiar with much of the detail that actually is the responsibility of the first sergeant.

"We have already mentioned the nature of garrison duty. There are many other problems connected with this subject, such as the question of clothing, general supply, perhaps even of the care of horses. The young lieutenant, as well as the company commander, should have complete knowledge of the furlough and complaint regulations, of disciplinary regulations, and of those regulations connected with the writing of reports. Considering everything, these subjects are so numerous and far-reaching in their extent that young lieutenants will lose heart if they are brought face to face with all of them at once. They must therefore start the study of the duties of company commander long before they may

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be called on to execute these duties. Naturally they have learned much during their past period of service, partly by the assimilation of information and partly by regular instruction. If such continuous advanced training is demanded of all lieutenants acting as platoon leaders, the responsibilities of company commander will be eagerly sought and effectively met. The initiative of the lieutenant cannot be depended upon entirely, however, and the company commander should encourage and facilitate the training of his younger officers by delegating his own duties to them on suitable occasions. If every company commander were fully conscious of his obligations in this connection, in a comparatively short time there would be a marked improvement in the training as a whole. Along with a knowledge of the regulations, practical experience is the best teacher of all."

3. COMMENTS OF OFFICIAL OBSERVER

In general, the systematic training of officers is often neglected and especially in the case of those on duty with troops. During the great activity incident to mobilization and the conduct of the campaigns to date, the training of the officers assigned to units in the German Army has apparently ceased or has been seriously curtailed. The purpose of the translated articles is to point out the fallacy of this procedure.

The author states that the responsibility for this training rests in the hands of the regimental and lower unit commanders and points out the extra effort required, both on the part of the officers themselves as well as their instructors.

One important attitude is emphasized in this article: officers, once having reached a particular grade, should immediately begin to prepare themselves to perform all the duties connected with the next higher grade. Too often do officers attempt to adjust themselves in grade, that is, they seek to perform well all the duties incident to their present grade and devote too little thought toward preparing themselves for the next higher grade. Because there have been many promotions connected with the great expansion in the German Army, this question is given particular attention. In fact, many officers in the German Army are now actually performing the duties of the next higher grade. This is especially true of first lieutenants commanding companies and batteries.

The system of mobilization in the German Army is simple and effective. The nation is divided into Wehrkreiscommandos, administrative area commands similar to our corps areas. Division mobilization centers are located in the Wehrkreiscommandos and there is also a relationship between the succession of divisions which have been formed in each of these division mobilization centers. One such relationship follows: When a new cadre of draftees have finished their basic training and are about to be formed into units, officers from the predecessor divisions

are transferred to the newly formed division to conduct its unit training and to form it into a well-rounded combat team whose standards are already established by the combat units which have graduated into the field army. Thus, experienced officers who have usually had combat service are assigned to a new unit without materially affecting the efficiency of the unit from which they were transferred. The influence of these officers on new officers is, of course, noteworthy.

The officers on duty in Berlin have had the privilege of inspecting the training of a wartime German division, and there is no question but that the state of training in the German Army is exceptionally good. The use of practice ammunition - ammunition with reduced charges for all infantry weapons - is a great advantage, for it produces all the noise and confusion of battle. Umpires go with the troops through their combat problems and assess casualties, which lie on the battlefield; the result is that the assault personnel are experienced in combat before they are ever employed on a battlefield. The Germans always hold critiques immediately after the exercise, on the spot where the exercise took place, in order that the commanders and umpires can point out exactly where and how mistakes occurred. Then, if it is of advantage, the exercise is conducted again. In this way, the outline of definitely limited objectives or purposes for a combat exercise is emphasized and combat perfection is approached.

Constant reference to standard texts is common practice in the German Army. The translation of the written word into execution is stressed. This gives the officer a real appreciation of the regulations and enables him to understand other sections of the texts more intelligently. It is also a further incentive to study the instruction texts, especially Truppenführung.

The German Army believes that leaders are developed - not born. They have proved the correctness of their belief by example.

Young line officers for the German Army are carefully chosen after considerable preparation and competition. They are given a splendid basic training to fit them for their duties in the lowest grades, and this article stresses the necessity of continued training in spite of the pressure of duties. This is possible under present conditions because, in spite of the fact that Germany has been at war almost two years, the land forces have engaged in active operations only a few weeks of that period.

It is pointed out in the article that every German soldier must learn to shoot the rifle. This is part of the basic disciplinary training which all soldiers receive, including the Air Force personnel.

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G-2/2657-220; No. 533 M.I.D., W.D. 11:00 A.M., October 31, 1941

SITUATION REPORTI. Eastern Theater.

Ground: Situation at Leningrad remains unchanged.

There is no definite information of military operations around Moscow. It is reported Germans have reached vicinity of Tula.

German High Command claims further advances in the Donets Basin and on the Crimea.

There is no further information regarding the situation at Rostov.

II. Western Theater.

Air: Bad weather limited British activity to slight low-level attacks on objectives along the French coast during daylight yesterday. However, Germany braved bad weather to continue its series of raids against Great Yarmouth.

German lists of casualties from bombings released yesterday listed 2400 Germans killed and 5300 injured from April 1 until September 30.

III. Middle Eastern Theater.

Air: The British Middle East Command announced yesterday that the R.A.F. had carried out several raids on Siderno and Soverato, in southern Italy, and on Comiso, in Sicily.

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