

DIARY

Book 500

February 22 - 24, 1942

- B -

	Book	Page
Barton, Mary - Cedar Rapids, Iowa		
For letter on cost of living and high taxation, see Financing, Government		
Bethlehem Steel Corporation		
Supreme Court report sent to HMJr by Frankfurter - 2/23/42.....	500	95
Business Conditions		
Haas memorandum on situation for week ending February 11, 1942.....		111

- C -

Chile		
See Military Reports		
Coordinator of Information		
See Revenue Revision		
Contracts		
Exemption from State Taxes: Assistant Secretary of Navy Bard's proposal discussed in HMJr's memorandum to Blough - 2/24/42.....		227
a) Blough memorandum - 3/10/42: Book 506, page 259		
Crawford, Gilbert		
See Foreign Funds Control		

- D -

Defense Savings Bonds		
See Financing, Government		

- E -

Economic Warfare		
See Latin America		
Exchange Market		
Resume' - 2/24/42.....		277

- F -

Ferguson, Major General (Retired) Harley B.		
See Treasury Buildings		
Financing, Government		
Financial Reports: Budget-FDR-Congressional correspondence concerning joint effort of Treasury and Budget - 2/23/42.....		78
Small incomes as affected by high cost of living, increased taxation, and defense bonds discussed in letter from Mrs. Mary Barton, Cedar Rapids, Iowa, to Mrs. FDR - 2/24/42.....		235
Defense Savings Bonds:		
Daily changes in stock of Series E Bonds - 2/24/42..		250

- F - (Continued)

	Book	Page
Foreign Funds Control		
Genus of foreign-owned property - White memorandum - 2/24/42.....	500	269
Crawford, Gilbert: Disbursing of German funds discussed in Treasury-Coordinator of Information correspondence - 2/24/42.....		273

- G -

Germany

 See Gold

Gold

Shipments from Germany to Switzerland - White memorandum - 2/23/42.....		143
Shift from dollar deposits to gold by foreign governments and central banks - White memorandum - 2/24/42.....		271

- I -

Insurance Companies, Life

 For tax-exempt income, see Revenue Revision

- L -

Latin America

Economic Warfare: Procedure for carrying out an active program - Foley-White proposal to be presented to Board of Economic Warfare for consideration - 2/24/42.....		265
--	--	-----

 Chile: See Military Reports

 Venezuela: See Military Reports

 Lahman, Herbert H. (Governor, New York)

 See Revenue Revision: 1942 Revenue Bill

Lend-Lease

Agreement signed between United States and United Kingdom - 2/23/42.....		123
---	--	-----

Life Insurance Companies

 See Revenue Revision: 1942 Revenue Bill

- M -

McConnell, Robert H.

 See also Foreign Funds Control: General Aniline and
 Film Corporation - Books 497, 501, and 504

Refund (tax) for 1933, 1934, and 1935 discussed in Foley memorandum - 2/24/42.....		243
---	--	-----

- M - (Continued)

	Book	Page
Military Reports		
Japanese warfare - notes on: War Department bulletin - 2/22/42.....	500	14
Reports from London transmitted by Halifax - 2/23-24/42.....		148,150,278
Kamarck summaries - 2/23-24/42.....		153,280
Venezuela:		
Treatment of envoys since breaking off of diplomatic relations - Coordinator of Information report - 2/23/42.....		155
Submarine action in the Caribbean and serious effect on economic position - Coordinator of Information report - 2/24/42.....		287
Chile: Rosetti (Foreign Minister) and influence on foreign policy discussed in Coordinator of Information report - 2/23/42.....		158

- O -

O'Mahoney, Joseph C. (Senator, Wyoming) HMJr thanks him for remarks concerning reduction of interest rate on national debt - 2/23/42.....		98
---	--	----

- P -

Procurement Division		
Reynolds' move from building discussed in Thompson memorandum - 2/23/42.....		110

- R -

Revenue Revision		
Extension for filing returns - Cann (Norman) memorandum - 2/23/42.....		50
Congress of Industrial Organizations income and expenditures study - preliminary report - 2/23/42..		52
Lehman asks about reciprocal deduction of Federal and State income taxes - 2/23/42.....		76
1942 Revenue Bill:		
Conference; present: HMJr, Sullivan, Paul, Tarleau, and Blough - 2/23/42.....		20
a) Special privilege and hardship provisions discussed		
Lehman (Governor, New York) asks about reciprocal deduction of Federal and State income taxes - 2/23/42.....		76
a) Discussion by HMJr, Blough, and Tarleau.....		208
Life Insurance Companies - tax-exempt income: Bell to be consulted as to effect of any legislation on Government bond market - 2/24/42.....		195
a) Conference with Bell explained to HMJr by Blough and Tarleau - 2/24/42.....		199

- S -

Switzerland
See Gold

Book Page

- T -

Treasury Buildings

Ferguson, Major General (Retired) Harley B.; To assist
in protection of buildings in Washington and in
the field - 2/23/42.....

500 106

- U -

United Kingdom
See Lend-Lease

- V -

Venezuela
See Military Reports

READING COPY OF HM, JR'S REMARKS ON
A F OF L PROGRAM IN WHICH MR. GREEN, PRESI-
DENT OF THE A F OF L ALSO PARTICIPATED

SUNDAY NIGHT FROM THE SECRETARY'S
DESK, FEBRUARY 22, 1942, at 8 P. M.

President Green and members of the American Federation of Labor: This pledge of yours to buy a billion dollars of Defense Bonds in 1942 is a magnificent example to the whole country. It is the biggest pledge that has come to us from any single organization. It amounts to about \$200 for every one of your five million members. In fulfilling your pledge you will be giving still further proof that American labor is ready to do its utmost to win this war for freedom.

85
875

This war is a crisis for the American labor movement in more ways than one. We in this country have prided ourselves upon our freedom of speech and worship, our system of equal justice under law, our free public education and the limitless opportunity that our way of life provides. From these American freedoms the trade union movement has grown and made its influence for good a mighty force in the community.

We have not yet made a paradise of this free country of ours. I know that there are many injustices still to be righted.

181
779

I know that millions among us still live in poverty through no fault of their own. I know that millions of our Negro people are still denied the free and equal opportunities to which our Constitution entitles them. I feel as humiliated as you do when I read that thousands of able and willing workers cannot find employment in war industries because of their nationality, race or religion.

All these faults and many more are undeniable; no one can honestly say that we have reached our destination. Nevertheless, we in this country have always been moving forward on the eternal quest for a better and broader and a more secure future for ourselves and our children.

297
663

That forward march has now been gravely imperilled by a combination of cruel and barbaric conquerors on other continents. They have begun by choking to death the free institutions of their own countries. They have abolished trade unions, they have perverted education and science, they have destroyed the rights and dignity of the individual, and they have re-established conditions of tyranny that we thought had passed forever from our kind of world. Not content with that, they have blotted out the independence of one free country after another. I shall not read the tragic list of countries, once as free as our own, which have had their peoples enslaved by these new forces of paganism and terror.

415
545

Nor do I need to tell you in detail of the crimes committed and the miseries inflicted upon hundreds of millions in the name of the so-called "new order." You know them well, and you know how many workers in other countries have been imprisoned, tortured or killed -- for no other reason than that they were members of labor unions. Organized labor, at least, never made the mistake of imagining that we could compromise with the authors of those crimes. Organized labor in this country has always recognized fascism for what it is, and has known from the beginning that the fascist system was a deadly menace to our free institutions.

527
433

Today, as you foresaw, the tide of fascist conquest and barbarism is sweeping the whole world. This evil thing in field-gray uniform and hob-nailed boots is creeping up, even on us in our sheltered continent. It has broken loose on both sides of us, across the Atlantic and Pacific.

We know now that we are not safe even here in America. We know that unless we and our allies win this war there will be no survival of free trade unions, no liberation of the millions of workers now enslaved abroad, no continuance of the rights that we have won in generations of struggle here at home, no chance to win a better future for the working men and women of the world.

652
308

As I have said repeatedly, this is not a token war. It cannot be fought or won by token effort. It is a war of desperate seriousness. It is so serious that it allows no margin of safety for any of us.

Organized labor has never underestimated the size or scale of the war effort that will be needed. Your unions, for example, long ago urged the quick conversion of our peacetime industries to war production, even though the effect would be temporary unemployment for large numbers of workers.

3/4

141
219

From now on the war effort on the home front will take many forms, among them the production of ever greater quantities of weapons, the conservation of materials, the acceptance of higher taxes, and the purchase of more and more Defense Bonds. It may not be dramatic to set aside a part of your pay each week for bonds, but it is tremendously important to the success of the war effort as a whole, and it is something that can be done by everyone who earns a regular income. I accept your pledge of a billion dollars as a demonstration that you will support the war effort with all your might, no matter how hard or how long the war may be.

863
97

Pause

You cannot set a price on the things for which America stands. You cannot measure their worth in terms of money or of sacrifice. They constitute a faith that is beyond price because it is worth more than life itself. It is a faith that Americans have fought for and died for, and they will do so again, for life without that faith would not be worth living. If Americans are to be true to themselves and to their future, they will fight and sweat and save, and exert every ounce of effort until victory is won.

-000-

960
0

Special Radio Program via NBC Blue Network
Sunday, February 22, 1942 8 - 8:30 P.M.
Broadcast from the Secretary's Office
in the Treasury

The Secretary of the Treasury
William Green, Pres. of A. F. of L.

The following will attend:

From the Treasury:

Mr. Harold N. Graves

Mr. and Mrs. Ferdinand Kuhn

Mr. and Mrs. James L. Houghteling

Mr. and Mrs. Herman Klotz

Mr. and Mrs. Vincent Callahan

Mr. James Barrett

From NBC:

Al Powley, Engineer

Bryson Rash, Announcer

Guests of the Secretary, Movie Program, Sunday
February 22 at 9:15 P. M.

Mr. and Mrs. D. W. Bell

Mr. and Mrs. John L. Sullivan

Mr. and Mrs. E. H. Foley, Jr. and two children

Mr. Harold N. Graves

Mr. and Mrs. Ferdinand Kuhn

Dr. and Mrs. Jacob Viner

Mr. and Mrs. Charles Schwarz

Mr. and Mrs. Roy Blough

Mr. and Mrs. J. L. Houghteling

Mr. and Mrs. Herman Klotz

Mr. and Mrs. Vincent Callahan

Guests of the Secretary at Supper following the
Broadcast:

Mr. and Mrs. Ferdinand Kuhn

Mr. Harold N. Graves (?)

Mr. and Mrs. James L. Houghteling

Mr. and Mrs. Herman Klotz

Mr. and Mrs. Vincent Callahan



New Type of Japanese Light Machine Gun
(See Section III)

MILITARY INTELLIGENCE DIVISION

INFORMATION BULLETIN NO. 9

NOTES ON JAPANESE WARFARE

WAR DEPARTMENT
WASHINGTON, D. C.

RESTRICTED

MILITARY INTELLIGENCE DIVISION
WAR DEPARTMENT
Washington, February 22, 1942

INFORMATION BULLETIN
No. 9
MID 461

NOTICE

The information contained in this series of bulletins will be limited to items from official sources which are reasonably confirmed.

This document is being given an approved distribution, and no additional copies are available in the Military Intelligence Division. Its reproduction is governed by the provisions relating to category B documents in Letter AG 350.05 (9-19-40) M-B-M.

NOTES ON JAPANESE WARFARE

FOREWORD

In view of the enlarged distribution now given to Intelligence Information Bulletins, the attention of all is invited to the provisions of paragraph 10a, AR 380-5, which is quoted in part as follows: "A document * * * will be classified and * * * marked *restricted* when information contained therein is for official use only, or when its disclosure should be * * * denied the general public."

In order that our troops may familiarize themselves with the appearance of their enemy, it is suggested that these photographs, which are themselves not classified as *restricted*, be removed and placed on bulletin boards.

RESTRICTED

CONTENTS

SECTION I. Statement by General Wavell on the Japanese Army in Malaya.....	1
1. Introduction.....	1
2. Training in the Japanese Army.....	1
3. Modern Military Techniques.....	1
4. Modern Techniques Displayed in Malaya.....	1
5. Discipline and Morale of Japanese Soldiers.....	2
II. Organization and Tactics of the Japanese Platoon and Section on the Malayan Front.....	3
1. The Infantry Platoon.....	3
2. The Infantry Section.....	3
3. The Approach March.....	5
4. Bivouacking.....	5
5. Transportation.....	5
6. Night Operations.....	5
7. Messing.....	5
III. Information upon Various Items of Japanese Matériel.....	6
1. A New Type of Japanese Light Machine Gun.....	6
(illustrated on the cover)	
2. Fighter Planes.....	7
3. Bombs.....	7
4. Observation Balloons.....	7
5. Artillery.....	7
6. Grenades.....	8
7. Grenade Dischargers.....	8
8. Revolvers.....	9
IV. The Japanese Parachute Attack upon Palembang.....	11
1. Large-Scale Use of Parachutists.....	11
2. Defeat of the Parachutists.....	11

ILLUSTRATIONS
(at end of text)

SECTION I

STATEMENT BY GENERAL WAVELL ON THE JAPANESE ARMY IN MALAYA

1. Introduction

The following is a paraphrase of a statement concerning the Japanese Army made recently by General Sir Archibald Wavell, supreme commander of the forces of the United Nations in the Southwest Pacific:

2. Training in the Japanese Army

The main object of an army is to fight. This idea is the foundation of all training. The Japanese have demonstrated that they are always quick to take over any foreign techniques which fit their own characteristics and special requirements. In this regard it is evident that they have made a close examination of the Nazi battle experiences of 1939, and that they have applied these to their warfare in Asiatic countries in a way which has been well thought out. But it has been proved by the Japanese themselves that they are not mere imitators of the tactics and techniques of others.

3. Modern Military Techniques

The Japanese have made important advances in the development of landing techniques including the designing and manufacture of specially constructed landing-craft carriers, landing craft, and assault boats. [See MID Information Bulletin No. 7, January 24, 1942, Section I and illustrations.] The fundamental virtues of foot soldiers—in both fighting and marching—have always been instilled in the Japanese Army. At the same time dependence on motor transport is reduced to a minimum. Nevertheless, captured motor vehicles and locally procured bicycles are exploited. As a result of these principles and methods, a type of combat has developed that is peculiarly suited to Eastern Asia, the part of the world with which the Japanese are most familiar.

4. Modern Techniques Displayed in Malaya

(a) *Summary.*—In Malaya modern techniques have been displayed in the following ways:

(1) The cooperation of supporting arms with the infantry is close. This is true especially in the cooperative action of light artillery and mortars.

(2) The radiophone has been effectively used in air-ground communication. Proof of this is the rapid and effective support from the air, including tactical reconnaissance; and the fact that the army has its own air arm has facilitated this cooperation. Forward companies always use voice radio for air-ground communication.

(3) Artificial battle noises, made by live mortar bombs and firecrackers, have been used to mislead their opponents as to the point of the main attack.

(4) Firing positions in trees are used to gain advantage over ground-bound opponents.

(5) In the jungle type of warfare which the Japanese have been carrying on, they have demonstrated the ability to move despite the lack of roads.

All of these factors are important in jungle country, where there is always poor visibility.

(h) *Japanese Engineering.*—Among other improved techniques of the Japanese is the skill they have shown in repairing demolished bridges. Speedy advances have been successfully made by reason of their ability to remove obstacles from their path, especially where tank units are advancing. Such achievements reflect the thorough training of their engineering units.

5. Discipline and Morale of Japanese Soldiers

(a) *Discipline.*—The Japanese have a high standard of internal discipline in their army, a fact borne out by their conduct among themselves, as well as the relationship between subordinates and superiors, which is evident in such things as the salute. External discipline, however, is not so well maintained, as, for instance, in their details of dress and in their conduct towards civilians. Manifestations of a competitive spirit and rivalry between army units are discouraged to the point of being almost nonexistent. Loyalty to the Emperor of Japan is the foundation of a strong tradition, and the basis of Japanese morale is the spirit of offense or attack, which is in harmony with this loyalty. To the Japanese soldier it is a privilege to belong in the army, in spite of the fact that there are no allowances such as large pay and good rations. In fact, a hard and strenuous life, on the contrary, is enforced as being the best way of maintaining discipline and high morale.

(b) *The Japanese Fighting Machine.*—All these virtues of the individual soldier have been brought out in Malaya, where the Japanese Army has demonstrated that it is a formidable fighting machine, highly capable of fitting modern tactics to rapidly shifting conditions.

(c) *Reasons for Japanese Success in Malaya.*—Underlying the success of the enemy forces in Malaya are:

- (1) Previous war experience;
- (2) Good discipline and high morale;
- (3) A high standard of training.

The possession of tanks and superiority in the air are other factors which have contributed their measure to success. There is a strong probability, however, that the Japanese divisions which were sent on the Malayan expedition were better trained than any other divisions in their army.

(End of General Wavell's Statement)

SECTION II

ORGANIZATION AND TACTICS OF THE JAPANESE PLATOON AND SECTION ON THE MALAYAN FRONT¹

1. The Infantry Platoon

(a) *Organization.*—The platoon consists of 42 men. It has four sections of 10 men each, and a platoon commander who is a second lieutenant, and a noncommissioned communications officer (*Reirakikashi*). No. 1 section usually is commanded by a sergeant, and Nos. 2, 3, and 4 are commanded by corporals. The platoon commander gives all orders for sections; for instance, such as "Section 1, Advance," "Section 2, Advance." There are three platoons in each company.

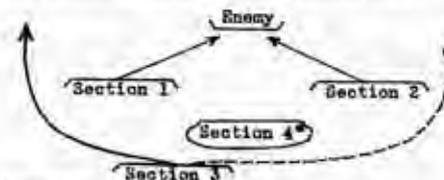
(b) *Armament.*—The first three sections of the platoon are armed with rifles, and the fourth, the Grenade Discharger (*Tekidanto*) Section, is armed with three grenade dischargers. Each rifle section is armed with one light machine gun, and has a machine gunner, two men who carry ammunition, and seven riflemen. There are no organized subsections and the light machine gun group is not intended to be split for action. No "tommy gun" is included in the section armament. Hand grenades are carried by all. In the Grenade Discharger Section, one man carries and fires each discharger, and two men, armed with rifles, carry ammunition for each weapon. Again, this section is not intended to be split but to be used as a unit reserve of fire power.

(c) *Intercommunication.*—The noncommissioned communications officer of the platoon maintains intercommunication between sections by visual means or by using soldiers as runners. The runners may use bicycles if the sections are not widely separated and if the terrain permits. (In China, bicycles have been used for intercommunication, especially between units up to the size of a company.) Regimental radio communication usually goes down as far as the company headquarters, which has a pool of 13 runners for communication up down to the platoons.

(d) *Antitank Defense.*—The Japanese platoons in Malaya apparently did not use antitank rifles. Instead, they used a variety of antitank bombs (*Hakubakurai*, *Kyuchaku*, *Bakurai*, *Kaubin*) and time bombs. The bombs undoubtedly were effective in close country, but in open country where close approach is impossible they would be useless. Some of these bombs are carried in the No. 1 Section, but how many and by whom is not known.

2. The Infantry Section

(a) *Tactics in Battle.*—(1) According to prisoners, figure 1 shows the most frequently used platoon employment of sections carried out by the Japanese in Malaya:



* Armed with grenade dischargers (reserve fire power).

Figure 1.

¹ Most of the information contained in Section II was obtained from prisoners of war. Its reliability is unassailable.

(2) Sections 1 and 2 of figure 1 make frontal assaults on the enemy. Section 3 attacks the enemy's flanks at a given time. The section rarely ever divides into subsections to attack both of the enemy's flanks at a given time, because (a) of the danger of hitting their own men by cross fire from two flanks, and because (b) of the danger of weakening section strength by splitting into subsections, particularly since there is only one light machine gun to a section. The Japanese have tried splitting a section but with very little success. In this case, for instance, Section 3 may be divided into one big subsection and one small subsection. Thus divided, the smaller subsection is used more as a decoy than for attack. The subdivision is seldom used because of unsuccessful results.

(3) The Grenade Discharger Section, No. 4, usually operates in a reserve fire-power position. It is usually located in the center of the formation, between and slightly to the rear of Sections 1 and 2.

(4) The light machine guns of the first three sections are used only in front and hardly ever as reserve fire power.

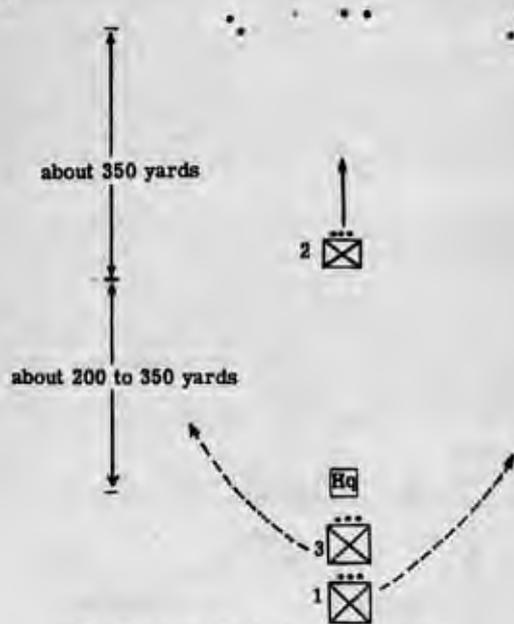


Figure 2.—Approach March of Japanese Infantry Company

¹ See photograph of a group of grenade throwers, figure 1, in Information Bulletin No. 4, January 9, 1942.

3. The Approach March

(a) *The Company*.—The Japanese infantry company uses roads in the approach march (fig. 2) until contact with the enemy is made. The leading element of the company consists of six scouts, who range about 350 yards ahead of No. 2 platoon. Back of this platoon by 200 to 350 yards is company headquarters, which is followed closely by No. 3 platoon and then No. 1 platoon.

(b) *The Platoon*.—The platoon also uses the roads in the approach march, if roads are available, even up to the time when contact is made. Usually one section travels along the edges of the road and the other sections travel under cover as far as possible on each flank. According to one prisoner, scouts are used to locate hostile positions, but upon locating them return to the sections for the attack.

4. Bivouacking

The Japanese troops often dig their own trenches (called *Go*) for use during the night. The trench is a box-like affair with space for only one person. Sentries are posted within a radius of 60 to 125 yards of the camp.

5. Transportation

(a) *Motor Transport*.—Motor transport is used mainly for the transportation of troops and supplies, which include ammunition. One prisoner of war stated that he traveled on motor transport most of the way from the Thai border deep into Malaya, adding that a short distance of the way was traversed on a bicycle and that only very little walking was done. There is no platoon truck. The individual soldier carries all of his equipment, which includes digging tools.

(b) *Motorcycles*.—The normal platoon organization does not include motorcycles.

(c) *Bicycles*.—Bicycles are used mainly as a means of transport. Illustrative of this, one Japanese battalion was transported as follows: two companies on bicycles and one company on motor transports. When the two companies on bicycles became tired, the personnel swapped places with the motor transport riders. (Bicycle troops are organized separately from the infantry.)

6. Night Operations

When night operations are used, the formation of the sections is much closer than in daytime operations because of the fear of losing contact. The stress in night operations is put on surprise, which is gained by outflanking and by silent movement. Weapons are of minor importance compared to the approach crawl, used until the enemy can be leapt upon. For instance, in the attack on the Kota Bahru airdrome the whole area was surrounded by Japanese who crawled through rice fields up to the actual perimeter of the field and guard posts. Some of the posts were overpowered with scarcely any shooting.

7. Messing

The independent mobility of the Japanese is assisted greatly by simplification of messing arrangements. Each man carries in a sack on his back 1 day's emergency rations and a 5 days' supply of rice. Since each is responsible for his own cooking, there is no waiting for hot meals to be brought up. Generally, the men of a section cook their food on a cooperative basis. No special cooking stove or other cooking apparatus is carried. Often a fire is made only once a day, in the morning, when enough food is cooked to last for the day. To a considerable extent, the soldiers live off the country. The quality of rations deteriorates as operations develop in intensity and often rice and salt are the only foods. Sugar usually is procured locally and it is a luxury for the Japanese Army.

SECTION III

INFORMATION UPON VARIOUS ITEMS OF JAPANESE MATÉRIEL

I. A New Type of Japanese Light Machine Gun (illustrated on the cover)

(a) *Acquired Weapon*.—During recent operations in Malaya the British captured the new type of Japanese light machine gun pictured upon the front cover of this bulletin. Since this gun may be fired from a position which is generally used in firing a Thompson submachine gun, it is believed that this new gun may have been erroneously referred to as a "tommy gun" in previous reports on Japanese tactics.

(b) *Characteristics of the Gun*.—Some of the characteristics of this new gun appear to be:

(1) It is gas-operated and magazine-fed and is patterned after the British Bren gun and the French Hotchkiss light machine gun. The magazine has a capacity of approximately 30 rounds. The cartridge has a rim instead of the American type of cannelure.

(2) The gun is provided with a bipod which is attached about 6 inches from the muzzle on the gas-cylinder bracket. The bipod height is approximately 16 inches. The barrel weight is approximately 5½ pounds. A carrying handle is provided in front of the magazine. The barrel most likely detaches from the receiver by means of rotating the carrying handle.

(3) The weight of the gun is between 22 and 25 pounds. The sights are offset so as to clear the magazine and carrying handle. A sling attached to the butt stock and to the gas-cylinder bracket is provided for carrying the weight from the shoulder. The barrel is provided with an angular groove similar to the Hotchkiss gun. This gun could be used also in the 6.5-mm caliber. However, the curved magazine in the photograph indicates that the model shown is a 7.7-mm. The barrel length apparently is between 24 and 26 inches.

(4) The special stock, of the drop type, is attached to the trigger guard and the stock has a crescent shape on the rear for placing it partially over the shoulder.

(5) A bayonet lug is provided at the forward end of the gas-cylinder regulator for mounting the rifle bayonet.

(6) The head of the bipod is provided with two positions: one, a folding position, the other, a position with the bipod perpendicular to the gun barrel. The arrangement of the carrying handle for detaching the barrel is similar to the type used on the French Hotchkiss and that used on the Bren gun. However, the open side of the handle extends to the front instead of to the rear as used on the Bren gun.

(7) The bipod does not have an adjustment for height. Both the Bren and the U. S. Browning Automatic Rifle, M1918A2, have adjustments for the bipod legs so that it can be set at different heights.

(8) The receiver of the new gun is somewhat more complicated than the Bren, owing to many irregular contours. The whole arrangement is considerably more complicated than the automatic rifle, A2, and would require at least 50 percent more time to manufacture.

(9) No flash hider is shown on the gun, whereas a flash hider is provided as part of the Bren gun assembly.

(10) Some of the features, such as the buffer and the rear-sight adjusting means, are patterned somewhat after the Bren design. However, basically, they are nearer a copy of the French Hotchkiss.

(11) The charging arrangement is on the left-hand side of the gun and is of the general type used by the Bren and the Hotchkiss.

(12) The photographs are not sufficient in detail to identify definitely the trigger mechanism. However, the buttons indicate that the gun can be fired either automatically or semiautomatically.

(13) The photographs do not show that any provision has been made for mounting this gun on a tripod or for antiaircraft firing.

(14) The type of bayonet used is very similar to the U. S. M1917.

(15) The overall length is probably between 41 and 43 inches, including butt stock.

2. Fighter Planes

(a) *New Type*.—Over the Dutch East Indies the Japanese are using a new fighter plane which is believed to be the new Nakajima O1. Its use has not been reported previously. The plane is said to have a top speed of 295 miles per hour. It is a low wing monoplane of the pursuit type, and it is armed with four machine guns and two 20-mm cannons. It has a 14-cylinder air-cooled engine. The plane is of light construction with a retractable tail-wheel and landing gear. It is single-seated and can carry a reserve gasoline tank, which may be dropped. The fighter has a high climbing speed.

(b) *Type 97*.—The Japanese Army type 97 fighter plane has a gasoline capacity of 136 gallons, it was disclosed recently in examination of one which had been shot down in the Kangoon area. The plane, manufactured in November 1941, carries 70 gallons in a fixed tank and 66 gallons in a tank which can be dropped from the plane when desirable.

(c) *Detachable Gasoline Tank*.—The extra, detachable gasoline tank being used by the Japanese on their pursuit planes is calculated roughly to increase the range of the planes by 260 miles.

(d) *Fighter Patrols*.—Fighter patrols of the Japanese were kept continually in the air to protect their columns of troops in Malaya.

3. Bombs

(a) *Varieties*.—Japanese bombs are of two varieties, army and naval. Army bombs have been mostly manufactured in the Osaka arsenals. Naval bombs have been mostly manufactured in the Kure and Yokosuka arsenals.

(b) *Construction*.—The bombs that the Japanese have been using generally are divided into nose, body, and tail, either welded together or, in addition to welding, riveted, screwed, or doublescrewed together. None of their bombs is cast or forged in one piece. Furthermore, these three parts are of different thickness, naturally with different degrees of fragmentation. The point of weld or riveting is the weakest point in the bomb. This accounts for the fact that bombs seldom have uniform fragmentation. Either the nose or the nose and the tail (in the case of tail fuses) detonate, but the body rarely ever does, especially in the case of the larger bombs. Poor detonation is not infrequent. Scattered powder, large fragments, or undetonated bomb bodies are found near the bomb craters after a bombardment.

(c) *Aerial Bombs in the Philippines*.—White phosphorus is being employed in the Philippines by the Japanese in their aerial bombs as a filler for its incendiary effect.

4. Observation Balloons

Shortly before crossing the Johore Straits onto Singapore Island, the Japanese used observation balloons for the first time in the Malayan Campaign—three were seen in Johore on February 7.

5. Artillery

When the Japanese reached the Straits of Johore, they increased considerably their use of artillery fire and also brought into action guns of a heavier caliber.

6. Grenades

(a) *Hand Grenades.*—It is believed that the Japanese are using two types of hand grenades. The "91 Type" and the "97 Type," both of which have cylindrical shape. The "91 Type" has a time fuze of 6 to 7 seconds, and the "97 Type" is fired by the percussion created when the grenade strikes its object.

To ignite the time-fuze of the "91 Type," a safety pin is removed and a sharp tap is given on some hard surfaces, such as the heel of a boot. This causes a firing pin inside the grenade to hit a percussion cap which ignites the fuze. The "91 Type" weighs, it is believed, a little less than 1 pound. The "97 Type" is reported to be slightly heavier, but further details are not known.

(b) *Stick Grenades.*—This grenade is made up of a cylindrical cast-iron pot which is 2 inches long, 2 inches outside diameter, and 1½ inches inside diameter. It is open at one end and closed at the other and is of uniform thickness. Inserted in this shell is a charge consisting of 2 ounces of lyddite in the form of a plug with a hole through the center to receive a detonator. It is covered by a thick paper cylinder to prevent the charge from coming in contact with either the detonator or the cast-iron shell. This charge is 2 inches long, and the detonator hole ¼ inch in diameter. A wooden handle is placed into the top of the iron cylinder to a depth of ¼ inch, and it is secured by three small screws which pass through the iron shell. This handle is 5 inches long and is drilled lengthwise through the cylinder with a ¼-inch hole.

The detonator is 2¼ inches long, ¼-inch outside diameter, and is made of brass. It is attached to one end of a 4-second fuze and is inserted at the other end of the fuze into an igniter, which is attached by three lugs to the wooden handle. The igniter consists of a thin paper cylinder with a diameter of ¼ inch, and the ring is 1¼ inches. The grenade is believed to weigh about 1 pound 3½ ounces.

To disarm the grenade, the following procedure should be followed:

1. First remove the wax from around the joint between the handle and the iron shell and locate the three screws around the circumference at the top of the iron shell and remove them.
2. Hold the grenade by the handle with the iron shell downwards, and, using a light metal dolly and hammer, tap all around the top edge of the shell, which will then drop off the handle.
3. Remove the lyddite by inverting the shell and tapping it slightly.
4. Remove the screwed metal cap on the top of the wooden handle and cut the cord away from the ring.
5. Using a round piece of ¼-inch iron about 6 inches long, insert it down the handle along the side of the cord and push out the detonator fuze and igniter complete. Thenceforth the grenade is not dangerous.

7. Grenade Dischargers

In Malaya the Japanese used two types of grenade dischargers. One of these types has not been described previously. Known as the "10-year Type," Model 1921, it has the following characteristics:

Caliber.....	50-mm (1.97 in.).
Length (overall).....	1 foot 8 inches.
Barrel.....	smooth bore.
Length of barrel.....	10 inches.
Weight unloaded.....	5½ pounds.
Range.....	65-250 yards.
Transport.....	carried on the man.

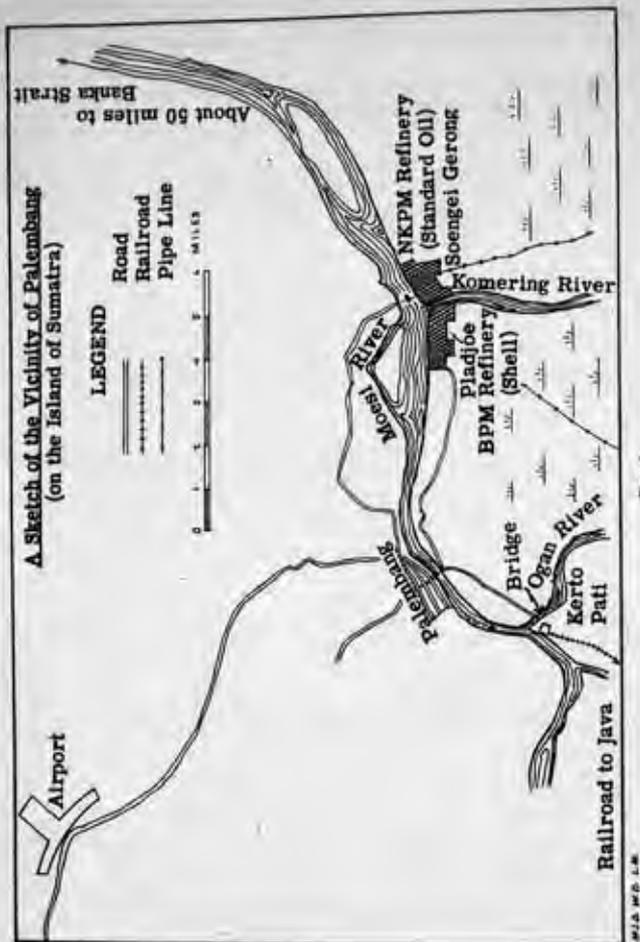
The grenade discharger is muzzle-loaded and is fired by a striker operated by a lever on the outside of the discharger body. The discharger is fired from the ground, where it rests on a small base plate. No bipod attachments were used.

The discharger fires hand grenades which weigh a little less than 1 pound. Before the grenades are fired in the discharger, a special attachment is screwed into the grenade base. The attachment consists of a percussion cap and propellant (believed to be ballistite). The safety pin in the grenade is removed before insertion into the barrel of the discharger, and the shock of the discharge has the same effect as tapping the grenade when thrown by hand.

8. Revolvers

The Japanese used two types of service revolvers in the Malayan Campaign. One, known as the pattern "14 Type," is of 8-mm (.312 in.) caliber.





SECTION IV

THE JAPANESE PARACHUTE ATTACK UPON PALEMBANG¹

1. Large-Scale Use of Parachutists

The Japanese used parachute troops for the first time on a large scale on February 14, when a total of 700 were dropped around Palembang, a large oil-refining center in south Sumatra. The position of Palembang in relation to its airport, oil refineries, the Moei River, and roads in that area are shown in figure 3.

2. Defeat of the Parachutists

(a) *Landings*.—The 700 men were dropped from 100 aircraft, several of which were Hudsons with British identifications. Armed with light mortars and submachine guns, the parachutists landed in three groups. One hundred men dropped to the earth close to the Standard oil refinery (Soengei Gerong), which is located on the Moei River below and east of Palembang. Three hundred landed close to the Shell oil refineries, immediately west of the Standard oil plants, and another 300 landed near the Palembang airdrome number 1, which is northwest of the city.

(b) *Mission*.—The mission of the Japanese parachutists was to capture the flying field and the oil refineries. They apparently were seeking to prevent the defending Dutch troops from destroying the refineries. The mission failed, for two reasons:

1. The Japanese employed too small a force;

2. Although they used two waves of parachutists, it was not until the following night, February 15/16, that supporting landings from the sea occurred. The lack of attacking strength was probably due to the fact that the Japanese did not know that 2 days before the attack the Dutch had doubled the garrison in Palembang, bringing it up to two battalions. Between the time the parachutists landed and the arrival of Japanese sea forces, the Dutch destroyed the oil refineries and killed or captured practically all the parachutists. The only useful purpose that the parachute raids may have served was the extent of interference and the delay caused in demolition work at the airdrome. The demolition work had to be halted while the Dutch forces engaged the parachutists, and by the time the parachutists had been conquered Japanese sea-borne forces captured the city. The Japanese claim that little damage was done to the airfield.

(c) *Sea-borne Invasion*.—The Japanese sent by sea a huge convoy of troops who took over Palembang on the night of February 15. The troops came up the Moei River, which is very wide and deep, in small craft and motorboats. The first group passed beyond the city before landing. This group was followed shortly afterwards by reinforcements which overwhelmed and forced the smaller defending forces to retire.

¹ See Section IV, WD Training Circular No. 75, 1941, for details regarding air-borne troops and parachutists.



JAPANESE TWO-MAN TANKETTE

Observe: (1) Relative size of man and tank; (2) Driver's port open; (3) Bogie wheels; (4) One gun in turret

This is a light armored vehicle, weighing about 3 tons, called Ishikawajima Tankette, M2592 (1932). It is often used with an armored trailer for supply and intercommunication. Its maximum speed is 30 mph. Its dimensions are: length 10' 2", width 5' 9", height 5' 4".



JAPANESE PRACTICING MOVEMENT OVER DIFFICULT TERRAIN

Observe: (1) Camouflage nets on helmets and bodies, (2) Intrenching shovel on soldier's back

This picture shows a drill being conducted at the Japanese Infantry School in Tokyo. The wheels appear to be part of the 70-mm infantry-accompanying gun, Model 92.



JAPANESE FIRING RIFLES FROM TRUCKS

Observe: (1) Tarpslins removed; (2) Pocks slung on vehicle's side; (3) Standing position of the troops; (4) Position of platforms in trucks; (5) Nomuse of rifle sling; (6) Type of target presented by these soldiers; (7) Light machine gun in rear truck
This picture reveals that the Japanese are aware of the necessity of training men (while being carried in vehicles) to bring fire on an enemy quickly.



A JAPANESE MOTOR PARK

Observe: (1) Mass parking in regular formation; (2) Woods in the rear; (3) Coverings thrown over hoods and windshields. This area is probably a bivouac. Coverings thrown over hoods and windshields prevent reflection of light and may also serve to keep motors dry.



JAPANESE TANK ON IMPROVISED BRIDGE

Observe: (1) Partly reconstructed bridge; (2) Supplies tied to rear of tank

The Japanese have shown skill in repairing demolished bridges. Their ability to remove obstacles and their daring contribute to the successful advances of the tank units. The tank shown in action here is probably Medium Tank, M2591 (1934).



JAPANESE TANKETTE, TRAILER, AND MOUNTED MEN

Observer: (1) Relative sizes of tankette and trailer; (2) Number of bogie wheels on tankette and its trailer; (3) Open driver's port.
The tank is probably the Ishikawajima Tankette, M2592 (1932).

RESTRICTED

MID 319.1 No. 639 M.I.D., W.D. 11:00 A.M., February 22, 1942.
 Situation B-11-41

SITUATION REPORTI. Pacific Theater.

Philippines: There were no new developments on Bataan. Fighting has become temporarily positional. Artillery dueling continues between our harbor forts and the enemy's Cavite shore batteries. Burma: Despite small enemy penetration on Bilin river, there were no important changes in the situation. Rangoon has been partly evacuated; those remaining have been urged by the Governor to put up a last ditch fight. Bombing of Bassein and Rangoon-Mandalay Railway are reported. Japanese push seems directed toward Sittang River, the last barrier between them and above railway. Bali: The battle of Bali continues and is believed to be greater than the Battle of the Macassar Straits. Three enemy naval vessels sunk; five damaged. One transport sunk and several damaged. Australia: All ferry traffic discontinued from Australia, according to ABDA Command.

II. Eastern Theater.

Hard fighting continues along the general front. There is no reported change in situation. (A situation map will not be issued this date.)

Air: German Stukas attacked Murmansk railroad line at several points.

III. Western Theater.

No land activity reported.

Air: British planes raided western Germany and laid mines in North Sea.

IV. Middle East Theater:

No change in general situation.

Air: German bombers attacked shipping in Tobruk harbor and mechanized columns in the Libyan desert. Malta bombed again, hits scored on airdromes and barracks.

RESTRICTED

TREASURY DEPARTMENT
WashingtonFOR RELEASE, MORNING NEWSPAPERS,
Monday, February 23, 1942.Press Service
No. 30-42

Secretary Morgenthau last night received a pledge for the purchase of \$1,000,000,000 in Defense Bonds during 1942 by the 5,000,000 members of the American Federation of Labor.

In a special radio program, William Green, the Federation president, told the Secretary that the workers in whose behalf he was speaking would "invest one billion dollars of their hard-earned wages this year for victory in the war." Mass meetings of AFL unions throughout the country listened to the talks by Mr. Green and Secretary Morgenthau.

"I am confident," said Mr. Green, "that every member of the American Federation of Labor will live up to this patriotic obligation and even go beyond it to assure the success of our vital campaign." He announced that already this year AFL members have purchased or subscribed for a total of more than \$200,000,000 worth of Defense Bonds.

Secretary Morgenthau called the pledge "a magnificent example to the whole country" and pointed out it was the largest pledge to come to the Treasury from any single organization.

"Organized labor in this country," the Secretary declared, "has always recognized fascism for what it is, and has known from the beginning that the fascist system was a deadly menace to our free institutions.

"We know now that we are not safe even here in America. We know that unless we and our allies win this war there will be no survival of free trade unions, no liberation of the millions of workers now enslaved abroad, no continuance of the rights that we have won in generations of struggle here at home, no chance to win a better future for the working men and women of the world."

The Secretary pointed out that "it may not be dramatic to set aside a part of your pay each week for bonds, but it is tremendously important to the success of the war effort as a whole, and it is something that can be done by everyone who earns a regular income."

He conceded that the people of America had not yet "made a paradise of this free country of ours" but argued that we "have always been moving forward on the eternal quest for a better and broader and more secure future for ourselves and our children."

TREASURY DEPARTMENT
Washington

17

FOR RELEASE, MORNING NEWSPAPERS,
Monday, February 23, 1942.

Press Service
No. 30-41

(The following address by SECRETARY MORGENTHAU is scheduled to be broadcast over the Blue Network at 8:10 p.m., Eastern War Time, Sunday, February 22, 1942. Special mass meetings of American Federation of Labor unions all over the country will listen to the broadcast.)

President Green and members of the American Federation of Labor: This pledge of yours to buy a billion dollars of Defense Bonds in 1942 is a magnificent example to the whole country. It is the biggest pledge that has come to us from any single organization. It amounts to about \$200 for every one of your five million members. In fulfilling your pledge you will be giving still further proof that American labor is ready to do its utmost to win this war for freedom.

This war is a crisis for the American labor movement in more ways than one. We in this country have prided ourselves upon our freedom of speech and worship, our system of equal justice under law, our free public education and the limitless opportunity that our way of life provides. From these American freedoms the trade union movement has grown and made its influence for good a mighty force in the community.

We have not yet made a paradise of this free country of ours. I know that there are many injustices still to be righted. I know that millions among us still live in poverty through no fault of their own. I know that millions of our Negro people are still denied the free and equal opportunities to which our Constitution entitles them. I feel as humiliated as you do when I read that thousands of able and willing workers cannot find employment in war industries because of their nationality, race or religion.

All these faults and many more are undeniable; no one can honestly say that we have reached our destination. Nevertheless, we in this country have always been moving forward on the eternal quest for a better and broader and a more secure future for ourselves and our children.

That forward march has now been gravely imperilled by a combination of cruel and barbaric conquerors on other continents. They have begun by choking to death the free institutions of their own countries. They have abolished trade unions, they have perverted education and science, they have destroyed the rights and dignity of the individual, and they have re-established conditions of tyranny that we thought had passed forever from our kind of world. Not content with that, they have blotted out the independence of one free country after another. I shall not read the tragic list of countries, once as free as our own, which have had their peoples enslaved by these new forces of paganism and terror. Nor do I need to tell you in detail of the crimes committed and the miseries inflicted upon hundreds of millions in the name of the so-called "new order." You know them well, and you know how many workers in other countries have been imprisoned, tortured or killed--for no other reason than that they were members of labor unions. Organized labor, at least, never made the mistake of imagining that we could compromise with the authors of those crimes. Organized labor in this country has always recognized fascism for what it is, and has known from the beginning that the fascist system was a deadly menace to our free institutions.

Today, as you foresaw, the tide of fascist conquest and barbarism is sweeping the whole world. This evil thing in field-gray uniform and hob-nailed boots is creeping up, even on us in our sheltered continent. It has broken loose on both sides of us, across the Atlantic and Pacific.

We know now that we are not safe even here in America. We know that unless we and our allies win this war there will be no survival of free trade unions, no liberation of the millions of workers now enslaved abroad, no continuance of the rights that we have won in generations of struggle here at home, no chance to win a better future for the working men and women of the world.

As I have said repeatedly, this is not a token war. It cannot be fought or won by token effort. It is a war of desperate seriousness. It is so serious that it allows no margin of safety for any of us.

Organized labor has never underestimated the size or scale of the war effort that will be needed. Your unions, for example, long ago urged the quick conversion of our peacetime industries to war production, even though the effect would be temporary unemployment for large numbers of workers,

From now on the war effort on the home front will take many forms, among them the production of ever greater quantities of weapons, the conservation of materials, the acceptance of higher taxes, and the purchase of more and more Defense Bonds. It may not be dramatic to set aside a part of your pay each week for bonds, but it is tremendously important to the success of the war effort as a whole, and it is something that can be done by everyone who earns a regular income. I accept your pledge of a billion dollars as a demonstration that you will support the war effort with all your might, no matter how hard or how long the war may be.

You cannot set a price on the things for which America stands. You cannot measure their worth in terms of money or of sacrifice. They constitute a faith that is beyond price because it is worth more than life itself. It is a faith that Americans have fought for and died for, and they will do so again, for life without that faith would not be worth living. If Americans are to be true to themselves and to their future, they will fight and sweat and save, and exert every ounce of effort until victory is won.

-oOo-

February 23, 1942
10:20 a.m.

TAXES

Present: Mr. Sullivan
Mr. Paul
Mr. Tarleau
Mr. Blough

H.M.JR: Now, I thought I would start in this morning doing special privilege and hardship provisions. I thought I would do the ones the way you have got them listed.

MR. PAUL: We didn't finish the other day with the corporate picture.

H.M.JR: Didn't we?

MR. PAUL: No, we just covered the excess profits tax rates.

H.M.JR: Then let's finish that. What is left unfinished?

MR. PAUL: Well, even with those increased corporate rates, we don't get enough tax. The next point in the corporate structure is the increase in rate of the surtax; and, incidentally, perhaps too much in the interests of neatness, our structure proposes the increase of

- 2 -

the normal tax to twenty-five percent. Now, there is no point in that except that it makes a better, more convenient figure.

H.M.JR: What is it now?

MR. SULLIVAN: Twenty-four, but we do the very thing we said we weren't going to do, allow any increase in the normal tax and that gives an added advantage of one percent to the people who hold partially tax-exempt securities.

MR. TARLEAU: John, that is right, but it is an added advantage only in the sense that we are just rounding out a figure.

MR. SULLIVAN: That is right, and I say we shouldn't sacrifice a principle just in the interests of neatness, because it is easier to compute twenty-five percent than twenty-four.

MR. TARLEAU: If you think there is a lot of feeling of that kind, we ought to say twenty-four.

MR. SULLIVAN: Well, we have already stated that we weren't going to approve any increases in normal tax, Tom. Now, to be sure, this is a small increase, but it does violate the principle that we announced.

H.M.JR: Some of you men were here and heard John McKee about holding up my hand on what I said publicly. You heard it, Randolph. You were here when John McKee kept saying that.

MR. BLOUGH: On the bank expense business.

H.M.JR: No, not the bank expenses.

MR. PAUL: I must confess I never knew that chap's name. Everybody called him John. I didn't know who he was.

H.M.JR: No, the point wasn't just that. I mean,

- 3 -

this same thing applies.

MR. BLOUGH: That was the conference it was on. I was trying to recall it to his mind.

MR. PAUL: Yes.

H.M.JR: No, let me just put it this way, because I don't know all of these intricacies in this thing, and I don't want to know them. I think this is true. I don't care whether it is the banks or anybody else. I made a statement about not wanting to circumvent this and that and the other thing, and I meant it. You fellows have got to see that I live up to it by not suggesting something which will.

MR. PAUL: Well, we don't think that our proposed action does circumvent it. There is a difference of opinion there, but we can see how other people would get the idea.

H.M.JR: Well, that is enough.

MR. PAUL: No, I don't think so.

MR. TARLEAU: You mean about the bank expenses.

MR. SULLIVAN: Now you are talking about the bank expense.

H.M.JR: I am talking about from twenty-four to twenty-five.

MR. SULLIVAN: No, I am against that because that is going the other way. That is increasing the normal tax, which we said we wouldn't do.

MR. PAUL: This is of no importance. I am perfectly willing to keep it at twenty-four.

H.M.JR: When did I say that, John?

MR. SULLIVAN: In the conference in which I participated.

- 4 -

We said that we weren't going to ask that the normal tax be reduced because that would be doing by indirection that which we couldn't do openly, but that we would oppose any increase in the normal tax because that would be conferring an additional advantage on the holders of partially tax-exempt securities.

H.M.JR: When did I say that? When was that conference?

MR. PAUL: January 26.

MR. SULLIVAN: Yes. I said it.

H.M.JR: Oh, you said it? To whom?

MR. SULLIVAN: To the press. I was sitting beside you.

MR. BLOUGH: Well, it really wouldn't matter, so far as that is concerned.

MR. SULLIVAN: This would mean that the increase would be in the surtax rather than in the normal tax.

MR. PAUL: This is of no consequence here. We can put that percent on the surtax.

H.M.JR: Why does somebody raise it if it goes contrary to this statement of the twenty-sixth? That is what bothers me.

MR. PAUL: It is not a thing about which anybody is going to complain. It seems a better structure to us to have a normal tax of twenty-five percent, but - and nobody is going to complain when you make - when you go against your statement in favor of taxpayers; but, if you want to adhere strictly plus and minus to your statement, then all right, we can just put that percent on the surtax. It is up for discussion. We are not going against it.

H.M.JR: Well, I think we ought to stick pretty

- 5 -

closely to that thing. I mean, the argument of neatness is the weakest argument I have ever heard advanced on a tax proposal.

MR. BLOUGH: In other words, nobody thinks it matters, but does it look better at twenty-five than at twenty-four?

H.M.JR: Well, why not look better at thirty?

MR. TARLEAU: Thirty is a good figure and twenty-five is a good figure.

H.M.JR: But we are on record now. I take it this favors whom?

MR. SULLIVAN: The holders of partially tax-exempt Federal securities.

H.M.JR: Why should we favor them?

MR. SULLIVAN: I don't think we should, and I don't think in one tax bill we can be conferring an additional, although inconsequential, advantage on them, and--

MR. TARLEAU: John, you are stressing this thing way beyond its importance. We can drop it.

MR. SULLIVAN: That is what I think we should do.

MR. TARLEAU: You bring a lot of moral issues in, which I think is unnecessary. We can drop the idea and keep it at twenty-four.

MR. PAUL: Well, let's consider that. This isn't worth wasting much time on.

H.M.JR: Then what is the next thing?

MR. PAUL: That means we raise the present surtaxes seven percent, which we raised here to twenty-one percent, and we will have to shift that and raise it to twenty-two. Now, that is a flat raise of fifteen percent in surtax.

- 6 -

That means a total tax of forty percent.

H.M.JR: Where are you reading from?

MR. PAUL: I am reading from page twenty-four of your statement.

MR. BLOUGH: Or you can get it on page three of this summary, what is called the program. There is the program. Now, page three of the program.

H.M.JR: I see.

MR. PAUL: That contemplates a raise, normal twenty-four plus twenty-two, or forty-six percent. We would like to get that to forty-five, but we can't do it and make the answer come out right. We have one other idea we want to submit to you there.

H.M.JR: I am listening.

MR. PAUL: All right. You should take that surtax. That increases the tax on all corporations, flat rate. It is not just on excess profits. Now, in addition to that, we have, as part of the corporate structure, suggested a so-called war - special war tax which you see just below item fifteen on page three.

H.M.JR: I have got that.

MR. PAUL: Ten percent, allowing a tax credit of five percent of the amount by which the surtax net income of the taxable year is less than the average surtax net income of the years '36 to '39.

H.M.JR: Why can't you fellows ever suggest anything different? You just keep making the thing more and more difficult all the time.

MR. PAUL: Well, we could make it very much more simple--

H.M.JR: It is just like the Department of Agriculture,

- 7 -

just one layer on the other.

MR. BLOUGH: Stam made an interesting suggestion over the phone this morning, and that is that we take the surtax and war tax and combine them into one tax, and by adjusting the credit get the same result we wanted to get. We are working on that now, and it would be a simple matter, and that would simplify it. Then he added the advantage of calling everything except the normal tax either war tax or excess profits tax.

H.M.JR: Can't you call your surtax, the war tax?

MR. BLOUGH: It would then be the war tax.

MR. PAUL: Surtax has been in for some time.

H.M.JR: Well, like daylight saving time we changed to wartime, why can't you call your surtax the war tax, and keep the people thinking--

MR. BLOUGH: We could combine fifteen and sixteen into a war tax.

H.M.JR: That is the first time I ever agreed with Stam on anything, so I am most likely wrong.

MR. SULLIVAN: I don't think you are.

H.M.JR: I mean, at least it kids the people into thinking maybe when the war is over there wouldn't be that tax.

MR. PAUL: Well, of course that is the advantage of separating them.

- 8 -

H.M.JR: Make a note on this. When you get all through with all of these taxes, I want a comparable flat rate, one tax. How much would I have to have to raise the same amount of money, you see.

MR. PAUL: We can tell you approximately now, can't we?

MR. BLOUGH: Yes, we think it would be approximately 65 percent.

H.M.JR: When you get all through with that, I am going to have a real argument with you fellows.

MR. PAUL: All right.

MR. BLOUGH: I don't think the argument is so much with us as it is with some other people, labor unions and so forth.

MR. PAUL: Well, the argument is some with us. I don't believe in a flat tax.

MR. BLOUGH: I do.

H.M.JR: Well, I would like to take a look at it anyway.

MR. PAUL: I want you to understand in this war surtax, whether it be separate or combined with the old surtax, it is an attempt to get more or less the same result as we would have gotten by the reduction of the income credit from ninety-five to seventy-five percent.

H.M.JR: Well, aren't you doing that?

MR. PAUL: We are getting not quite the same result, but--

H.M.JR: Aren't you reducing it?

- 8 -

H.M.JR: Well, I can't take it.

MR. BLOUGH: People who would like to see lower corporate rates after the war, of which I am one - I would like to see it called the war surtax. Combine the two and call it war surtax.

H.M.JR: Well, work on it because I couldn't take another separate tax.

MR. PAUL: Of course, we are also advocating--

H.M.JR: The normal, surtax, the war tax - it is too much for me.

MR. PAUL: Let me say this just in defense of this. I think we can combine them, but one must remember that we have just developed this war tax idea as a compromise with Stam last Thursday so its simplicity will come with further development of the subject. We haven't under this structure any more war taxes than we had before, because we are recommending the elimination of the capital stock tax and the declared value excess profits tax.

H.R.JR: Well, that is a nuisance tax that has been eliminated.

MR. PAUL: It is a nuisance tax, but it is a fair amount of revenue. That is one reason why these rates are what they are.

MR. BLOUGH: I think it might be well if we might, Mr. Secretary, stress the idea that the war tax is to burden less heavily concerns which are now making less after excess profits tax than they did before the war. If the concern through priorities or something else has had its income go down, its tax rate can be lower than the concern whose income has stayed up or gone higher, and that is the notion underlying the war tax.

- 10 -

MR. PAUL: No.

H.M.JR: Why not?

MR. PAUL: This is in lieu of that.

H.M.JR: Oh, I wouldn't do that. Is that part of the trade?

MR. PAUL: That is part of - if you are going to take the seventy-five or any reduction of the income credit, you have got to have a long political battle over it. You can get this without a political battle.

H.M.JR: Can you get the same result?

MR. PAUL: Not exactly, but very much the same.

H.M.JR: Well, if you are going to have this excess profits tax - make sense to me by reducing this credit back from ninety-five to seventy-five, but I don't understand this.

MR. BLOUGH: May I speak on it just briefly?

H.M.JR: I wish you would. It sounds like a bum deal to me.

MR. BLOUGH: I think the reason there is so much opposition to lowering that ninety-five to seventy-five can be based on two psychological reasons. The first is that they are stubborn; and having stuck for it twice, they are going simply out of stubbornness to stick for it again. Maybe that is not a very good reason. The second reason is this, that they have been thinking in terms of an excess profits tax, a tax on something which is abnormal, a sort of a tax on something that is a little immoral. Now, when we lower the excess profits credit down to seventy-five percent, we certainly aren't saying that someone who made as much in this year as he made in the base period is getting it immorally or an abnormally high profit, and I think they feel a resentment

- 11 -

about calling that excess profits tax. Now, if we do the same thing and call it something else, they seem willing to take it. The real reason--

MR. PAUL: That is a face-saving device.

MR. BLOUGH: The reason this doesn't do quite the same as the other is because the rate isn't so high. By raising the rate higher and combining the surtax, you will get very much the same result.

H.M.JR: You haven't got any examples for me?

MR. BLOUGH: As to the comparison of the two?

H.M.JR: Well, take any company and run it through--

MR. BLOUGH: Yes, we have an example in here as to how it works, but not a comparison of the two.

H.M.JR: Could you sit down here and give me an example, the way it would work, the way it is set up here?

MR. BLOUGH: Surely.

H.M.JR: Come over here next to me.

MR. BLOUGH: Example eleven back here has that kind of a comparison worked out. Now, that first case - this happens to be the Coca-Cola Corporation. In 1940 it had a net income of thirty-five point eight million dollars. Now, it is a high profit company as you know, and would use the average earnings method. It had an excess profits credit of thirty point eight. Now, at the present time it would have a total normal tax, surtax and excess profits tax, of thirteen million dollars under present law, and we just put that out at the side. The present law is thirteen million.

- 12 -

H.M.JR: What?

MR. BLOUGH: Present law tax thirteen million dollars. Now, we would deduct the thirty-eight from the thirty-five eight, and we get five billion dollars--

H.M.JR: This is their profits?

MR. BLOUGH: This is their income, and this is their profit and this is the credit, their excess profits credit on ninety-five percent basis, yes. They would have an excess profits income subject to tax of five million dollars.

H.M.JR: That isn't excess profits is it?

MR. BLOUGH: No, this is their current year. This is this year's income, the tax on their 1940 income. This is the base period credit.

H.M.JR: I see. They start with five million?

MR. BLOUGH: So they have excess profits of five million. Now, we propose a top rate of seventy-five percent and figuring it - not all of that is at the top rate, so it makes three and a half million dollars excess profits tax. Now, the three and a half million dollars excess profits tax--

H.M.JR: That isn't the present thing now, that is what you propose, isn't it?

MR. BLOUGH: That is right. the present rates would be less than three million out of this thirteen million. We take the thirty-five, eight, deduct the three five from it. That is this income. This is the excess profits tax. We get thirty-two point three million dollars, which is the income after excess profits tax. Now, the normal and surtax under present law would be fourteen million nine. That is the twenty-four percent--I mean under our proposed rates, I am sorry, not under our present law but under our proposed rates of twenty-five percent normal and twenty-one per-

- 13 -

cent surtax. We get fourteen point nine million. Now, in addition to that it would pay a special war surtax of three point two million dollars, which is ten percent of thirty-two point three. Now, this company having made more than it made in the base period, doesn't get any benefit of the reduction due to the fact that its credit has gone down - I am sorry, that its income has gone down. It doesn't get any benefit of that, so it pays at the full three and two tenths - full ten percent or it pays three and two tenths percent million. So we have a total tax of three and a half million excess profits tax, fourteen point nine million normal tax and three point two million war-tax, so that Coca-Cola would pay twenty-one point six million out of thirty-five point eight tenths million of income, compared to thirteen million back here under the present law so its tax under our proposal would be raised eight and six tenths million dollars.

H.M.JR: Just divide thirty-five point eight into twenty-one point six and see what you get.

MR. BLOUGH: It is about sixty percent. It is a little less than sixty. It is sixty and four-tenths percent.

H.M.JR: If there is a flat tax?

MR. BLOUGH: If there is a flat tax--

H.M.JR: If it went to sixty-five they would pay more.

MR. BLOUGH: If it were sixty-five, they would pay more, that is correct.

H.M.JR: And George would be for a flat tax, as I understand.

MR. PAUL: I think he would, but generally speaking, the high profit corporations would pay less.

- 14 -

MR. BLOUGH: Of course he expects Coca-Cola to go down. He expects Coca-Cola to make less, does he not?

MR. TARLEAU: Yes, because of the sugar. Mr. Secretary, the spread between the high profit of Coca-Cola and the others is cut down by these changes. The spread now is between sixty-five and - what is it that we got, Roy, sixty? Sixty point four, isn't it?

MR. BLOUGH: Yes.

MR. TARLEAU: So that we are cutting down the difference between Coca-Cola's tax with a benefit of ninety-five percent credit and the average corporation. They are closer together now because of this war tax.

H.M.JR: Well, this would be from ninety-five to seventy-five. This isn't fair--

MR. SULLIVAN: No, it is not.

H.M.JR: They don't want this.

MR. SULLIVAN: No, that isn't on the basis of the reduction.

H.M.JR: Well, he had seventy-five.

MR. BLOUGH: I am sorry, that was the rate of tax. That is one trouble with the seventy-five. You see, this is not the seventy-five percent credit. This is the seventy-five percent tax rate.

H.M.JR: Oh.

MR. BLOUGH: I am very sorry, Mr. Secretary. We have gotten those two seventy-five's in the picture.

H.M.JR: What is the seventy-five you are using?

MR. BLOUGH: The seventy-five I am using there is the maximum rate of tax we propose or suggest that the--

- 15 -

MR. PAUL: "hat is the difference, Roy, between the seventy-five under our scheme? It can easily be changed. Between cutting the credit to seventy-five and this proposal.

MR. BLOUGH: It is almost impossible to compare them because you would have to make other changes in the other rates, but as I recall, it is somewhat higher than this, a million or two dollars higher than this.

H.M.JR: Have you got an example? For instance, for a steel company or an airplane company?

MR. BLOUGH: Let's see whether this one has one. Here is Curtiss-Wright.

H.M.JR: All right, what page is that.

MR. BLOUGH: That is the next page.

H.M.JR: We will take that.

MR. BLOUGH: We probably should have had this out in a little table. It is written out in text form.

H.M.JR: You have got to do it on a piece of paper for me.

- 15 -

MR. BLOUGH: Its net income, 1940, is twenty-six million. It didn't have any base period earnings to amount to anything, so it used the invested capital method, and it had a credit under invested capital of eight million, which means it had eighteen million dollars excess profits. Now, under present law, its tax is fifteen point three. We will put that out at the side. Now, under the proposal with excess profits of eighteen million, the excess profits tax, using the present method, which would use the eighteen million but would apply higher rates than are now applied, the excess profits tax would be thirteen point two million dollars. Now, the thirteen point two subtracted from the twenty-six point eight leaves twelve point eight million dollars subject to normal and surtax. We get that by subtracting the thirteen, two from this net income up here and the normal and surtax then, under the proposal, would be five point nine million dollars, and this company then would pay the special ten percent war tax, and it would have no relief because its profits are greater than they were in the earlier years, so it would pay ten percent of thirteen point two million or one point three million war tax, so that you would have total taxes of normal and surtax five nine, war tax one three, excess profits thirteen two, total tax twenty point four million dollars, total tax.

H.M.JR: As opposed to--

MR. BLOUGH: As opposed to a present tax of fifteen point three million dollars.

H.M.JR: That is a very high percentage.

MR. BLOUGH: Seventy-eight and three-tenths percent of twenty-six million dollars, and under the present law it pays fifty-nine percent. Of course it is one of those companies whose profits have gone up by leaps and bounds in the last few years.

MR. PAUL: That is one of the companies on the other side. That is above the sixty-five percent, you see.

MR. BLOUGH: Those are all the illustrations of that we had. I would be very glad to work out in table form - I can see that the text doesn't work. I can have it set up in a little schedule for you.

H.M.JR: Has this got two examples?

MR. BLOUGH: There are two there, that is right.

H.M.JR: It is not enough.

MR. BLOUGH: Well, we have a lot more. I just don't happen to have them with me.

H.M.JR: Give me one on U. S. Steel, for instance. Not now.

MR. BLOUGH: Well, I have the materials in the other book.

H.M.JR: Well, you can give it to me. Where do you stand on this, John?

MR. SULLIVAN: On this device?

H.M.JR: Yes.

MR. SULLIVAN: I think you mean as compared with going after the reduction from ninety-five to seventy-five percent.

H.M.JR: Yes.

MR. SULLIVAN: They haven't changed up there, sir. They haven't changed and at the conference at Senator George's apartment last week it was very evident that they did not intend to change. Stamm and Doughton are adamant, and George is playing with them.

H.M.JR: Well, doing it this way, how much of a concession is this?

- 18 -

MR. SULLIVAN: This is the same thing as a flat increase in your corporate rate with a provision for the benefit of the company that is making less money now than it made in the four base period years.

H.M.JR: You mean it takes care of those that are making less money now?

MR. SULLIVAN: Those who are making less money will not pay as much in increased taxes as those who are making more money.

MR. PAUL: That is getting away from the advice of the flat sixty-five percent tax.

H.M.JR: Well, that is good. I mean, if the companies that are making less money now shouldn't be hit as hard as those that are making more.

MR. PAUL: That is our whole idea. That is why we were trying to get the ninety-five down to seventy-five. This is just another device of doing the same thing. Now, the answer doesn't come out precisely the same in every case.

H.M.JR: But they will take this?

MR. PAUL: They will take this and we will get our three billion.

H.M.JR: That just makes the thing that much - but if you did the other thing - supposing we came out with the other thing. Then they would lick us and give us this, maybe?

MR. PAUL: I don't know. We would stir up a lot of trouble. We have got enough trouble on other points, I think. We have had trouble on the tax-exempts and sales tax, and since we get here substantially our point of favoring the companies that are making less money, which is what we have been essentially trying to do right along, I think this is a happy formula which saves the face of our opponents and gets us what we want.

- 19 -

H.M.JR: Well, this is the first time I have heard it, and it has soaked in. These other things I have heard before and this one I haven't.

MR. PAUL: Well, this is all very recent.

H.M.JR: Now, let's just pass this. What else have you got?

MR. PAUL: Well, that is the corporate picture. We have a question of relief for corporations which is quite important.

H.M.JR: What is that?

MR. PAUL: Well, that is your favorite baby, Tommy. I think you and John had some disagreement about that. The idea is to provide very generous relief to the company which has any abnormality about its base, not the invested capital base, but the income base. For instance--

H.M.JR: I am listening.

MR. PAUL: For instance, in the years 1936 to 1939, some industries weren't representative of their true earning capacity. That would be true, for instance, of the machine tool industry which made no money then, all cyclical industries. Now, taking your income credit, and this relief we will admit that that doesn't always do justice in exceptional cases, and one of our thoughts was to have a special board in the Treasury to administer relief. They are a very difficult type of case. The board would have to have a great sense of fairness and discretion. We had something somewhat like it in the old war tax, and it wasn't administered then too happily, but I think that was because we had a Harding and Coolidge administration. To have some generous relief provision means--

H.M.JR: But haven't these people all come down? I mean, it is going to be discretionary with us.

- 20 -

MR. PAUL: We were thinking of establishing a special board for that purpose. Well, if you don't do that you are going to have great trouble getting an acceptance by the corporate world of any such rates as seventy-five percent.

H.M.JR: What kind of relief would you get? Would you say they would have to pay less taxes?

MR. TARLEAU: Build their credit up. A person comes to you, Mr. Secretary, and he says - well, as we know, some cases have come to us where they have done nothing but lose money in the base period. Their corporations are the cyclical ones and they just hit a bad cycle in their base period, and they say that, "If you assume every dollar that we make now is an excess profit and subject to the higher tax rate, it would be ruinous to us. You ought to adjust our credit to take into account the fact that we were in a depressed condition in that base period."

H.M.JR: Then you are going to have what, a hearing?

MR. TARLEAU: Yes, sir. They would have to have a hearing, and they would have to show what adjustments are necessary in their opinion in order to make that profit a fair one.

H.M.JR: A public hearing?

MR. TARLEAU: Oh, yes, just like any other proceeding in a court where they would have to make their case.

MR. PAUL: In the last war that wasn't public.

MR. TARLEAU: I think this ought to be, because of the great public interest in the excess profits tax, just the way any board proceeding is published.

MR. PAUL: That probably would save us from a lot of scandal.

- 21 -

H.M.JR: If I have anything to do with it, it will have to be public.

MR. TARLEAU: Oh, yes, just as any Board of Tax Appeals case is public. A man can sit in a board case and hear what happens. I think the impelling reason for something of this kind is the fact that these tax rates, Mr. Secretary, are going up to such great lengths that if a person is unfortunate enough to have hit a depressed condition during the years '36 to '39, you are practically confiscating his income. That would be what it amounts to.

H.M.JR: What else have you got? I will have to soak that one in.

MR. PAUL: That is pretty much the corporate picture.

MR. BLOUGH: I would like to speak on that one just a half a minute if I might.

H.M.JR: Yes.

MR. BLOUGH: When we were working on this seven twenty-two, the relief provision of a year ago, we tried to make a provision for what would happen if an earthquake or a fire or something like that had brought about an abnormal situation in the base period. We strenuously opposed, however, putting into seven twenty-two, the relief provision, any relief if the demand was abnormally low or something else had happened in the base period, because you can't write that into a statute of general application without this board, and this is an extension of the idea that was in last year's relief provision.

H.M.JR: Well, how would this board be appointed?

MR. PAUL: By you.

H.M.JR: With the consent of Congress?

MR. TARLEAU: That is a detail, Mr. Secretary, that I think is very important, and I am trying to get our boys

- 22 -

to submit alternative plans to you and how this board should be appointed. One idea is that you should appoint it. The other one is that it should be appointed by the President with the advice and consent of the Senate.

H.M.JR: Because you take that thing that Eddie Greenbaum ran over there with these twenty-two different advisers. I don't know whether you (Paul) were one of them or not.

MR. TARLEAU: That Amortization Board.

H.M.JR: They were not public hearings, and now these fellows have sort of gone back to their work or are out of work.

MR. BLOUGH: They couldn't do that here.

H.M.JR: If there ever was an investigation - as I understood - what was it, they sat one week in five or something?

MR. SULLIVAN: They circulated.

H.M.JR: Yes. But I mean supposing they ever investigate that thing. It would be terrific to explain why one man did one thing and twenty-one did something else. Wouldn't it be?

MR. SULLIVAN: No, I don't think it would be, sir, because it was a fine board, and I think those men are all - they all kept their skirts pretty clean.

H.M.JR: Oh, yes, but I mean, do you suppose there were records made?

MR. SULLIVAN: Yes, I think there were, although I don't know for sure.

H.M.JR: Did the company get a chance for a hearing or was it just gone over?

MR. SULLIVAN: I don't think they got a hearing.

H.M.JR: They did it on a case basis, is that what you call it?

MR. SULLIVAN: That is right.

MR. BLOUGH: There is no use blinking the fact that this would be a very hard thing to do.

MR. SULLIVAN: I think in what Mr. Tarleau is trying to do, the cases are very, very hard. My reluctance at first blush, when I first learned about this, to see it adopted was predicated on my general resistance to any device that gives to the Treasury such tremendous power without laying down in the statute some guide as to how that power is to be directed, and if it is possible, in the statute to define the limits within which relief can be accorded by the board, we will be in a much better situation, and I think Tommy agrees with me on that, don't you Tom?

MR. TARLEAU: Surely. All I want to do is to not lay down some restrictions that the relief goes out of the window. I agree with you on as many standards as we possibly can have in the statute. I am not at all sure that the Secretary, when he finally makes his mind up, will want it in the Treasury. He may want it in a special division of the Board of Tax Appeals rather than in the Treasury, because he doesn't want the Treasury to be subject to any possible criticism of arbitrary action. That is one of the things I was working on last night to see whether we could make it a special division of the Board of Tax Appeals.

H.M.JR: Believe it or not, I don't want any more power.

MR. SULLIVAN: Well, this is tremendous power for whoever has it.

MR. PAUL: Oh, that is certainly true, and it couldn't

succeed as a board unless it was composed of men of such high caliber that it had the complete public confidence.

MR. SULLIVAN: That is right, and I think they have got to be free from the political pressure that would result from a change of administration.

MR. TARLEAU: That is perfectly true.

MR. PAUL: But this is a very essential element.

H.M.JR: Oh, I can see that. Of course, the Board of Tax Appeals is set up so that it lives over - what are they, twelve year appointments?

MR. SULLIVAN: Yes.

MR. TARLEAU: They are appointed, some for fourteen years, and then they step down, don't they? Some are appointed for ten and twelve, but anyway, they are long-term appointments. It may well be that we ought to put them in the board as a special division of the board just to handle this type of case.

MR. SULLIVAN: Mr. Stam is advocating a - giving more more work to the Board of Tax Appeals for the duration.

H.M.JR: What would he do with the cases?

MR. SULLIVAN: Set up some separate board here in Treasury.

H.M.JR: Well, I am willing to take any responsibility in the Treasury, but I am not looking for any--

MR. PAUL: I am not very much in sympathy with that.

MR. SULLIVAN: No, I am not with that.

H.M.JR: What else on corporations?

MR. PAUL: That pretty much covers the corporate

picture.

MR. BLOUGH: Have you talked about the thought of possibly returning some after the war?

MR. PAUL: No, we haven't talked about it again, but it has been implicit in several conversations. That is your idea of having the re-employment fund.

H.M.JR: Especially since I hear that when you saw these three gentlemen they all kind of liked it. Is that right?

MR. SULLIVAN: Yes, very much. Nelson said that that refund would have to go to all corporations, that if it were conditioned so that it would just go to corporations in need of relief, that it wouldn't work and it wouldn't accomplish the desired result among the--

H.M.JR: I don't know whether he is right on that.

MR. SULLIVAN: No, I am just reporting his thoughts.

MR. PAUL: I didn't get quite that impression. He did say it would be rather difficult, however, to find the conditions under which it should be returned.

MR. SULLIVAN: I asked him, Randolph, if it should go back to all or just to those, and he said, "No, it would have to go back to all."

H.M.JR: Well, I don't see how that would work. The idea is, as I understood it, that when we get above eighty percent that this was there for that purpose, and I think - wouldn't it be - most of those that went above eighty would be companies like the CurtissWright anyway, wouldn't they?

MR. BLOUGH: Any company that had one dollar at the highest rate.

H.M.JR: But I mean, it would be mostly companies

in the war business, wouldn't it?

MR. BLOUGH: Most of the money would come from those companies.

H.M.JR: The thing that surprised me was that you (Sullivan) said that Patterson said they are not setting up provisions to pay the company to put their machinery back again.

MR. SULLIVAN: That is right, and I received this morning, it just came in before I came in here, a contract from the War Department which makes allowance for converting from peacetime to military production. I haven't had a chance to read it, and also a letter from Judge Patterson to Donald Nelson raising the question as to whether or not a similar provision should be made in future contracts to pay for the reconversion from military production to peacetime production after the war is over.

H.M.JR: But they are paying the companies for dismantling their plants at present?

MR. SULLIVAN: I think they are paying most of them.

H.M.JR: Well, if they are not paying them to set the machinery up again, this seven and a half percent would be all the more--

MR. PAUL: Very true.

H.M.JR: But I can also see that some would get it and some wouldn't get it.

MR. SULLIVAN: Oh, yes.

MR. PAUL: It was, as a basic proposition, popular with all three of them.

MR. SULLIVAN: They all just went for it. Big and quick.

H.M.JR: Roy, I wish you would make one note. I

don't know whether it is in my own statement, but I would like to say something about - that the excess profits tax should be the one and only tax that we shouldn't have any - and so forth and so on. I don't know whether I have said that before.

MR. PAUL: No. Patterson, particularly, didn't you think, John--

MR. SULLIVAN: Yes, I raised that with Patterson and all with Forrestal.

Now, Vinson is after us and Walsh is too, and I think I would like to have a conference with Forrestal, Patterson, Vinson, and Walsh, and see if we can't thrash this thing out now.

H.M.JR: Well, don't you think we ought to wait until we know a little bit - get this thing a little bit more jelled?

MR. SULLIVAN: No, I don't, sir, because the pressure is on. Walsh demanded that Surrey be available to help him draft a bill, and we thought we ought to play with Walsh. He has been pretty helpful to us on finance. Surrey is available. The idea that Walsh gave him can't possibly be worked out, and I think if we have this conference now, it will clear the air.

H.M.JR: Well, let me think that one over. That is full of dynamite.

MR. SULLIVAN: Well, I would want to tell - oh, incidentally, I would want to have George and Doughton at that conference, too.

H.M.JR: Well, I think I would have to go into it myself.

MR. SULLIVAN: Yes, that would be fine, but I think we ought to plan to do it tomorrow at the latest, because the pressure is getting very, very strong up there.

H.M.JR: Well, you fellows have given me a lot of things to think about this morning. Let me think about it. I have got nothing particularly this week other than taxes. I mean, I am trying to keep the shop running. I have got my debt limit bill, and I have got my Chinese and Ecuador and a few odds and ends, but otherwise, I am all right.

MR. SULLIVAN: Well, Vinson is calling me tomorrow. I have been stalling Vinson for a week, and he said, "Well, I am going to call you Tuesday morning, and I want a bill."

H.M.JR: Well, I will be seeing you again today.

MR. SULLIVAN: The other thing I would like to get some action on is partial exchange in the rule that says there shall be no extensions for corporation returns. The Bureau feels that that will work a great hardship, and we are getting all kinds of letters and telegrams.

H.M.JR: Well, can't the Commissioner write me a letter on that asking me, if that is what he wants?

MR. SULLIVAN: I will have Mr. Cann write a letter.

H.M.JR: Is the Commissioner still sick?

MR. SULLIVAN: He is in Florida.

H.M.JR: Well, let somebody from there write a letter.

MR. SULLIVAN: All right, and can I bring that in to you today?

H.M.JR: Yes.

MR. SULLIVAN: We would like to give the collectors the power to extend for sixty days--

H.M.JR: You get Cann, if he is Acting Commissioner,

to write it for me.

MR. SULLIVAN: Yes, sir, I will.

H.M.JR: O.K. Well, let me look at my own desk,
and you will hear from me again today, all of you.

THE HOUSE WAYS AND MEANS COMMITTEE SCHEDULED A START OF HEARINGS ON

THE \$7,000,000,000 WAR REVENUE BILL FOR MARCH 3.

2/23--R310P

ADD TAXES, HOUSE

SECRETARY MORGENTHAU WILL PRESENT THE ADMINISTRATION'S RECOMMENDATIONS. THE COMMITTEE WAS EXPECTED TO HEAR REPRESENTATIVES OF INDUSTRY AND THE GENERAL PUBLIC THE FOLLOWING WEEK, BEGINNING MARCH 9.

WAYS AND MEANS COMMITTEE CHAIRMAN DOUGHTON AND CHAIRMAN GEORGE OF THE SENATE FINANCE COMMITTEE ARE EXPECTED TO CONFER WITH MORGENTHAU LATE THIS WEEK, AND MAY REACH SOME AGREEMENT THEN ABOUT WHAT NEW TAXES THE ADMINISTRATION WILL PROPOSE.

2/23--R322P B-0



TREASURY DEPARTMENT

WASHINGTON

OFFICE OF
COMMISSIONER OF INTERNAL REVENUE

MEMORANDUM SUBMIT TO
COMMISSIONER OF INTERNAL REVENUE
AND REFER TO

February 23, 1942.

Memorandum for the Secretary:

Subject: Extensions for Filing.

At the present time the Bureau of Internal Revenue, in accord with your prior instructions, is restricting the granting of extension to file both corporation and individual tax returns. The offices of the various collectors of internal revenue have authority to grant extension where individual taxpayers are concerned. Extension of time within which to file corporation returns is granted only by direction of the Commissioner, except in the Territory of Hawaii.

The policy in effect respecting the extension of time in which to file returns was occasioned by the abuse of this privilege which had developed over a long period of time.

At the present time the Bureau is being constantly urged by professional and business organizations to relax the present policy in granting extension of time within which to file. It is urged that prevailing war conditions have cut into ranks of skilled accountants and have also depleted the tax staffs of large industrial organizations and banking institutions. It is also pointed out that the income tax blanks were not available at the customary time, which allegation is true due to the delayed enactment of the Revenue Act of 1941.

Notwithstanding the representations made to the Bureau, I do not recommend any general extension of time. It is believed, however, that conditions warrant some relaxation of the existing procedure. It is recommended that authority to grant extensions in the instance of corporations be restored to the various collectors. It is recommended that collectors be authorized to grant extensions of sixty days

BUY

from March 15th in the instance of both corporation and individual returns where it is shown that the delay in filing is due to conditions beyond the control of the taxpayer, giving some recognition to the effect of the curtailment of competent accounting personnel.

Nelson H. Carr
Acting Commissioner.

W. M. Nuttall
I concur in this recommendation.

THS

FEB 23 1942

Dear Mr. Hetsel:

This will acknowledge receipt of your letter enclosing the "Preliminary Report on CIO Income and Expenditures Study" and a copy of the "Resolution on Taxes."

Your kindness in sending this material to me is greatly appreciated.

Sincerely yours,

(Signed) H. Morgenthau, Jr.

Secretary of the Treasury

Mr. Ralph Hetsel, Jr.,
Director, Economic Division,
Congress of Industrial Organizations,
1106 Connecticut Avenue, N.W.,
Washington, D. C.

H. M. C. Tule
W. Thompson

ASD REP:deb

PHELIP MURRAY, *President*

DALYMPER, *Vice President*
TUSHNET, *Vice President*
GIBSON, *Vice President*

FRANK ROBINSON, *Vice President*
REED ROBINSON, *Vice President*
BAIL ROYB, *Vice President*

JAMES R. CLARK, *Secretary*
ALLAN S. HAYWOOD, *Director of Organization*
JOHN BRONF, *Director of Industrial Union Councils*

LEO FERRISMAN, *General Counsel*
LEO DE CAUX, *Publicity Director*
J. R. HOLL, *Comptroller*
RALPH HETZEL, JR., *Director Economic Division*



CONGRESS OF INDUSTRIAL ORGANIZATIONS

1106 CONNECTICUT AVENUE, NORTHWEST

WASHINGTON, D. C.

February 12, 1942

Office of
DIRECTOR, ECONOMIC DIVISION

TELEPHONE DISTRICT 3582

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

Dear Mr. Secretary:

I am sending you herewith a copy of the preliminary report on our income and expenditure study which you discussed with Mr. Carey and me in December. The report has not yet been published and it is simply a preliminary compilation. We still have a number of questionnaires to come in.

It seems to me the study emphatically indicates the great extent to which the wage increases of last year went to the purchase of the three necessities - food, clothing and housing.

I am also enclosing for your information a copy of the resolution which the CIO Executive Board adopted on taxes.

Sincerely yours,

Ralph Hetzel, Jr.

uopwa 27

RESOLUTION ON TAXES

WHEREAS, (1) The war production program requires the best efforts of all American workers, and

(2) It is essential in order to reach such maximum production that American workers and their families receive incomes sufficient to maintain the worker and his family in full efficiency, good health and well-being, and

(3) Profits of industry under the war program are soaring to outrageous heights, and

(4) The President of the United States has asked for an additional tax program of \$7 billion and such an amount can be collected from taxes which do not fall further upon working men and their families,

NOW THEREFORE BE IT RESOLVED, that the CIO call upon the Congress to enact a tax program which will stop war profiteering and the creation of war millionaires and which will protect the standard of living necessary to maintain American production at a maximum. Such a program should provide for the necessary federal revenue to come from the following sources:

1. Increased normal taxes and excess profit taxes on corporations.
2. Increased taxes on the present individual income tax base.
3. Closing of loopholes in the individual income tax and the corporation taxes, such as mandatory joint returns and tax-free bonds.
4. Increased rates and lowered exemptions on estate and gift taxes.
5. Excise taxes on certain luxury goods.

AND FURTHER BE IT RESOLVED, that the CIO oppose most vigorously any

-3-

attempt to establish a general sales tax or a flat wage tax for general revenue because such taxes are the most vicious kind of discrimination against the working people.

The Executive Officers of the CIO are hereby authorized to proceed with the prosecution of such a tax program, to urge its passage in the Congress of the United States and to call upon all affiliates to support it unstintingly.

Preliminary Report
ON
CIO Income and Expenditures Study

Congress of Industrial Organizations
Economic Division
Ralph Hetzel, Jr., Director
February 6, 1942

Congress of Industrial Organizations
Economic Division
Ralph Hetzel, Jr., Director
February 6, 1942

Preliminary Report

on

CIO Income and Expenditures Study

Introduction

In the early part of December 1941, the CIO Economic Division in cooperation with the Research Departments of most of the CIO affiliated unions, undertook a study to determine how workers spent the increased income which they received as a result of wage increases. This study so far has covered 16 industries located in 53 towns and cities in 9 states.

The preliminary results of the survey show that the average monthly income of the families was \$173.20. The average size of family was 4.

The study sought to compare the months of November 1941 and November 1940. The monthly income for November 1941 was 14.6 percent, or \$22.14, higher than the income in November 1940. The study only attempted to determine the amount of expenditures for seven main items in the worker's budget. They were food, clothing, housing, car operations, household operations, installment purchases and personal care.

Food Expenditures

The average family spent \$54.42 a month for food. This represents 31.4 percent of the total income of the family and is \$12.29, or 29 percent more than was spent a year ago. During this same period, food prices, according to the Department of Labor's index of the cost of foods, increased 17.8 percent. Nearly two-thirds of the increased food expenditure, therefore was drawn off in higher prices and does not represent increased food purchases.

Clothing Expenditures

The average family in November 1941 spent \$18.49 on clothes. This represented 10.6 percent of their total monthly income and was \$5.56 a month more than they spent in November 1940. The increased expenditures for clothing between November 1940 and November 1941 was 43 percent. During the same period, according to the Bureau of Labor Statistics, clothing prices rose 12.6 percent.

Housing Expenditures

The average monthly rental was \$23.49. This represents 13.6 percent of total income of these families, or an increase of \$2.05 a month over rentals in November 1940. This increase in rental is 9.6 percent, while the BLS rental index increased during this same period by only 3.1 percent.

A comparison of the increased expenditures for food, clothing and rental with the actual increases in prices for these three items shows that the average worker family did spend more for these items than was necessitated by increased prices alone. The families were able through increased income to spend somewhat more for food and clothing and rent. On these three items—food, clothing and shelter—the average family increased their expenditure by \$19.84. This compares with the wage increase of \$22.14. Very significant is the fact that by far the greatest part of increased expenditures went to the three main necessity items—food, clothing and rent.

For the four other items in the family budget included in the CIO questionnaire, expenditures increased as follows:

	<u>Amount increase over 1940</u>	<u>Percent increase over 1940</u>
Monthly car expenditures	\$1.85	30.6
Household operations	1.89	16.1
Installment purchases	3.12	34.5
Personal care	0.67	33.0

In addition to determining the expenditures for these seven budgetary items, the questionnaire attempted to ascertain how many families were increasing their purchases of household appliances, household furnishings, and the like. Preliminary examination of the answers to this set of questions shows that 63 percent of the families questioned had increased their purchases of some type of electrical appliances, such as lamps, electric irons, refrigerators, stoves, vacuum sweepers, washing machines, etc. Some 64 percent of the families increased their expenditures for household furnishings. While

these percentages are rather high, they do not tell the entire story. They must be considered in the light of the increased expenditures by the average family for installment purchases, which was \$3.12, or only 11 percent of the total increased expenditures of these families.

The average family reported that they had increased their expenditures for medical and dental care by 55 percent. Thirty-three percent of the families stated that they had been able to repay back debts as the result of having increased income. Only 10 percent of the people reported any increased bank savings, although 30 percent of the families reported that they were purchasing either defense stamps or bonds. About 35 percent of the people found a little extra money available to increase their expenditures for recreational purposes. Some 29 percent of the families bought either a used or new car. Over three-fifths of the cars purchased by these families were used and only 6 percent of the people who purchased cars never formerly owned an automobile.

The following table summarizes the expenditure study:

	<u>Amount of Expenditure</u>	<u>Percent of Income</u>	<u>Average Monthly Increase</u>	<u>Percent Increase</u>
Food	\$54.42	31.4	\$12.23	29.0
Clothing	18.49	10.6	5.56	43.0
Housing	23.49	13.6	2.05	9.6
Car Operation	7.91	4.6	1.85	30.6
Household Operation	13.62	7.9	1.89	16.1
Installments	12.17	7.0	3.12	34.5
Personal Care	2.70	1.6	0.67	33.0

Average Monthly Income - \$173.20

Average Size of Family - 4

Average Monthly Increase in Income - \$22.14

Percent Increase - 14.6%

Significant are the following comments taken from the questionnaires. These comments were written in answer to the question, "What in your opinion do you think are the principal things for which you have used your increased income?"

Mansfield, Ohio — "The increased income just about covers the increase in the cost of living to date, but with food, clothing, fuel, etc. rising each week, will soon be falling behind."

Mansfield, Ohio — "The increase in our income does not cover the advance in prices on food, and coal, and clothing not naming other articles too numerous to mention. If I did not get a little extra time there would hardly be enough money to meet my expenses each pay. The food prices seem to jump every day or so. And for instance yard goods or dress materials that cost 8¢ or 10¢ last year cost 19¢ to 25¢ this year. Shoes that cost \$1.50 are now \$2.00. In food, eggs were 20¢ to 25¢ last year. Now they are 40¢ to 45¢. Cheese in the spring was 17¢ per pound—now 34¢ a pound. Lard 2 lbs. for 15¢, now 2 lbs. for 27¢ — that is just an example."

Wilkes-Barre, Pa. — "In 1940 I received income of \$68 per month, in 1941 I am receiving income of \$78.20 per month. I am purchasing same amount of material as I did in 1941 but I am paying more for them. Prices in some cases had risen far beyond the fifteen percent pay increase which I had received in 1941."

Watrons Heights, Pa. — "We had started to save the forepart of this year until the price of living went completely out of our control and now we have no savings of any kind. We attend less shows and other forms of recreation now. Personally, I had to give up fishing and hunting, the only forms of recreation that I indulged in."

Vexona, Pa. — "Keeping bills straightened out and paying gas, light and water bills on time."

Beverly Island, Pa. — "Food - biggest item and most worry. It is all I can do to juggle the finances to meet household expenses. No comforts and house isn't livable. Roof leaks, dirty cellar. It would take at least \$200 a month to run my home adequately."

Johnstown, Pa. — "Buying floor covering, blankets, coal, phone, buying furniture for cash, clothing for children, etc."

Akron, Ohio — "Miss \$14 monthly installment payment come in a while. Need dental care but not able to get it done. Going in debt. Would buy defence bonds if could, but don't even have a dollar a week to spend. Children have never been to a movie. If I had to pay taxes, it would take bread and butter out of my children's mouth. Increased feed prices and more clothing. Coal has increased. Having considerable difficulty making ends meet. As much as I would like to contribute to my church and government through defense bonds and stamps, I just can't. Have had to keep children home from school until pay day because haven't had any money for shoes. It has been two-and-a-half years since I bought a suit. Borrow money between pay periods in order to tide self and family over. Don't smoke or drink because no money for even a cigarette."

February 23, 1942
2:30 p.m.

Operator: Go ahead.

HMJr: Hello.

Sumner
Pike: Hello, Mr. Secretary.

HMJr: How are you?

P: Well, I seem to be sort of the central figure here in the squabble, but I'm getting along all right, I guess.

HMJr: Well, I don't know what happened, you see, so - I heard from Purcell that the President said it was all right to have you come over.....

P: Well.....

HMJr:but he just didn't want to put it in writing.

P: Well, Hopkins called Purcell up this morning.

HMJr: Hopkins did what?

P: Called Purcell up this morning.

HMJr: Oh, I didn't know about that.

P: Well, apparently that was a hang-over from what I told you about Leon, you know, some weeks ago.

HMJr: Oh, yes.

P: And apparently the President must have spoken to him after - well, sometime after Saturday night.

HMJr: Talked to who?

P: Talked to Hopkins.

HMJr: Yes.

P: Because I didn't get the conversation and Purcell didn't give me the details of it.

HMJr: Yeah.

P: But I think they were to see each other this afternoon. I think that's probably what's kept Purcell from doing anything this morning. Oh, I remember the other thing, of course, we're still short two Commissioners who are up in Philadelphia today taking advantage of sort of a half holiday - I guess trying to look after themselves for living space.

HMJr: I see. Well, what was Hopkins' attitude?

P: Well, apparently what had happened was that when Leon asked me to go on that rationing thing two or three weeks ago, the President told Leon that he'd ask Hopkins to see personally what might be arranged.

HMJr: I see.

P: Well, in the meantime, as I gathered, he hadn't done anything about it.

HMJr: Who, Hopkins?

P: Hopkins hadn't.

HMJr: Oh.

P: And he must have been reminded by the President sometime over the week-end.....

HMJr: I see.

P:because he got hold of Purcell this morning.

HMJr: Oh, yes.

P: And as far as I know, Purcell said that they had made arrangements to see each other.....

HMJr: Yeah.

P:this afternoon.

- 3 -

HMJr: I see.

P: And - of course, on that thing, Mr. Secretary, from what the President said as it was reported to me, I couldn't under any interpretation of a brief and temporary period, why you can't - rationing doesn't come under that definition at all.

HMJr: No.

P: I mean, it just couldn't work.

HMJr: No.

P: This one thing, if you were miraculously lucky, you might be able to do it in a short time.

HMJr: That's Aniline Dye.

P: Yes.

HMJr: Yeah.

P: And so I think that can come under - come under what I understand him to have said that it should be temporary and for a brief period.

HMJr: Yes. And the other wouldn't.

P: The other certainly wouldn't, because after all, it's going to grow more and more complicated and can't help but become meaner and meaner as time goes on.

HMJr: No question - it's a dirty job anyway.

P: Why sure it's a dirty job. (Laughs) But I think naturally Purcell might have felt that he had to talk to him, since obviously the President had needled him after having replied to him on this thing.

HMJr: I see.

P: I think Hopkins told him that he had seen the letter that Purcell wrote to the President, and

- 4 -

he could only have seen that, I suppose, in one place.

HMJr: Yeah.

P: So as far as I know, that's the stand-in; and I'm sort of in the position of the debutante who never thought she amounted to much until she took her first gargle of Listerine and then all at once changed around.

HMJr: I see. Well.....

P: In other words, I'm at the disposal of - the way it works out - with Purcell. As I understand it, I'm just out of it.

HMJr: Well, still, you have some choice in the matter, haven't you?

P: Well, only this, that I - from the Commission's point of view, I think still - and have felt right along - that, look at it alone, we ought not to have any disturbance here for awhile.

HMJr: Yes.

P: On the other one - I mean, on the Henderson matter - well, that just doesn't fit what, we'll call, the President's definition. I'd say that's out entirely.

HMJr: You say that's out.

P: This one - if Ganson'll go along, why I'm really willing to be up there tomorrow morning.

HMJr: I see. Well, he's coming in around three, and I'll see him then.

P: And whatever works out will be okay with me, and I'll be - I'll play soldier in the thing, in other words.

HMJr: Well, it's nice to have so many people want you.

P: Yeah. I feel immensely flattered, but at the

same time it's a little bit embarrassing.

HMJr: Well, it's happened to me so often. Just as soon as I want somebody, everybody else wants them.

P: Well, maybe they're following your trail, like these gold-rushers.

HMJr: Well, I don't want.....

P: But in this particular case, it did happen that Henderson was first in time; and I suspect that it just got dropped until probably he found out, and he didn't find out through me, I'm sure, or anybody over at the place. He must have got it direct from the President.

HMJr: I see.

P: As you said, he did see the - he told Purcell this morning that he had seen the letter.....

HMJr: All right.

P:that Purcell sent over.

HMJr: Okay.

P: Righto.

HMJr: Thank you.

P: Good-bye.

February 23, 1942
2:33 p.m.

HMJr: Bob.

Congressman
Deughton: Hello, Henry, how are you?

HMJr: I'm alive and kicking. How are you?

D: I've driven four hundred miles since four
o'clock this morning anyhow.

HMJr: Well, you're a better man than I am.

D: Oh, no. Not in any sense; not in any way
about anything.

HMJr: Better man than I am.

D: Well, I've done that, all right.

HMJr: Bob, I understood that you wanted to know
whether a week from Tuesday was all right
to me.

D: Yes. Well, no, I didn't say I wanted to know;
but I would like to know as soon as I could.
They kind of suggested Tuesday as a tentative
date and said they'd let me know by tomorrow.

HMJr: Yeah.

D: I don't want to rush you, you know.

HMJr: Well, here's the thing.....

D: We need at least a week's notice if we can get
it so the boys can all be here and kind of make
their plans.

HMJr: Well, I'll be ready Tuesday, a week.

D: Well, if I give out the statement tomorrow then
that you'll appear before the committee Tuesday
week and will start on that tax program, will

- 2 -

that be satisfactory?

HMJr: Well, the only thing is this. I see the press at four today. You couldn't give it out before then, could you?

D: Before when?

HMJr: Before four o'clock today.

D: Well, yes, I guess I could.

HMJr: Well, it would help me; because they've just been making my life miserable.

D: All right.

HMJr: If you could give it out before four o'clock.....

D: I'll just send a note over to the press gallery and phone the boys, too.

HMJr: Would you do that?

D: I'll get right after it right now.

HMJr: That would help.....

D: All right. We'll begin at ten o'clock in the committee room on - that's the second, isn't it?

HMJr: Just a minute. I've got a calendar right here.

D: See what it is; I don't remember. Seems like it's about the second.

HMJr: The third.

D: The third.

HMJr: Third.

D: Tuesday, the third.

HMJr: Yeah.

- 3 -

D: All right. Thank you for calling. I'll get right after it.

HMJr: And then we'll see each other before that.

D: Yes. I'd be glad to see you any time at your call.

HMJr: Thank you.

D: Thanks very kindly.

HMJr: Good-bye.



71

TREASURY DEPARTMENT
PROCUREMENT DIVISION
WASHINGTON

OFFICE OF THE DIRECTOR

February 23, 1942

MEMORANDUM TO THE SECRETARY:

Supplementing my memorandum to you of February 20th, we are now able to report that the indicated deficiencies on seven of the items scheduled on our status report of the Russian Program dated February 18th will be cleared up by April 1st. There are two items on which clarification of specifications is required from the Russians before the balances can be allocated, which matter the War Production Board now has under discussion with the Russians. There remain five matters of allocation deficiency and one priority difficulty. Two of the allocation items are the result of insufficient mill capacities; the three other allocation deficiencies have to do with requisitions just recently received from the Russians. The priority difficulty concerns the necessity for a higher rating, and each of these matters is under active consideration.

In addition, the War Production Board has suspended 10,000 tons of rails from British production and we will secure delivery of that tonnage for Russia during the month of March, and 4800 tons of steel plates will also be shipped during March. Both of these items are Non-Protocol.

We are keeping in close touch with War Production Board and will advise you promptly of further developments.

Clifton E. Mack
Clifton E. Mack
Director of Procurement

FOR DEFENSE



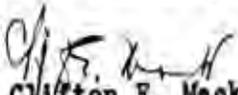
February 23, 1942

MEMORANDUM TO THE SECRETARY:

Supplementing my memorandum to you of February 20th, we are now able to report that the indicated deficiencies on seven of the items scheduled on our status report of the Russian Program dated February 18th will be cleared up by April 1st. There are two items on which clarification of specifications is required from the Russians before the balances can be allocated, which matter the War Production Board now has under discussion with the Russians. There remain five matters of allocation deficiency and one priority difficulty. Two of the allocation items are the result of insufficient mill capacities; the three other allocation deficiencies have to do with requisitions just recently received from the Russians. The priority difficulty concerns the necessity for a higher rating, and each of these matters is under active consideration.

In addition, the War Production Board has suspended 10,000 tons of rails from British production and we will secure delivery of that tonnage for Russia during the month of March, and 4800 tons of steel plates will also be shipped during March. Both of these items are Non-Protocol.

We are keeping in close touch with War Production Board and will advise you promptly of further developments.


Clifton E. Mack
Director of Procurement

February 23, 1942
2:53 p.m.

Clifton
Mack: Yes, sir.

HMJr: I have your letter of the twenty-third on this Russian thing.

M: Yes.

HMJr: Of course, you know what you're writing about, but I don't.

M: Yes.

HMJr: And I - you see, you don't tell me which the items are. Now, you've got that schedule before you.....

M: Yes.

HMJr:which I sent over, you know, for Nelson.

M: Yes.

HMJr: Now, if you could get me a letter which I could have the first thing tomorrow morning - I don't know whether there are numbers on those things or not, you see. Let me know which of those things have been cleared up.

M: Very good.

HMJr: Number them, or by line number so and so, you see.

M: All right, I'll do that.

HMJr: But you see, I can't tell. There are two items on which a clarification of specifications is required from the Russians. You don't say which the two items are.

M: Yes, that's so.

HMJr: Then you say - report deficiency on seven items. You don't say which the seven are.

M: Yes.

HMJr: Two of the allocations are the result of insufficient mills. You don't mention which the two are.

M: Yes.

HMJr: I mean, I can't dream it.

M: Well, that's true. I'm having that schedule revised, but perhaps I'd better in the meantime get a letter over to you and list those items.

HMJr: Get a letter over so that I can have it in the morning, showing me which are the ones that cleared up, you see.

M: Very good.

HMJr: And then indicating somehow on this chart which ones are still to be done.

M: Very good.

HMJr: In other words, I want amplification.

M: Very good. I'll do that.

HMJr: Now - and then you still - you're not down to some which they refuse to do?

M: Oh, no. No, there are certain items that they just recently received requisitions on.

HMJr: Oh.

M: And.....

HMJr: Well, I think you ought to mention those and say when we got the requisitions.

M: All right.

HMJr: What day did we receive them.

M: All right. I'll do that.

- 3 -

HMJr: See? You get what I want.

M: Yes, I do.

HMJr: Thank you.

M: I do. Yes, sir.

February 23, 1942
4:25 p.m.

Governor
Lehman: How are you?

HMJr: Fine.

L: Good. Say, Henry, I heard a rumor yesterday.....

HMJr: Yes.

L:that the Treasury Department is thinking of recommending that any states that didn't allow the deduction from state income tax payments of the federal tax would not be allowed - the citizens would not be allowed to deduct the state tax - hello.

HMJr: I never heard of it.

L: All right, fine. I just wanted to make sure of that.

HMJr: No, never heard of it, Herbert.

L: That would, of course, put an absolutely on the type - it would mean thirty or forty or fifty million dollars less in revenues here and, gosh, we just can't stand it.

HMJr: Never heard of it, Herbert.

L: All right, fine, Henry.

HMJr: Just charge it off to fifth columnists.

L: All right, fine. I'm glad to hear that.

HMJr: All right.

L: How's everything else going?

HMJr: As well as you can expect. As well as you can expect.

L: You haven't heard anything more - I mean, Epstein haen't said anything more about that, has he?

HMJr: No.

L: Because I had a talk with him, and I don't think he will. If he talks, I told him he has to talk personally and not representing the state.

HMJr: I haven't seen anything more.

L: The man who has, of course, been the most active in this thing is LaGuardia.

HMJr: Oh, really?

L: Well, I mean, I think he's representing the cities, and I can understand their position, too, of course.

HMJr: Well, he hasn't said anything so far this year.

L: I see. Well, I heard he had been saying it around.

HMJr: Well, he may have behind his hand.

L: Yes.

HMJr: But he hasn't on the record.

L: Well, it's come to me from a number of sources.

HMJr: Yes.

L: All rightie.

HMJr: Thank you.

L: How's Elinor?

HMJr: She's fine.

L: Good. Give her my love, will you?

HMJr: Give mine to Edith.

L: Thank you very much.

HMJr: Good-bye.

L: Good-bye.

February 23, 1942

Dear Harold:

The Secretary and I both appreciate your furnishing us with a copy of your memorandum of February 17, addressed to the President with which you transmitted a letter of the same date to be signed by the President to the Speaker of the House and your memorandum of February 16 addressed to the President on the subject "Effect of Recent House Action on Financial Reporting Program."

Your memorandum of February 16 and the President's letter of February 17 thoroughly cover the subject and I hope they will be instrumental at least in clearing the atmosphere, whether or not we get the additional funds.

Sincerely yours,

S/ DAN

Honorable Harold D. Smith,
Director,
Bureau of the Budget,
Washington, D. C.

DWB:ELS

EXECUTIVE OFFICE OF THE PRESIDENT
BUREAU OF THE BUDGET
WASHINGTON, D. C.

79
Saul Kelly

OFFICE OF
THE DIRECTOR

February 18, 1942.

My dear Mr. Secretary:

I am inclosing a copy of letter from the President to the Speaker of the House and copy of my memorandum to the President concerning our joint operations under Executive Order 8512. I am hopeful that this approach will help resolve some of the confusion that has developed in Congressional minds.

Sincerely yours,

Edward A. Tamm
Director

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

Inclosure

RECEIVED

FEB 17 1942

MEMORANDUM FOR THE PRESIDENT:

The attached letters to the Speaker of the House and the President of the Senate, prepared for your signature, deal with an issue which I feel necessary to bring to your attention. They relate to action of the House in eliminating an item of \$250,000 from the Treasury-Post Office appropriation which was included to carry out the Treasury part in the joint effort under Executive Order 8512 of developing a reliable system of financial reports for the Government.

The item itself is not as important as the issue which the Committee on Appropriations and certain Republican members made of the case. They recited arguments in eliminating the item which go to the very heart of the prerogatives of the Executive. They propose turning essential management functions over to the Government's auditor and divesting the President of his right to determine the kind of financial information required by the Executive Branch. The proposed letters together with the supporting memorandum, which we have prepared in collaboration with the Treasury, tell the story.

Already there are evidences that the departments are taking their cue from the House action and are withdrawing their support to the financial reporting program which you launched by Executive Order 8512.

The Senate is now considering this item so the letters should be sent immediately if you approve them.

(Signed) WINSTON D. SMITH
Director

Enclosures

THE WHITE HOUSE
WASHINGTON

FEB 17 1942

My dear Mr. Speaker:

In submitting the 1942 Budget, I included in the estimates for the Treasury Department an item of \$280,000 for the purpose of carrying forward the work of financial reporting under Executive Order No. 8512. These funds were to be used to make available financial information essential to the President, the Bureau of the Budget, and the Treasury Department, in the management of the Government's fiscal affairs. It has come to my attention that the House of Representatives has eliminated this item in its action on the Treasury-Post Office appropriation bill.

I find that both the Committee Report and the discussion on the floor of the House reflect misunderstanding as to the objectives and provisions of Executive Order No. 8512 and the accomplishments thereunder.

The report and debate on this item include a number of erroneous assumptions. It is assumed, for example, that the Chief Executive can be divested of his right to determine the character and form of financial information required by the Executive Branch. It is assumed that the General Accounting Office can readily supply all of the financial information required by the Executive Branch, and this with little if any additional expense. It is assumed that requirements under Executive Order No. 8512 for the submission of financial reports by executive agencies conflict with the functions of the General Accounting Office. It is assumed that the need for reliable reports of the financial operations of the Government is not urgent even though we are launched on a war program involving many billions of dollars.

With these assumptions I must take issue. They conflict with the responsibility of the President under the Constitution and statutes, particularly the Budget and Accounting Act of 1921. They run counter to the essentials of sound business management. They fail to recognize that the President, aided by the Bureau of the Budget and the Treasury, has and must always have responsibility for determining what financial information is required by the Executive in the administration of the Budget and in the management of the Government's finances.

- 2 -

Executive Order No. 8512 is aimed at one objective — to provide a system of financial reports for purposes of budgetary and fiscal management. In order that the reports will be of real value I have directed that they shall be prepared in accordance with uniform classifications and standards as determined by the Secretary of the Treasury and the Director of the Bureau of the Budget. Since the Government's financial operations center in the Treasury, it was appropriate to designate that Department as the agency to compile the information.

The Director of the Bureau of the Budget is the official to whom I look to place before me the pertinent facts upon which to base budget programs and policies. The Bureau obviously must be supplied with many kinds of data, financial and otherwise, for use in examining budgetary proposals, in following through on the execution of the budget, and in analyzing the financial condition of agencies. In addition, the Treasury must have financial data immediately available for its fiscal operations including the financing of the vast war effort. I need not remind the Congress of the magnitude and complexity of our fiscal program.

The task of collecting and analyzing financial information for executive use is purely executive in character and must be responsive to rapidly changing conditions. The fact that we are at war makes it even more necessary that we have the proper data on which to base our budgetary operations, our revenue operations, and our borrowing operations. Surely this is essential and emergent.

From the accompanying memorandum prepared by the Director of the Bureau of the Budget, you will see that great care was given to the drafting of the Executive Order. It is also evident from the memorandum that I was mindful of the role of the Comptroller General and of the duties conferred upon him by the Budget and Accounting Act. A reading of the Order will show that it is so worded as to recognize — rather than to encroach upon — the prerogatives of the Comptroller General. No action has been taken under the Order which infringes upon the Comptroller General. On the contrary, as the Comptroller General has indicated, Budget Bureau and Treasury officials have worked in close collaboration with the representatives of the General Accounting Office.

- 3 -

The issue raised by the action of the House is vital to effective financial administration within the Executive Branch and has far-reaching implications which I fear have been overlooked. I feel sure that this misunderstanding would be corrected upon a re-consideration of the question by the House.

Very truly yours,

(Signed) FRANKLIN D. ROOSEVELT

The Honorable,
Speaker of the House of Representatives

Enclosure

February 16, 1942

MEMORANDUM TO THE PRESIDENT:Subject: Effect of Recent House Action on Financial Reporting Program

As you know, one of my first steps after assuming the office of Director of the Bureau of the Budget was to initiate a program designed to achieve budgetary administration extending far beyond the mere preparation of the Budget Document. I have made a sustained effort to develop the facilities essential to sound budget planning and effective follow-through once the budget is enacted. Considerable progress has been made in this direction, but these accomplishments may be undermined by the reaction expressed last week by the House in respect to the Treasury estimate for work under Executive Order 8512. In view of the far reaching implications of the House action, I feel impelled to bring to your attention the facts and issues involved.

Reasons for Issuance of Executive Order 8512

You will recall that I was concerned over the absence of a systematic program for the compilation of reports on the Government's financial operations and transactions. While a large volume of accounting activity is carried on by individual Government agencies, there apparently had been no effective tie-in of such activity with the over-all needs of the Chief Executive and his fiscal agencies. This unavailability

- 2 -

of essential fiscal data not only has impeded businesslike administration but has also been the subject of criticism on the part of Congressmen, the accounting profession, the press, and others who have sought to secure an insight into the Government's finances.

While earlier Executive Orders required the compilation of certain financial information, these attempts were not far reaching enough to solve the problem. For example, Executive Order No. 6226 required reports on apportionments and the status of appropriations. However, the data supplied to the Treasury Department under that order were neither accurate nor detailed enough to permit them to serve as the basis for effective budgetary control. This can be attributed largely to the fact that neither the Bureau of the Budget nor the Treasury had sufficient staff to develop detailed plans and to make certain that all departments understood the requirements and actually observed them.

The conditions prevailed despite the fact that the Budget and Accounting Act of 1921 clearly contemplates that the President shall include in the budget complete data on the Government's financial condition. In fact, this Act vests the Bureau of the Budget with wide authority to require information from Government agencies.

After thorough analysis of the situation, I recommended to you the issuance of an Executive order setting up the broad framework for a comprehensive system of financial reporting. This Order, No. 8512, issued August 15, 1940, superseded the earlier orders which dealt with

- 3 -

particular segments of the problem. The order was carefully drafted and the Department of Justice gave it intensive study. Because of the confusion which has characterized the discussion of this order by the House of Representatives, I should like at this point to comment on certain of its important features.

Principal Features of Executive Order 9512

Past experience indicated that the financial data supplied by the individual agencies must be processed by some central fiscal agency if the information is to be assembled in such form as to meet over-all managerial needs. The volume and complexity of the data required make this a formidable task. It was assumed that the facilities for accomplishing this task should be within the executive organization since it would be illogical to say, as the House action might suggest, that the President should depend upon an agency not clearly under Executive direction for the collection of financial data from the executive agencies.

It was appropriate to place this responsibility for assembling the data in the Treasury Department since it already has a mass of financial information available within its own confines. As the result of the responsibilities now vested in Treasury by existing law, that Department necessarily has information as to appropriations, amounts advanced to disbursing officers, checks issued, checks paid, moneys paid into the Treasury, public debt transactions, internal revenues, customs, etc.

- 4 -

Reorganization Plan III, in establishing the Fiscal Service within the Treasury, has provided the means for integrating the financial data available from the numerous sources within that Department. The Treasury has a vital interest in any such system of reporting since it needs a sound factual basis for its financing operations, the difficulty of which has been considerably increased by the war effort.

If the data required by the individual agencies were not integrated with the Treasury's own fiscal information, the resultant reports would be disjointed and of very limited significance. The Executive order accordingly provides that such integration be effected through a summary system of central accounts to be maintained by the Treasury. Such accounts are simply a device for the compilation of the required reports and could hardly be regarded as an accounting system. In fact, the only realistic approach to the problem of central financial reporting for an enterprise as vast and complex as the Federal Government seems to be that the over-all statements must be prepared on the basis of reports received from the individual agencies concerned rather than on the basis of a detailed central accounting system.

The entire stress of Executive Order 8512 is upon the objective of supplying management with the financial information which it needs to discharge its responsibilities. Thus, while the Order makes the Treasury Department responsible for the compilation of the information, the Director of the Bureau of the Budget, acting on behalf of the

- 3 -

President, is given the ultimate responsibility for determining the basic reporting requirements. Furthermore, in defining the types of reports to be prepared by the Secretary of the Treasury, the Order provides specifically for those required for the compilation of the budget and for other purposes of budgetary administration. It further states that the reports shall include such information as the Director of the Bureau of the Budget may determine to be necessary and desirable for adequate budgetary and executive control.

Any system of fact-gathering, whether it be of a financial or general statistical character, must employ uniform classifications and terminology if the reports are to have any meaning. In other words, the agency that requires the information must define the types of data which it needs so that all those furnishing the information will have a common understanding. The discussion in the House of Representatives suggests that these determinations might properly be made by the General Accounting Office. While that agency has an important part in this program, it obviously cannot have the final decision as to what data is needed for management.

The Order in no way attempts to dictate to the Comptroller General as to how he shall discharge his responsibilities for the prescription of accounting systems. In fact, the Order specifically provides that the Secretary of the Treasury shall effect suitable coordination of his summary accounts with the accounting systems prescribed

- 6 -

by the Comptroller General. It is, of course, reasonable to assume that the Comptroller General in prescribing accounting systems will recognize the informational needs of the responsible administrative officials so that accounting will serve as a real tool of management rather than as an end in itself.

Collaboration Among General Accounting Office, Treasury,
and the Bureau of the Budget

The work under the Order has proceeded on the basis of sustained collaboration among the General Accounting Office, Treasury, Bureau of the Budget, and the operating agencies. The three fiscal agencies jointly prepared a revision of General Accounting Office Bulletin No. 1 dealing with object classification of expenditures. The General Accounting Office, recognizing that those using the data must determine the necessary classifications, initiated a proposal that in lieu of Bulletin No. 1, the Bureau of the Budget should determine expenditure classifications for budgetary purposes. About the same time, the three agencies also worked together in the formulation of a system for reporting on the Lend-Lease program.

The Treasury Department and the Bureau of the Budget studied the fiscal data available in the individual governmental agencies in order to make certain that the new reporting requirements made the fullest possible utilization of such information. Concurrently, the two agencies took the opportunity to explain the Order to the various departments and establishments.

- 7 -

Prior to the beginning of the current fiscal year Regulation No. 1, setting forth the initial reporting requirements, was issued under Executive Order 8512. This Regulation was submitted to the General Accounting Office prior to its issuance, and certain modifications suggested by that Office were embodied in the final draft.

Regulation No. 1 under Executive Order 8512

Regulation No. 1 prescribes requirements as to apportionments and provides for complete monthly reporting on the status of individual appropriations, thereby laying the foundation for an intelligent follow-through on the expenditure phase of the budget program. It also prescribes an object classification which was approved by the House and Senate Appropriation Committees.

Immediately after the issuance of Regulation No. 1, the Treasury and the Bureau of the Budget initiated a joint effort to make certain that all agencies fully understood the requirements of the Regulation and were taking the necessary steps to comply with it. As a result of the Regulation, the Bureau of the Budget is now receiving data that are invaluable in checking on the execution of the budget plan. The Estimates Division of the Bureau is now using these reports in making and adjusting apportionments, in establishing and releasing budgetary reserves, and in comparing actual budgetary obligations with previous estimates. These reports will serve as a basis for the operations of the Budgetary

- 2 -

Control Section now being established within the Fiscal Division of the Bureau. These reports are also proving their value in determining the status of the war procurement program, presenting as they do the obligations of the individual procuring agencies.

Future Program

Regulation No. 1, of course, represents only the starting point in the effectuation of Executive Order 8512 and is only one phase of the program. In addition to work on this phase, considerable attention is being given to the development of a system of reports covering the fiscal operations and conditions of governmental corporations and similar activities of a commercial character. The importance of securing corporate data is self-evident. It is interesting to note that in calling for information of this type Senate Resolutions 150 and 292 designated the Treasury Department as the compiling agency. Treasury's experience with these two resolutions has placed it in a strategic position to assist in the development of similar requirements under Executive Order 8512. Another problem that is receiving extended consideration is the development of analyses of financial transactions according to the broad functions and the specific activities involved. Such analyses studied in relation to the work accomplished will greatly strengthen budgetary planning and control.

An important by-product of the work under Executive Order 8512 is the stimulation of considerable interest on the part of agencies in

improved financial administration. It has made agencies more conscious of the managerial importance of fiscal data and has brought to light inadequacies in fiscal facilities that might have otherwise continued indefinitely.

With war expenditures amounting to many billions of dollars, the task of financial administration becomes more difficult, and the need for informative reports is greatly increased.

Implications of House Action

It is unfortunate that the recent House discussion of the Executive order reflected serious misconceptions as to its provisions and raised questions not related to the issue. The discussion stressed an attempt to encroach upon the prerogatives of the General Accounting Office although the Comptroller General has stated that no such attempt has been made. The discussion not only failed to distinguish reporting from accounting and auditing, but also overlooked the fact that the Treasury now has available a great mass of fiscal data. Moreover, the discussion treated financial reporting as if it were something extraneous to the functions of the Government's largest fiscal department. While the discussion by the House assumed that the General Accounting Office is outside the Executive Branch, it advocated, at the same time, making the Chief Executive dependant upon the General Accounting Office for the fiscal data vital to the over-all administration of the Executive Branch.

- 10 -

The action of the House involves far more than the mere disallowance of the Treasury estimate for financing its activities under the Executive Order. As the record now stands it might seriously impede the Executive Branch in its efforts to secure the data indispensable to the very type of budgetary administration which is apparently desired by the Congress. I strongly urge, therefore, that the necessary steps be taken to correct certain erroneous impressions on the basis of which the House apparently took its recent action.

(Signed) HAROLD D. SMITH

Director.

THE WHITE HOUSE

94

Washington

FEB 17 1942

My dear Mr. Wallace:

I am herewith sending you a copy of a letter, together with an accompanying memorandum by the Director of the Budget, which I have sent to the Speaker of the House of Representatives.

These documents relate to the Treasury—Post Office appropriation bill now being considered in the Senate Appropriations Committee.

Yours very truly,

(Signed) FRANKLIN D. ROOSEVELT

Honorable Henry A. Wallace

President of the Senate

Enclosures 2

dca/vf 2/14/42

February 23, 1942.

Dear Felix:

Thank you very much for sending me a copy of the pamphlet containing the opinion of the Supreme Court in the matter of Bethlehem Corporation profits. I shall be glad to study this interesting piece of homework and thank you for sending it to me.

Sincerely,

(Signed) Henry

Honorable Felix Frankfurter,
Associate Justice of the Supreme Court,
Washington, D. C.

GEF/dbs

Dear Henry

Let me know
what was with your
spare time, I need
you too bit of home-
work.

Ever yours
E. G. Ladd

En

seek utilization of the first and second methods but chose, under the third alternative, to make purchases through ordinary business bargaining.

The "actual cost" to Bethlehem of building the ships over which this dispute arises was about \$109,000,000. The generously inclusive formula¹ for determining "actual cost," not challenged by the government here, was not peculiar to these contracts. It was based on the standard formula used by the Fleet Corporation in its contracts with other shipbuilders. And, as in practically all contracts of this type, there was no risk of loss.² The total profits claimed under the contracts by Bethlehem, and allowed by both courts below, were about \$24,000,000,³ or a little more than 22% of the computed

¹ Included in the detailed and comprehensive itemization of "actual cost" were the following and "items similar thereto in principle":

"The net costs . . . of labor (including compensation of labor by way of bonuses), and materials, machinery, equipment, and supplies . . . and other direct charges, such as insurance on the vessels, etc.

"A proper proportion of running expenses, including ordinary rentals, . . . repairs, and maintenance, light, heat, power, insurance, management, salaries (including compensation by way of bonuses), and other indirect charges . . .

"A proper proportion of interest accrued . . . on bonds or other debts or loans existing or contracted for prior to the date of this contract and the proceeds of which shall be used, or shall have been or shall be invested in plant, equipment, etc., that shall be used, in the performance of the work under this contract.

"A proper proportion of taxes of all kinds accrued during the taxable year with respect to the business or property, except any Federal taxes.

"A proper proportion of physical losses actually sustained within the taxable year in connection with the construction of the vessels under this contract, including losses from fire, flood, storm, riot, vandalism, any acts of God, acts of war, or other casualties and not compensated for by insurance or otherwise.

"A reasonable allowance, according to the condition, for depreciation of values of the property and plant of the Contractor used in connection with the work under this Contract."

Neither in the contracts nor under any relevant statutory provision was there any restriction on salaries and bonuses to be paid to executives of the shipbuilder or its affiliates. Cf. Sections 505(c) and 804(c) of the Merchant Marine Act of 1916, 49 Stat. 1955, 1999, 2013.

² Even in the case of lump sum contracts with the government, it is generally recognized that the real risk of loss is negligible. It is usual in this kind of contract to set prices high enough to cover, or otherwise specifically to provide against, unforeseen contingencies. And where loss does occur contrary to the expectation of both parties, Congress often passes special bills making the contractors whole.

³ These ships apparently cost the government at least a large part of still another \$4,825,416. The government paid this amount to Bethlehem to aid in expansion of plant facilities to build the ships—facilities which were turned over to Bethlehem after the war. The government's money was contributed under a contract commonly in use whereby the contractor was given the option of purchasing the additional facilities at a depreciated value. Whether the government, upon conveyance of the property, received any compensation at all does not clearly appear.

cost.⁴ This figure of \$24,000,000 does not include such profits as may have been made by Bethlehem Steel Company, Bethlehem's parent, which sold it at the maximum prices established by the War Industries Board, 43,000 tons of steel used in these ships.⁵ The percentage of profits in relation to the actual investment and working capital devoted by Bethlehem to the building of the ships was not found by either of the courts below.⁶

In No. 8, the government filed a bill in equity against Bethlehem and others. The bill alleged that the government had been induced to enter into the contracts by fraudulent representations of Bethlehem's agents; and as an independent ground for relief, that it had been the duty of Bethlehem to perform the contracts fairly, honestly, and economically "in the shortest practicable time" for no more than "a fair and reasonable profit" and that any provisions in the contract for payment of more are "void and unenforceable." The prayer was for an accounting and a decree requiring Bethlehem to refund all amounts previously paid to it by the government in excess of what the court should find to be just and reasonable compensation for building the ships. Bethlehem filed an answer and a counterclaim for damages based on alleged breach of contract by the Fleet Corporation.

In No. 9, Bethlehem brought suit at law against the Fleet Corporation claiming damages for breach of the same contracts. In an affidavit of defense and counterclaim the Fleet Corporation repeated the allegations made by the government in No. 8 and sought the same relief.

The two actions were jointly referred by the District Judge to a Master who held hearings and made findings. In No. 8, the Master

⁴ While profits on individual contracts ranged above and below 22%, both in the proceedings below and in this Court the whole series of contracts was regarded as a unit. The government has made no separate argument with respect to the individual contracts in which more than the average profit was realized, nor has Bethlehem with respect to the contracts in which the amount due under the half-savings clause proved to be small. The only finding of the Master in which any separation of contracts is made shows that the profits realized on contracts in which the estimated costs were checked by the Fleet Corporation were higher than those on contracts in which the Fleet Corporation accepted Bethlehem's estimates without check.

⁵ Compare the statutory method of restricting profits of affiliates embodied in Section 803 of the Merchant Marine Act of 1936, 49 Stat. 1985, 2012.

⁶ The contracts contained a provision, usual in Fleet Corporation contracts, under which the government agreed "to provide the cash funds necessary to pay for work already done and materials already furnished and for carrying on the work under this contract."

recommended that the government's bill be dismissed, and on the authority of *Nassau Smelting Works v. United States*, 266 U. S. 101, further recommended that Bethlehem's counterclaim be dismissed for want of jurisdiction, the amount claimed being in excess of \$10,000. In No. 9, he recommended that judgment be entered for Bethlehem for \$5,272,075⁷ with interest at 2% from September 1, 1922. The District Judge declined to allow any interest, applying the law of Pennsylvania as he thought our decision in *Erie R. Co. v. Tompkins*, 304 U. S. 64, required. In all other respects he followed the Master's recommendations and rendered judgment accordingly. 23 F. Supp. 676; 26 *id.* 259. The Circuit Court of Appeals affirmed. 113 F. 2d 301. On application of the United States and the Fleet Corporation, we granted certiorari. 311 U. S. 632.

As the case reaches us, the controversy revolves primarily around the section of the contracts which sets out what is to be paid to Bethlehem. In all the contracts, that section contains substantially the following provisions:

"The price to be paid for each vessel to be constructed and furnished in accordance with the terms of this contract . . . shall be the actual cost, plus the definite sum for profit hereinafter in this Article provided for, based upon an estimated base cost to the Contractor . . . Should the actual cost be less than the estimated . . . cost . . . the Contractor shall be allowed as profit on each vessel in addition to said fixed sum for profit . . . one-half the amount by which such actual cost of each vessel falls short of the estimated cost . . ."

Thus, a high estimated cost would increase the probability of "savings" to be divided between Bethlehem and the government. And the more the estimated cost exceeded actual cost, the greater would be Bethlehem's share. It can be seen, therefore, that the estimated cost agreed upon by the parties is a pivotal figure.

I.

The government charged Bethlehem with fraud in submitting estimated cost figures which were adopted in the contracts. It was alleged that Bethlehem's agents made two false representations: (1) that it was impracticable to estimate closely what the cost would be and (2) that the estimates Bethlehem submitted, and which the Fleet

⁷ The government concedes "that \$1,514,996 of the judgment awarded . . . in the action at law is . . . due under contracts other than those now under attack."

Corporation accepted, were fair and reasonable under the circumstances. The Master found that there was no evidence to support this charge of fraud. The District Judge approved this finding as did the Circuit Court of Appeals which said that it had "carefully considered the record in the light of this contention [of fraud]" and concluded that "the estimates submitted by Bethlehem and prepared for it by its representative Brown were fairly and honestly made and as accurate as could be expected under the uncertain conditions then prevailing." And in this Court the petitioner accepts these findings. Therefore, in considering other attacks upon Bethlehem's right to recover, we must do so on the assumption that there was no fraud in Bethlehem's negotiations with the government.

II.

The government contends that even in the absence of fraud, Bethlehem is entitled to nothing by virtue of the half-savings clauses.

One argument is that the contracts gave Bethlehem the benefits of participating in the savings only if Bethlehem by special efforts increased its efficiency and brought actual costs below the estimates agreed to in the contracts.

Neither the specific language of the half-savings provision nor its context supports this contention. On its face, the provision contains an unconditional promise to pay Bethlehem one-half of the difference between the actual and estimated cost of the ships in question. That such a method of computation would tend to discourage careless expenditures and encourage vigorous attempts at realizing economies in building the ships is hardly debatable. But the half-savings clause does not impose any positive obligations upon the builder. The Master found, upon consideration both of the terms of the contracts and testimony on the understanding of the parties, that a showing of savings, without more, obligated the government to share them with Bethlehem. It cannot be maintained that this finding, accepted by both courts below, is without ample support.

Nothing in the negotiations between the parties as revealed in the record indicates that they had a contrary understanding of the contracts. Bethlehem held out against the Fleet Corporation's early insistence upon lump sum contracts. It continually asserted that uncertainties about final cost due to rapidly rising prices would require it to protect itself by insisting upon a figure too high for the Fleet

Corporation's acceptance and therefore itself proposed the cost-plus-fixed-fee-plus-half-savings method of determining compensation. While there seems to have been recognition that this method might induce greater efforts at efficiency which would be to the advantage of both parties, there is not the smallest hint that either Bethlehem or the government regarded the substitution of this method as imposing any positive obligations upon Bethlehem in addition to those it would have had under lump sum contracts.

In the alternative, the government urges that the half-savings clauses are severable, and that if the contracts imposed upon Bethlehem no obligation of special effort to effect savings, these clauses were unsupported by consideration, and are therefore unenforceable. The Master and the courts below, however, treated these clauses as non-severable; to do otherwise would call for departure from accepted principles of the law of contract. Whether a number of promises constitute one contract or more than one is to be determined by inquiring "whether the parties assented to all the promises as a single whole, so that there would have been no bargain whatever, if any promise or set of promises were struck out." Williston on Contracts (rev. ed.) § 863 and cases there cited. The record makes it clear that each of the contracts here was assented to as a single whole, and that consummation of a bargain between the parties depended upon inclusion of the half-savings clause. Furthermore, we know of no federal or state statute or established rule of law in any jurisdiction inconsistent with the elementary proposition that a promise to build ships is good consideration for a promise to pay a sum of money whether fixed in amount or depending upon the relationship between actual and estimated cost.⁸ Cf. *Dayton Airplane Co. v. United States*, 21 F. 2d 673, 682-683.

III.

The government further argues that if the half-savings clauses must be taken as permitting Bethlehem to participate in savings however caused, the contracts are invalid because unconscionable. Without specifying that it relies on the law of any particular jurisdiction, the petitioner rests its argument on an asserted general

⁸ Of the cases called to our attention by the government, only in *Burke & James, Inc. v. United States*, 63 Ct. Cl. 36, was a bonus for savings clause held severable and invalid although regarded as "part and parcel of the original contract." We agree, as did both courts below, with the Master's statement that the *Burke* case is not applicable here because "the facts upon which the decision of that case was based are so different."

doctrine of unconscionability at common law. Since there is no governing constitutional or federal statutory provision, if these were contracts between private individuals, the law of some locality would be controlling. *Erie R. Co. v. Tompkins*, *supra*. Whether the same rule would apply to government contracts in general or to the contracts of the Fleet Corporation⁹ in particular, we need not decide. For assuming the applicability of the *Tompkins* case to the contracts before us, would we have to determine whether the law of the District of Columbia or of some particular state is decisive. For in invoking the asserted doctrine of unconscionability claimed to be applicable here, the government relies entirely upon the alleged existence of two elements: duress and profits grossly in excess of customary standards. And for reasons we shall set out, neither of these two elements exists here.

Duress. The word duress implies feebleness on one side, overpowering strength on the other. Here it is suggested that feebleness is on the side of the government of the United States, overpowering strength on the side of a single private corporation. Although there are many cases in which an individual has claimed to be a victim of duress in dealings with government, e. g., *Union Pac. R. R. Co. v. Pub. Service Comm.*, 248 U. S. 67, this, so far as we know, is the first instance in which government has claimed to be a victim of duress in dealings with an individual.

The argument by which the petitioner seeks to establish that the contracts were made under duress is essentially this: Germany's submarine warfare made it imperative that the government secure the greatest possible number of ships in the shortest possible time; there was a scarcity of ships and shipbuilding facilities in the United States; Bethlehem, the largest shipbuilder in the world, not only had shipbuilding facilities available, but also a trained organization; at a time when Bethlehem's facilities and trained organization were vital to the prosecution of the war, it declined to accept terms proposed by the government, but insisted upon prices which some of the government's representatives thought too high; although Congress had authorized the Executive to commandeer

⁹ The District Court treated the contracts as governed by the law of Pennsylvania. The Circuit Court of Appeals treated them as governed by the law either of Pennsylvania or the District of Columbia, but did not decide which. The Fleet Corporation was organized under the laws of the District of Columbia. Although wholly owned and controlled by the government it has been held subject to suit either in state or federal courts. *Sloan Shipyards v. U. S. Fleet Corp.*, 256 U. S. 549; *Merchant Fleet Corp. v. Harwood*, 281 U. S. 519.

shipbuilding facilities if necessary, Bethlehem's organization was also needed and the government was without power to compel performance by an unwilling organization; the government therefore had to accept contracts on whatever terms Bethlehem proposed or, doing without the ships which Bethlehem could produce, run the risk of military defeat.

Two basic propositions underlie this argument: (1) The government's representatives involuntarily accepted Bethlehem's terms, (2) The circumstances permitted the government no other alternative.

Upon reviewing the negotiations between the representatives of the government and the representatives of Bethlehem, we cannot find support for the first proposition. The Master found, and the courts below agreed, that "the contracts resulted from negotiations in which both parties were represented by intelligent, well informed and experienced officers whose sole object was to make the best trade possible, under conditions which included the uncertainties of war time contingencies, the results from which were not and could not have been known at the time the contracts were made." Two of the three principal negotiators for the Fleet Corporation have testified in the proceedings before the Master. It is abundantly clear from their testimony that, during the course of the negotiations, they did not consider themselves compelled to accept whatever terms the other side proposed. In the disposition of the two main differences between the negotiators there is no evidence of that state of overcomes will which is the major premise of the petitioner's argument of duress. Cf. *French v. Shoemaker*, 14 Wall. 314, 332.

One of the differences was settled by the government's abandonment of its earlier insistence upon a lump sum arrangement together with a guaranteed date of delivery. In view of the rising prices and unpredictable labor supply of the time, Bethlehem's reluctance to enter into contracts on such terms does not seem unreasonable.¹⁰ And if the government's abandonment of its position is to be regarded as evidence of compulsion, we should have to find compulsion in every contract in which one of the parties makes a concession to a demand, however reasonable, of the other side.

¹⁰ Cf.: "Obviously no sane man would bid on a lump-sum contract under such conditions, unless perchance he should treat the matter as a pure gamble and include an excessive margin in his proposal for unforeseen contingencies." Report of Chief of Construction Division, War Department Annual Reports (1919) 4147.

The other major difference between the negotiators was on the matter of price. There is evidence that some of the Fleet Corporation's representatives considered Bethlehem's demands high, but we cannot conclude that the figure finally accepted by the Fleet Corporation was accepted because its representatives felt themselves powerless to refuse. On the contrary, Bethlehem by letter voluntarily offered to accept contracts on terms to be fixed by the Fleet Corporation's general manager. This offer was rejected, one of the Fleet Corporation's negotiators testifying that it preferred to make contracts rather than assume the attitude of dictating terms. Moreover, the general manager of the Fleet Corporation, in whom final authority was vested and who approved these contracts, was of the opinion that high estimated cost figures would be advantageous to the government because "care must be exercised that they be not placed at too low a figure, for if they are, the probabilities are that the contractor will lose interest in keeping the cost down." And one of the negotiators for the Fleet Corporation has given testimony that he was not so much concerned with cost as with speed of production since "legislation was already in the offing in the form of war profit taxes . . . to take care of extreme cases." We must therefore conclude that the negotiations do not show that Bethlehem forced the government's representatives to accept contracts against their will.

If the negotiations do not establish duress, the government finds it in the circumstances themselves. The petitioner concedes that the government could have commandeered Bethlehem's plants, but it contends that if the plants had been commandeered, Bethlehem's organization would have been unwilling to serve the government in them. Heavy reliance is placed on an observation in the Master's report that "the Government did not have power to compel performance by an unwilling organization." We shall later consider the alleged lack of power. We now point out that the alleged unwillingness is an assumption unsupported by findings or evidence. Since the possibility of commandeering appears not even to have been suggested to Bethlehem, we have no basis for knowing what its reaction would have been. We cannot assume that if the negotiations failed to produce contracts acceptable to both sides, Bethlehem would have refused to contribute to the war effort except under legal compulsion. We cannot lightly impute to Bethlehem's whole organization, composed as it was of hundreds of

people, such an attitude of unpatriotic recalcitrance in the face of national peril.

But even if we were to assume, as we do not, an initial attitude of unwillingness, we do not think that the government was entirely without means of overcoming it. For the representatives of the Fleet Corporation, an agent of the United States, came to Bethlehem armed with bargaining powers to which those of no ordinary private corporation can be compared. If it chose to, the Fleet Corporation could have foregone all negotiation over price, compelling Bethlehem to undertake the work at a price set by the President with the burden of going to court if it considered the compensation unreasonably low. And the power to commandeer Bethlehem's entire plant and facilities, in accordance with authority specifically delegated by the President, provided the Fleet Corporation with an alternative bargaining weapon difficult for any company to resist.

The government nevertheless urges that the circumstances here are analogous to those under which courts of admiralty have held contracts to be unenforceable. In particular, it points to the principle that courts of admiralty "will not tolerate the doctrine that a salvor can take advantage of a situation, and avail himself of the calamities of others to drive a bargain; nor will they permit the performance of a public duty to be turned into a traffic of profit." *Post v. Jones*, 19 How. 150, 160. We think this principle has no real relevance to the case before us.

In the first place, if there was a "traffic of profit" here, it was not the unanticipated result of an accident as in the salvage cases. When Congress authorized the procurement of ships through ordinary commercial negotiations, it must have known that the purchases could not be made in a market of open competition because existing shipbuilding facilities would be overtaxed by the construction program. See Department of Commerce, Government Aid to Merchant Shipping (rev. ed. 1923) 493; Hearings before House Committee on the Merchant Marine and Fisheries on H. R. 10500, 64th Cong., 1st Sess., *passim*. And Congress must have anticipated that in the contracts agreed upon profits would be expected and that the self interest inherent in commercial transactions would make itself felt. Therefore, in seeking to establish duress from the circumstances in which these contracts were made, the government is relying on the identical circumstances which were in existence at the time Congress chose the policy of authorizing procurement of ships through commercial negotiation. We cannot now invalidate

contracts made pursuant to a congressionally selected policy on the sole ground of the coercive effect of circumstances which Congress clearly contemplated. To do so we should have to repudiate legislative power exercised in proper constitutional sphere.

In the second place, the captain of a ship in distress on the high seas who is completely at the mercy of his salvor cannot be likened to a sovereign power dealing with an individual contractor. We cannot regard the government of the United States at war as so powerless that it must seek the organization of a private corporation as a helpless suppliant. The Constitution grants to Congress power "to raise and support Armies", "to provide and maintain a Navy", and to make all laws necessary and proper to carry these powers into execution. Under this authority Congress can draft men for battle service. *Selective Draft Law Cases*, 245 U. S. 366. Its power to draft business organizations to support the fighting men who risk their lives can be no less.

Profits. The general common law rule of unconscionability on which the petitioner relies is said to deny enforcement to contracts when the profits provided for are grossly in excess of a standard established by common practice. Whether there is such a rule, what is its scope, and whether it is part of the body of law governing these contracts, we need not decide. For high as Bethlehem's 22% profit seems to us, we are compelled to admit that so far as the record or any other source of which we can take notice discloses, it is not grossly in excess of the standard established by common practice in the field in which Congress authorized the making of these contracts. And in particular, it may be added, the Master found that the ships built by Bethlehem cost the government less than comparable ships built by other shipbuilders. The government made no attempt to establish, nor is there any indication in the record, that the profits realized by other shipbuilders were any less than Bethlehem's.

To establish a standard of customary profits, the petitioner points to the experience of the Navy and War Departments and other branches of the government in connection with straight cost plus contracts. Because 10% was the profit specified in many such contracts, the government asserts that it is an appropriate figure here, and urges that the profits on these contracts, tested by such a standard cannot be allowed. The relevance of experience with cost plus contracts to the contracts here is not clear. The Shipping

Board deliberately chose to avoid cost plus contracts where possible, having found them unsatisfactory in practice. Moreover, the record shows that the total cost to the government of comparable ships under cost plus contracts was higher than the total cost of the ships Bethlehem built under the contracts here in question. And experience in many fields has demonstrated that the percentage of profit actually realized under cost plus contracts is likely to be far more than the percentage specified. As stated in 1918 by Charles E. Hughes, later Chief Justice, in his report to the Attorney General on the aircraft industry, "contracts of this sort lead to waste, foster abuses, and impose an almost intolerable burden of cost accounting, in itself a hindrance to rapid production." Report to the Attorney General on the Aircraft Inquiry (1918) 134. See also, Expenditures in the War Department—Comps, House Report No. 816, 66th Cong., 2d Sess., 49-53. The 10% which the petitioner derives by reference to the cost plus contracts of certain governmental department cannot be taken as a standard of common practice. It is an illusory figure without basis in the realities of business experience.

If profits earned under government contracts in general are taken as the standard of comparison the 22% claimed here is overshadowed in too many instances for it to be regarded as extraordinary. The Hughes report referred to above, for example, points out (pp. 136-146) that most of the airplane production during the last war was under contracts providing for much higher profits. To take an example of the profits made on food products, the Federal Trade Commission determined that in 1917, profits on the sales of salmon canneries, a major portion of whose output was purchased by the government, ranged from 15 to 68% of cost, averaging 52%.¹¹ Federal Trade Commission, Report on Canned Salmon (1918) 63. In the shipbuilding industry itself, even in peace times, profits were found by a special committee of the Senate which investigated the munitions industry to have been from 25% to 37% on the cruisers built in 1927, about 22% in 1929, and of like range for other years. Senate Report No. 944, 74th Cong., 1st Sess., 4.

If the comparison is made with industrial profits, not limited to profits on government contracts alone, the 22% asked for here

¹¹ The Federal Trade Commission Report does not give separate figures on sales to the government, but points out (p. 7) that the government had announced its intention to purchase 80% of the 1918 pack.

likewise lose all claim to distinction. An exhibit, the accuracy of which the government has not challenged, incorporated into the record of this case, indicates that in terms of profit on gross sales, the largest American steel company made 43, 63, and 64% during the years 1916, 1917, and 1918. As computed by the Federal Trade Commission, net earnings in 1917 of the same company on all its business were 25% of total investment, and the Commission cites instances of other steel companies whose earnings thus measured ranged from 30 to 320%. Federal Trade Commission, Letter on Profiteering (1918) 9. Profits of lumber producers, again in terms of return on investment, ranged as high as 121%; and of producers of petroleum products, as high as 122%, over half of the industry earning more than 20%. *Id.* 12, 13. During the first six months of 1917, one of the two major sulphur producers in the country sold its product at an average price of \$18.11 per ton, more than 200% above cost which was \$5.73 per ton; the other major producer earned 236% on its investment during the first eleven months of the same year. *Id.* 11. The Federal Trade Commission's collection of data for various other industries, a collection which the Commission stated was "by no means a complete catalog", affords many additional examples of the same kind. But further confirmation should be unnecessary for a conclusion no businessman would question: that the profits claimed here, seen in their commercial environment, cannot be considered exceptional.

The profits claimed here arise under contracts deliberately let by the Fleet Corporation under authority delegated by the President in accordance with an act of Congress. Neither Congress nor the President restricted the freedom of the Fleet Corporation to grant measures of profits common at the time. And the Fleet Corporation's chosen policy was to operate in a field where profits for services are demanded and expected. The futility of subjecting this choice of policy to judicial review is demonstrated by this case, coming to this Court as it does more than twenty years after the ships were completed. In any event, we believe the question of whether or not this policy was wise is outside our province to decide. Under our form of government we do not have the power to nullify it, as we believe we should necessarily be doing, were we to declare these contracts unenforceable on the ground that profits granted under Congressional authority were too high. The profits

made in these and other contracts entered into under the same system may justly arouse indignation. But indignation based on the notions of morality of this or any other court cannot be judicially transmuted into a principle of law of greater force than the expressed will of Congress.¹²

IV.

The problem of war profits is not new. In this country, every war we have engaged in has provided opportunities for profiteering and they have been too often scandalously seized. See Hearings before the House Committee on Military Affairs on H. R. 3 and H. R. 5293, 74th Cong., 1st Sess., 590-598. To meet this recurrent evil, Congress has at times taken various measures. It has authorized price fixing. It has placed a fixed limit on profits, or has recaptured high profits through taxation. It has expressly reserved for the government the right to cancel contracts after they have been made. Pursuant to Congressional authority, the government has requisitioned existing production facilities or itself built and operated new ones to provide needed war materials. It may be that one or some or all of these measures should be utilized more comprehensively, or that still other measures must be devised. But if the Executive is in need of additional laws by which to protect the nation against war profiteering, the Constitution has given to Congress, not to this Court, the power to make them.

Affirmed.

The CHIEF JUSTICE and Mr. Justice JACKSON, who as former Attorneys General actively participated in the prosecution of these cases, take no part in this decision. Mr. Justice ROBERTS also takes no part in the decision.

¹² Cf.: "It would be very dangerous, indeed, to the best interests of the government . . . if . . . this [Court] should . . . render decrees on the crude notions of the judges of what is or what would be morally right between the government and the individual." *Smoot's Case*, 15 Wall. 36, 45-46.

Mr. Justice MURPHY, concurring.

I concur in the opinion of the Court insofar as it relates to duress and coercion and the non-severability of the "bonus for savings" clauses, but desire to add a brief further statement of my views.

In voting for affirmance of the judgment, I do not wish to be understood as expressing approval of an arrangement like the one now under review, by which a company engaged in doing work for the Government in time of grave national peril—or any other time—is entitled to a profit of 22 per cent, under contracts involving little or no risk and grossing many millions of dollars. Such an arrangement not only is incompatible with sound principles of public management, but is injurious to public confidence and public morale. The fact that such cases were common during the last war, as evidenced by the circumstances recited in the opinion of the Court, provides no justification to my mind for such a practice then or now. No man or set of men should want to make excessive profits out of the travail of the nation at war, and government officials entrusted with contracting authority, and the Congress bestowing such authority, should be alert to prevent it.

The question before the Court for decision, however, is not whether an arrangement like the one presented for review accords with our conceptions of business morality or with correct administration of the public business. Having made a bargain, the Government should be held to it unless there are valid and appropriate reasons known to the law for relieving it from its obligations. It is the duty and responsibility of the courts, not to re-write contracts according to their own views of what is practical and fair, but to enforce them in accordance with the evidence and recognized principles of law.

In my opinion the elements of duress and coercion have not been established in this case. The doctrine that "necessitous men are not free men", a doctrine evolved by the English courts of chancery in the eighteenth century for the protection of harassed debtors,¹ is not applicable to the Government of the United States, armed as it is with both an actual and a potential arsenal of powers adequate to protect its interests in dealings with private persons.

I am also of opinion that the "bonus for savings" clauses are

¹ *Vernon v. Bethell*, 2 Eden 110, 113. And see *Wood v. Abrey*, 3 Maddock's Chan. 216; *Underhill v. Horwood*, 10 Ves. 209.

integral parts of the contracts in question and part of the entire consideration moving to Bethlehem in exchange for its promise to build ships. To characterize these clauses as severable and supported by consideration only if Bethlehem promised to increase its efficiency is ingenious, but requires us to close our eyes to the actualities of the record before us and to ignore fundamental contract law.

Nor can I accept the proposition that the "bonus for savings" clauses are properly interpreted as meaning that Bethlehem was to receive one-half of the "savings" only insofar as Bethlehem could prove that the "savings" were due to its increased efficiency. Such an interpretation, it is true, would prevent Bethlehem from benefitting by reason of purely fortuitous "savings". However, in the absence, as here, of fraud, mistake, or that overreaching which we label "duress" and "coercion", contracts should be interpreted as they are written, not as they might or should have been written in the light of after-thought and subsequent experience. The language of the "savings" clauses does not limit Bethlehem's participation in "savings" to those attributable only to its own efforts. The Master found that "Bethlehem was to participate in savings however earned". The suggested interpretation, ignoring the language of the contracts and the expressed understanding of the parties, gratuitously rewrites the contracts to accord with notions of fairness acquired in the light of subsequent developments.

It is understandable that one may be indignant at Bethlehem's claim, but such indignation does not justify the distortion of established legal principles to relieve the Government of its approval of a hard bargain. It cannot be left out of consideration that the Government entered into the agreements with full understanding of their terms. Surely there is much to be said in favor of the Government's standing behind obligations, even though quite onerous, which it incurred with knowledge of the circumstances. The possibility that the Government may be relieved of bargains twenty-four years after agreeing to them is not conducive to mutual trust and confidence between citizens and their government.

The judgment should be affirmed.

Mr. Justice FRANKFURTER, dissenting.

The Founders divided our government into three branches, partly to prevent autocratic concentration of power and partly to achieve appropriate division of labor in the difficult task of government. The President has his duties, the Congress its duties, and we ours. What powers the Congress should give the President in order to obtain the most effective production of war supplies, how the President should exercise those powers, whether a system of private contracts for war materials is conducive to unjustifiable waste and profiteering, or whether government production of necessary war supplies is a wiser course—these and like matters are not our business and upon them we should neither express nor intimate views. However circumscribed the judicial area may be, we had best remain within it. But the function of the judiciary is not so limited that it must sanction the use of the federal courts as instruments of injustice in disregard of moral and equitable principles which have been part of the law for centuries. I am compelled, therefore, to dissent from the judgment of the Court.

In the summer of 1917 the United States was at war with Germany. The enemy's submarine was taking terrific toll of our shipping. The immediate threat to our national security had to be met promptly. Congress enacted the Emergency Shipping Fund Act of June 15, 1917, 40 Stat. 182, conferring vast powers upon the President. He was authorized to place orders for such ships or material as "the necessities of the Government" may require; to modify, suspend, cancel or requisition contracts for the building, production, or purchase of ships or material; and to take over any plants and ships constructed or in the process of construction. If any person owning any ship, plant, or material refused to build or sell ships or material ordered by the Government "at such reasonable price as shall be determined by the President", he was empowered to take possession of the ships, material, or plant of such person.

On July 11, 1917, the President delegated all the authority vested in him by this Act to the United States Shipping Board Emergency Fleet Corporation. A stupendous task was thereby imposed upon the Fleet Corporation. "The program of construction, as well as operation was gigantic. It involved an expenditure of more than three and a half billion dollars, a sum greater than any expended

by any corporation in a similar period of time. Many of the officials and board members were without experience in either shipbuilding or operation. No adequate organization existed at the beginning. A complete organization to carry out its large program had to be created. There was a shortage of shipbuilding skill as well as shipbuilding facilities. The need for ships was imperative and constantly increased during the combat period." Report of the Select Committee on U. S. Shipping Board Operations, H. Rep. No. 1399, 66th Cong., 3d Sess., p. 24.

Bethlehem was the largest shipbuilding company in the world. Its five subsidiaries and their plants were experienced shipbuilders, with efficient and well-equipped organizations. As the Master in this case found, "it was understood by all parties concerned that the Fleet Corporation shipbuilding program would call for capacity production at each of Bethlehem's shipyards". Of course the Government had the power to take over Bethlehem's shipyards and plants. But the United States was at war. It needed ships—and it needed them at once. The shipyards and plants of a recalcitrant shipbuilder would not produce the necessary tonnage, at least not in the needed time, without an organization able to operate them at maximum efficiency. The Master found that "A failure to induce Bethlehem to undertake the shipbuilding program covered by these contracts, followed by the taking possession by the Fleet Corporation of the Bethlehem plants, could not have accomplished the desired result. It was Bethlehem's organization that was necessary to insure success to the shipbuilding program of the Fleet Corporation and, as the Government did not have the power to compel performance by an unwilling organization, if Bethlehem demanded its price on the basis of substantial commercial profits rather than contribute such services on a patriotic basis, the Government was obliged to take the contracts on such basis or not at all."

Bethlehem does not deny that in these negotiations the Government's legal power to requisition its shipyards was, for purposes of bargaining, an empty weapon. "It is also true," Bethlehem admits, "that, although the Fleet Corporation had the power to take over Bethlehem's yards, what it really required for the carrying out of its program was the use of Bethlehem's organization—its knowledge of how to build ships." The representatives of both Bethlehem and the Fleet Corporation knew that the Government

did not regard its power to requisition plants and shipyards as a satisfactory alternative to making contracts with private shipbuilders for the construction of ships.¹ It is not for us to say that the Government should not have determined upon such a policy. It is enough that when these contracts were made, none of the parties believed that there was open to the Government the feasible alternative which now, twenty-five years later, this Court says was open to it.

This was the setting in which the contracts in suit were made. Bethlehem was represented throughout the negotiations by Joseph W. Powell, its vice president and operating manager, and Harry Brown, its technical manager, described by the Master as "two of the ablest and most experienced shipbuilders and estimators of shipbuilding costs in the United States". On behalf of the Fleet Corporation the active negotiators were Admiral E. T. Bowles, manager of its division of steel ship construction, and G. S. Radford, manager of its contract division. The Master characterized Bowles and Radford as "equally competent shipbuilding experts". However, they were not empowered to conclude contracts on behalf of the Fleet Corporation. That ultimate authority belonged to Charles Pier, the vice-president and general manager of the Fleet Corporation. Pier was a business man who had had no previous shipbuilding experience, and the Master found that "At the time of the negotiations relating to the contracts in controversy, the relations between Powell and Pier were very close. Pier, as Powell knew, had had no shipbuilding experience whatsoever, had implicit confidence in Powell's integrity and shipbuilding ability and experience, and was accustomed to look to him for information and assistance with respect to matters of shipbuilding."

¹ Whatever the scope and importance of the Government's requisitioning power in other situations (compare Baruch, *American Industry in War*, p. 77, with Sen. Rep. No. 944, 74th Cong., 1st Sess., pt. 2, pp. 4-5, 111-15), it was without significance in the Fleet Corporation's shipbuilding program. The reports of the Shipping Board show that the exercise of the power was limited to the requisition of vessels which had been built or were being constructed; the power does not seem to have been employed to take over the shipyards of recalcitrant private contractors. Indeed, the policy of the Government, based upon its wartime needs, was to encourage, financially and otherwise, the construction and maintenance of shipyards by private interests. See 1st Annual Report of the U. S. Shipping Board (1917) pp. 12-16; 2d Annual Report (1918) pp. 23-26, 120-22; Report of Director General Charles Pier to the Board of Trustees of the U. S. Shipping Board Emergency Fleet Corporation (April 30, 1919) pp. 12-14, 75, 123; Report of the President of the U. S. Shipping Board Emergency Fleet Corporation to the Board of Trustees (August 1, 1919) pp. 25-26.

Following a conference in Washington on June 15, 1917, attended by Powell and other shipbuilders, the General Manager of the Fleet Corporation requested Bethlehem to submit formal proposals for the construction of ships. Throughout the entire negotiations which followed, the Fleet Corporation tried to persuade Bethlehem to enter into "lump-sum" contracts. Powell refused, insisting upon the so-called "half-savings" form of contract which he had originated. He set forth his proposals in his letter of December 13, 1917, to the Fleet Corporation: "Because of the unprecedented conditions surrounding the Labor and Material market, it is impracticable to estimate within a reasonable percentage what will be the actual cost of construction, and it is therefore impossible to submit fixed prices for any of these vessels, except upon a basis so far above estimated cost that any figure acceptable to this Company would not be acceptable to the Emergency Fleet Corporation. It is proposed, however, that they be constructed on the basis of actual cost plus a fee, with an agreed upon probable cost, this Company to be paid in addition to the fee one-half of any saving that may be made below this cost figure, and with the further provision that the estimated cost figure will be increased due to any increase in rates of wages that may be approved by the Emergency Fleet Corporation."

After further conferences, Powell submitted a proposal, dated December 19, 1917, specifying the estimated costs and fixed fees of the vessels to be constructed. On the morning of January 3, 1918, before the Fleet Corporation had expressed any views on the proposal of December 19, Powell handed Piez a letter, dated January 3, 1918, offering to construct a greater number of vessels than was specified in his earlier proposal. The letter concluded "that while this company cannot undertake any capital expenditures at its expense, if the terms in our proposal do not otherwise meet with the Emergency Fleet Corporation's approval, we are prepared to accept the order to construct these vessels on such terms as may be personally determined by Mr. Charles Piez, the Vice President and General Manager, and strongly urge there be no delay in placing this order, as we are making this offer because of our knowledge of the vital emergency now confronting this nation in connection with the requirements for additional merchant vessels."

Upon receipt of this letter, Piez arranged a conference between Powell, Brown, Bowles, and Radford, which occurred on the afternoon of January 3. But Bowles and Radford did not know, and

neither was informed before or during the conference, of the offer made to Piez in Powell's letter of January 3. It can hardly be said, therefore, that this letter, neither addressed to nor made known to the real negotiators for the Government, was a factor in their negotiations.

At the conference, which lasted about five hours, Bowles again attempted to persuade Powell to undertake the construction upon a lump-sum basis. Powell was adamant, however, and Bowles had to acquiesce in the half-savings form of contract in order to reach any agreement. Powell insisted that the estimates previously submitted by Bethlehem were fair and reasonable. Neither Bowles nor Radford submitted any estimates or counter-proposals, "their criticism being limited to the opinion expressed by Bowles that the original and reduced estimates submitted by Powell were too high". Powell made several reductions in the estimates, and in response to Bowles' inquiry, Brown assured him that the estimates were about as accurate as could be made under the circumstances. Bowles and Radford thereupon agreed to the prices, subject to confirmation by Piez. On the same day they handed Piez the following memorandum:

"We hand you herewith the Bethlehem Shipbuilding Corporation's proposal dated December 19, for additional construction at their various plants, amounting in all to 19 vessels, exclusive of tugs. It may be noted that, with the exception of three ships, the vessels in question are troop ships and tankers—ships of a type that only real shipbuilders can produce satisfactorily. As is well known, we have been having difficulty in placing such vessels.

"We wish to place on record the fact that the Bethlehem Shipbuilding Corporation's representatives have insisted on comparatively high prices for these vessels; that they have only with difficulty been persuaded to quote us on the types of ships referred to; and, that their attitude has been characterized by an arbitrary refusal to guarantee or stand behind delivery dates. In other words, it was difficult to persuade them to quote even a tentative delivery date, and they refused positively to accede to a bonus and penalty clause for delivery.

"The letter herewith, addressed to the Bethlehem Shipbuilding Corporation, in reply to their proposal, has been prepared for your signature and is now presented with the recommendation that it be signed. While the prices we have agreed to, with representatives of the Bethlehem Shipbuilding Corporation, are not satisfactory to us, nevertheless, they represent a material reduction from the prices quoted by that Corporation. Realizing that the

Nation will need these vessels we have been actuated by the belief that further delay in placing the contracts should be eliminated and we believe we have made the best compromise possible under very difficult conditions."

As a consequence of these negotiations, the thirteen contracts here in controversy were executed, seven on February 1, 1918, and six thereafter.

The provisions of these contracts demand careful analysis. The contract marked No. 183, calling for the construction by Bethlehem of three steel tank vessels each weighing about 9,100 tons, is typical.

In order to provide the sums necessary for carrying on the work under the contract, the Fleet Corporation agreed to deposit in advance "such sums as may be necessary to constitute and keep constituted a fund from which to finance the work, to provide for payments to be made for materials, and for wages and salaries of persons employed upon the work hereunder." The Fleet Corporation agreed also to assist Bethlehem "to secure with the utmost practicable expedition and at the minimum cost consistent with the existing conditions, the facilities, utilities, parts, materials and supplies required for the work under this contract". The price to be paid for each vessel was defined to include (a) the "actual cost", plus (b) a fixed fee of \$185,000, plus (c) one-half the amount by which the actual cost of each vessel should fall short of an estimated cost of \$1,865,000.

It would be difficult to draft a more inclusive definition of "cost" than that contained in this contract. "Actual cost" was defined to include the following items, as well as "items similar thereto in principle": (a) the net costs of labor (including bonuses), materials, machinery, equipment, and supplies furnished by Bethlehem, and all other direct charges, such as insurance on the vessels, etc.; (b) a "proper proportion" of running expenses, including rentals, cost of repairs and maintenance, light, heat, power, insurance, management, salaries (including bonuses), and all other indirect charges; (c) a "proper proportion" of interest accrued on bonds, loans, or other debts existing or previously made, the proceeds of which "shall be used, or shall have been or shall be invested in plant, equipment, etc., that shall be used," in the performance of the contract; (d) a "proper proportion" of taxes of all kinds, except federal taxes, with respect to the business or property; (e) a "proper proportion" of physical losses sustained in connection

with the construction of the vessels under the contract, including losses from fire, flood, storm, riot, vandalism, acts of God, acts of war, or other casualties; and (f) a "reasonable" allowance for depreciation of property and plants used in connection with the construction under the contract.

The Master found that under the "half-savings" clause Bethlehem was entitled to receive one-half the difference between the estimated cost and the actual cost, regardless of how this difference was achieved. Bethlehem was therefore not required to show that the "savings" were attributable to its efforts to increase efficiency.

Since the estimated costs of construction specified in the contracts are crucial in fixing the extent of Bethlehem's profits, it is necessary to consider how they were determined. According to the explanation furnished by Bethlehem, Brown prepared the estimated costs specified in Bethlehem's letter of December 19, 1917, as follows: As the basis of his estimate he took the cost of constructing Hull 253, a 9,100 ton tanker which had recently been completed at the Fore River yard. The cost of the material in Hull 253 was about \$389,000, consisting of \$150,000 for the steel structure and \$239,000 for the remaining material. Brown estimated that the cost of the material in a similar tanker to be constructed in 1918 would be \$817,000, including \$399,000 for the steel structure and \$418,000 for the remainder. His estimate assumed an increase in freight rates and costs of delivery of 42%. The next item was the cost of labor, which on Hull 253 amounted to 38.75 cents per hour. Brown assumed that wage scales would rise to 50 cents per hour, an increase of 29%, and that efficiency would decrease about 30%. Therefore, he estimated a total labor cost of \$548,000, as compared with the actual labor cost upon Hull 253 of \$326,000. Similarly, the estimates of plant operating expenses were computed on the basis of equally large assumed increases. The total estimated cost of material, labor, operating expenses, and overhead amounted to \$1,694,000, to which Brown added a flat 10% allowance to cover items such as armed guard equipment and "to make allowance for other contingencies", making a total estimated cost of \$1,863,000, or approximately \$205 per ton. To this figure Powell added an additional \$10 per ton because, as he testified, "there was an item of increased cost of steel, which represented a contract for

very high-priced steel that we had to use in connection with this program, and which amounted to about \$2.50 a ton spread over the program that we expected to undertake. That was a very rough figure. Whatever else I put on I put on because I knew I was going to have to trade the final contract out with Admiral Bowles and I knew I would not get what I asked for, and if I did not ask for more than I expected I would not get out where I wanted to be." Brown testified that "He [Powell] took the figures that I gave him and added \$10 a ton to it" for some reason which he could not recall.

The estimated cost finally specified in the contract for the construction of the three vessels was \$1,865,000; the estimated cost of such vessels proposed in Powell's letter of December 19, 1917, was \$1,983,800, a difference of \$118,800, or less than 6% of the proposed estimate.

The Master found that during the negotiations the Fleet Corporation was uninformed as to the probable cost of materials and labor, Bethlehem's overhead and operating expenses, and depreciation and similar charges. Consequently, at the conference of January 3, 1918, from which emerged the contracts in controversy, the representatives of the Fleet Corporation did not submit any counter-offers to Bethlehem; they merely insisted that Bethlehem's estimates were too high. Brown's testimony is illuminating as to the nature of the bargaining at the conference:

"Q. Now I am asking you whether with respect to these vessels Admiral Bowles submitted any price of his own?

"A. No, sir.

"Q. Did he ask you how your estimates were made up?

"A. No, sir.

"Q. Did he ask you to justify your estimates in any way?

"A. No, sir.

"Q. He just objected to them repeatedly and said they were too high?

"A. Yes, sir.

"Q. But did not ask you to justify them?

"A. No, sir.

"Q. Until Powell finally came down to a figure which Bowles was willing to accept?

"A. Well, I should put it this way; to a figure which Mr. Powell refused to go below."

The total estimated costs of construction in the thirteen contracts in controversy amounted to \$119,750,000. The total actual costs,

as defined in the contracts, were \$92,390,521. The estimated costs therefore exceeded the actual costs by \$26,759,479, or, to put it another way, the estimated costs were almost 29% greater than actual costs. Nowhere in the long record, as the Master found, is there any explanation or justification for the tremendous disparity between the estimated costs submitted by Bethlehem, or those specified in the contracts, and the actual costs.

Bethlehem's profits under these contracts amount to approximately \$24,000,000, or about 22% of actual costs including extra work. In two of these contracts, Nos. 191 and 226, its profits exceeded 34% and 32%, respectively. Moreover these figures do not include the profits made by Bethlehem Steel Company, an affiliate, on the sales to Bethlehem at the maximum prices permitted by the War Industries Board of 43,000 tons of steel used in the construction of ships under these contracts.

To speak of Bethlehem's profits as only 22% is in any event misleading. The profits are 22% of "cost", and not 22% of what might fairly be described as Bethlehem's capital investment in these contracts. For under these contracts Bethlehem took absolutely no risk of loss; in addition, the Government agreed to advance all sums necessary to finance the construction of the vessels. Even in usurious transactions the lender takes the risk of the borrower's insolvency. Here Bethlehem took no risks at all.

Bethlehem has already received from the Government the total costs of construction (including items for wage increases and extra work), plus fixed profits of \$11,962,400 (representing about 11% of the actual costs including extra charges), plus bonuses of \$8,093,157 under the half-savings clause (over 7% of costs). It has thus received total profits of more than \$20,000,000 under these contracts. In the present suits it is seeking additional sums of more than \$7,500,000, of which about \$3,800,000 represents bonuses under the contracts in question. In sustaining the judgments of the lower courts, this Court is awarding Bethlehem further profits of about 4% on these contracts.

The Master expressly found that it was essential that Bethlehem undertake to build the vessels provided for in the contracts, and that since the Government needed Bethlehem's organization, it had no satisfactory alternative. It had to make the contracts on Bethlehem's terms or not at all. He concluded, nevertheless, that since "the Fleet Corporation made the contracts with open eyes, al-

though resenting the commercial attitude of Bethlehem and condemning Bethlehem for demanding its 'pound of flesh', the contracts were enforceable by Bethlehem in the absence of any proof of fraud.

The District Court concurred in the proposition that the absence of fraud made the contracts invulnerable. But its conclusion is contradicted by its findings: "The managers for the contractor adopted the famous Rob Roy distinction who admitted he was a robber but proudly proclaimed that he was no thief. The contractor boldly and openly fixed the figures in the estimated cost so high as to give them the promise of large bonus profits. The managers for the Fleet Corporation knew that the estimate was high and why it was made high and so protested it. The reply of the contractor's managers was, 'We will take the contract with this promise of bonus profits incorporated in it but not otherwise. You take it or leave it'. Whatever wrong there was in this, may have been the wrong in a daylight robbery but there was no element of deception in it." 23 F. Supp. 676, 679.

Similarly, the affirmance of the Circuit Court of Appeals appears to have been based upon the assumption that the government's failure to show fraud was fatal: "It is of course obvious that these negotiations took place in time of war when the need of the Government for ships was extremely urgent and the necessity of reaching an agreement with Bethlehem, therefore, vital. It is equally clear that Bethlehem insisted upon assuring itself a margin of profit which in view of the necessities of the Government was so large as to indicate an attitude of commercial greed but little diluted with patriotic feeling. There is no doubt that this attitude on the part of Bethlehem was deeply resented by the Government representatives but the latter were faced with the alternative of either agreeing to Bethlehem's terms or taking possession of its shipyards and having the Government itself construct the vessels. We think the record clearly indicates that the Government representatives felt that the latter course could not have accomplished the shipbuilding program with the speed which was essential. It was Bethlehem's existing shipbuilding organization that was necessary to insure success to the program of the Fleet Corporation. Consequently the Government representatives, feeling as they did that Bethlehem's organization was necessary to their program, were obliged to accept the terms offered by Bethle-

hem. This they did with full knowledge, as we have said, that the estimated cost figures included in the contracts did not represent close approximations but were so prepared as to assure to Bethlehem substantial additional profits by way of the bonus for savings. It follows that while Bethlehem may be condemned for having taken advantage of the Nation's necessities to secure inordinate profits it cannot be charged with having misrepresented the facts to the Government's representatives." 113 F. 2d 301, 305-06.

Thus, not less than six times did the Circuit Court of Appeals declare that the unconscionable terms of this contract were forced upon the Government by the dire necessities of national self-preservation. Nevertheless the Court found itself impotent to resist the demand that the courts themselves become the means of realizing these "inordinate profits". But law does not subject courts to such impotence. Courts need not be the agents of a wrong that offends their conscience if they heed the commands of law.

In England prior to 1285 (Statute of Westminster II, 13 Edw. I, c. 50) suitors were frequently "obliged to depart from the Chancery without getting writs, because there are none which will exactly fit their cases, although these cases fall within admitted principles." Maitland, *Forms of Action at Common Law*, Lect. IV (1936 ed.) p. 51. Today it is held that because the circumstances of this case cannot be fitted into a neatly carved pigeonhole in the law of contracts, "daylight robbery", exploitation of the "necessities" of the country at war, must be consummated by this Court. It is said that familiar principles would be outraged if Bethlehem were denied recovery on these contracts. But is there any principle which is more familiar or more firmly embedded in the history of Anglo-American law than the basic doctrine that the courts will not permit themselves to be used as instruments of inequity and injustice? Does any principle in our law have more universal application than the doctrine that courts will not enforce transactions in which the relative positions of the parties are such that one has unconscionably taken advantage of the necessities of the other?

These principles are not foreign to the law of contracts. Fraud and physical duress are not the only grounds upon which courts refuse to enforce contracts. The law is not so primitive that it sanctions every injustice except brute force and downright fraud. More specifically, the courts generally refuse to lend themselves to the en-

enforcement of a "bargain" in which one party has unjustly taken advantage of the economic necessities of the other. "And there is great reason and justice in this rule, for necessitous men are not, truly speaking, free men, but, to answer a present exigency, will submit to any terms that the crafty may impose upon them." *Vernon v. Bethell*, 2 Eden 110, 113. So wrote Lord Chancellor Northington in 1761.

The fact that the representatives of the Government entered into the contracts "with their eyes wide open" does not mean that they were not acting under compulsion. "It always is for the interest of a party under duress to choose the lesser of two evils. But the fact that a choice was made according to interest does not exclude duress. It is the characteristic of duress properly so called." Holmes, J., in *Union Pac. R. R. Co. v. Pub. Serv. Comm.*, 248 U. S. 67, 70. In that case a state unconstitutionally exacted a fee for a certificate of authority to issue railroad bonds. A railroad which had paid the fee and obtained a certificate, rather than run the risk of subsequent invalidation of its bonds and imposition of serious penalties, was held to have been coerced into making the payments. In *Swift Company v. United States*, 111 U. S. 22, 29, the taxpayer's only alternatives were "to submit to an illegal exaction, or discontinue its business". The payment of the tax in these circumstances was held to be under duress. See also *Ward v. Love County*, 253 U. S. 17, 23. The courts generally regard the dilemma of the taxpayer who must either pay the taxes or incur serious business losses as a species of duress. E.g., *Morgan v. Palmer*, 2 Barn. & C. 729; *Ripley v. Gelston*, 9 Johns. 201; *Scottish U. & N. Ins. Co. v. Herriott*, 109 Iowa 606; see Notes, 64 A. L. R. 9, 84 A. L. R. 294.

Underlying all these cases is the law's recognition of a basic psychological truth. In *Atkinson v. Denby*, 7 Hurlst. & N. 934, 936, Cockburn, C. J., said that "Where the one person can dictate, and the other has no alternative but to submit, it is coercion". See also Abbott, C. J., in *Morgan v. Palmer*, 2 Barn. & C. 729, 735: "But if one party has the power of saying to the other, 'that which you require shall not be done except upon the conditions which I choose to impose,' no person can contend that they stand upon anything like an equal footing." And these were decisions in days when law was supposed to be much more rigid and more respectful of forms than we now ordinarily deem just.

The fundamental principle of law that the courts will not enforce a bargain where one party has unconscionably taken advantage of the necessities and distress of the other has found expression in an almost infinite variety of cases. See *Lomergan v. Buford*, 148 U. S. 581, 589-91; *Snyder v. Rosenbaum*, 215 U. S. 261, 265-66. Perhaps the most familiar is the situation of the mortgagor who under the pressure of financial distress conveys his equity of redemption to the mortgagee. The courts will scrutinize the transaction very carefully, *Villa v. Rodriguez*, 12 Wall. 323, 339, and if it appears that the mortgagee has taken unfair advantage of the other's position, the conveyance will not be enforced. Compare *Vernon v. Bethell*, 2 Eden 110; *Glose v. Phipps*, 7 M. & G. 586; *Richardson v. Barrick*, 16 Iowa 407.

Similarly, an heir or remainderman who is compelled by financial circumstances to sell his expectancy for a song may recover it if the vendee has unduly exploited the other's distress. *Wood v. Abrey*, 3 Maddock's Chan. 216, 219 (where the Vice-Chancellor, Sir John Leach, said: "If a man who meets his purchaser on equal terms, negligently sells his estate at an under value, he has no title to relief in equity. But a Court of Equity will inquire whether the parties really did meet on equal terms; and if it be found that the vendor was in distressed circumstances, and that advantage was taken of that distress, it will avoid the contract."); *Underhill v. Harwood*, 10 Ves. Jr. 209; *M'Kinney v. Pinckard*, 29 Va. 149; *Butler v. Duncan*, 47 Mich. 94; *Brown v. Hall*, 14 R. I. 249. In *Administrators of Hough v. Hunt*, 2 Ohio 495, 502, a person heavily in debt, in order to obtain a further loan with which to meet debts falling due, agreed to buy land at more than double its value. The court found that the lender had unjustly taken advantage of the borrower's necessities and therefore rescinded the contract: "The rule in chancery is well established. When a person is encumbered with debts, and that fact is known to a person with whom he contracts, who avails himself of it to exact an unconscionable bargain, equity will relieve upon account of the advantage and hardship." This was written in 1826. To the same effect are *Vyne v. Glenn*, 41 Mich. 112, and *Bither v. Packard*, 115 Maine 306.

Another class of cases in which this principle has been applied arises where a customer of a gas or electric company pays charges which he asserts he is not obligated to pay, rather than have his

service disconnected. Payments made in such circumstances are regarded as coerced. See *Boston v. Edison Electric Illuminating Co.*, 242 Mass. 305, 310; *Westlake & Button v. St. Louis*, 77 Mo. 47; Note, 34 A. L. R. 185.

Cobb v. Charter, 32 Conn. 358, illustrates another type of controversy in which the courts have given effect to the historic principle of duress which is now seemingly rejected as an innovation. The defendant there had possession of a chest of tools belonging to the plaintiff, a mechanic. He refused to give up the chest, which the plaintiff needed in order to ply his trade, unless the latter would pay a bill for which he denied responsibility. The plaintiff's payment of the bill in these circumstances was held to have been made under duress. Accord: *Louergon v. Buford*, 148 U. S. 581, 589-91; *Fenwick Shipping Co. v. Clarke Bros.*, 133 Ga. 43; *Stanton v. Jerome*, 54 N. Y. 480; *Harmony v. Bingham*, 12 N. Y. 99.

In *Stiefler v. McCullough*, 97 Ind. App. 123, a merchant who had to obtain a loan in order to remain in business agreed to pay the president of a bank an exorbitant sum in consideration for his services in procuring a loan. The court refused to enforce this agreement as unconscionable. Similarly, in *Niedermeyer v. Curators of State University*, 61 Mo. App. 654, a student paid tuition fees which he regarded as excessive, and which he did not believe he was required to pay under his contract with the university, only because he feared expulsion for non-payment. This payment was held to have been made under duress and hence recoverable. Cf. *Baldwin v. Sullivan Timber Co.*, 20 N. Y. Supp. 496; *Kelley v. Coplice*, 23 Kans. 474.

Strikingly analogous to the case at bar are the decisions that a salvor who takes advantage of the helplessness of the ship in distress to drive an unconscionable bargain will not be aided by the courts in his attempts to enforce the bargain. *Post v. Jones*, 19 How. 150, 160; *The Tornado*, 109 U. S. 110, 117; *The Elfrida*, 172 U. S. 186, 193-94. In *Post v. Jones*, *supra*, it was said that the courts "will not tolerate the doctrine that a salvor can take the advantage of his situation, and avail himself of the calamities of others to drive a bargain; nor will they permit the performance of a public duty to be turned into a traffic of profit". These cases are not unlike the familiar example of the drowning man who agrees to pay an exorbitant sum to a rescuer who would otherwise permit

him to drown. No court would enforce a contract made under such circumstances.²

To deny the existence of duress in a Government contract by ironic reference to the feebleness of the United States as against the overpowering strength of a single private corporation is an indulgence of rhetoric in disregard of fact. The United States with all its might and majesty never makes a contract. To speak of a contract by the United States is to employ an abstraction. We must not allow it to become a blinding abstraction. Contracts are made not by 130 million Americans but by some official on their behalf. Because the national interest is represented not by the power of the nation but by an individual professing to exercise authority of vast consequence to the nation, action by Government officials is often not binding against the Government in situations where private parties would be bound.³ The contracts here were not made by an abstraction known as the United States or by the millions of its citizens. For all practical purposes, the arrangement was entered into by two persons, Bowles and Radford. And it was entered into by them against their better judgment because they had only Hobson's choice—which is no choice. They had no choice in view of the circumstances which subordinated them and by which they were governed, namely, that ships were needed, and needed quickly, and Bethlehem was needed to construct them quickly. The legal alternative—that the Government take over Bethlehem—was not an actual alternative, and Bethlehem knew this as well as the representatives of the Government.

The suggestion is made that Bethlehem's profits under these contracts were not exceptional when compared with the profits made under similar contracts, and that the enormous profits claimed by Bethlehem under these contracts cannot be regarded as

² The books are full of cases in which courts have refused to lend themselves as collecting agencies of contracts made under circumstances offensive to the conscience. See, for example, in addition to the cases cited in the text, *Johnson v. Ford*, 147 Tenn. 63; *Harris v. Cary*, 112 Va. 262; *Northwestern Mut. Life Ins. Co. v. Barker*, 241 Ky. 400, 407; *Caivano v. Brill*, 171 Misc. 298.

³ E. g., the right to recover money paid under mistake of law, *Wisconsin Central Railroad v. United States*, 164 U. S. 190, 212, and the unavailability against the Government of the defenses of laches or neglect of duty, *United States v. Kirkpatrick*, 9 Wheat. 720, 735, and estoppel based on unauthorized acts of its agents, *Lee v. Monroe*, 7 Cranch 366; *Utah Power & Light Co. v. United States*, 243 U. S. 389, 408-09.

supporting the inference that Bethlehem took advantage of the Government's distress. But the only contracts before us are those involved in this litigation. There is nothing in this record which enables us to say that although these contracts are unconscionable, all contracts made by the Government during the same period were no less unconscionable. And even if this were so, it would be no argument that this Court should give its sanction to these contracts by making itself the instrument for realizing the unconscionable profits. What little light the record does cast upon contemporary contracts gives no justification for regarding these contracts as typical. The policy of Charles M. Schwab, Director General of the Fleet Corporation, was to make contracts providing for a maximum profit of 10%, out of which all federal taxes would have to be paid. See Letter of Oct. 2, 1918, to Edward N. Hurley, Chairman of the Shipping Board, relating to contracts with the American Shipbuilding Company.

If we are to go outside the record, the evidence is confusing and unreliable. It must be borne in mind that Bethlehem took no risk of loss, that under the contracts it was protected from the risks of rising costs of labor, materials, transportation, etc., that under the contracts it was not required to make any capital expenditures, that the Government agreed to advance all sums that should be necessary for the performance of the contracts. It is idle to compare the profits made by Bethlehem under these contracts with profits made by industrial concerns of various types under different types of contracts. Such figures are statistical quicksand unless we are told also that in each case the contractor was not required to make any capital investment, that he was insured against normal business risks, and that he was guaranteed a profit, regardless of any change in circumstances.

We know that the policy of the Navy Department with respect to so-called straight cost-plus shipbuilding contracts was to allow profits of 10% of actual cost. See Annual Report of the Secretary of the Navy (1917) p. 33; Annual Report (1918) p. 685; Annual Report (1919) pp. 572-76; Annual Report (1920) pp. 147-48. We know that, similarly, the policy of the War Department with respect to cost-plus contracts for the construction of cantonments was to allow profits not exceeding 10% of cost. See Annual Report of the Secretary of War (1917) vol. 1, p. 28; Annual Report (1918) vol. 1, p. 1319; Annual Report (1919) pp. 4138-42. See also Crowell,

Government War Contracts, p. 85 (in "emergency building contracts" a sliding scale of profits was employed, ranging from cost plus 7% on contracts less than \$100,000 to cost plus 2½% on contracts more than \$10,000,000). Similarly, contracts for the construction of buildings to house war workers were let on the basis of cost plus 2½% on contracts over \$1,000,000, and 3½% on contracts under \$1,000,000. See testimony of Otto M. Eldlitz, President of the U. S. Housing Corporation, Hearings before the subcommittee of the Senate Committee on Public Buildings and Grounds pursuant to S. Res. 371, 65th Cong., 3d Sess., p. 35.

These statistics obviously do not tell the whole story of Government contracts in the last war. But they indicate plainly enough that this Court should not accept, as a basis for decision in this case, the premise that Bethlehem's profits were conventional when compared with profits made in comparable transactions.

It is said, further, that even if these contracts are unenforceable when measured by standards of justice and equity enforced by the courts for centuries, nevertheless this Court must enforce the contracts now before us because Congress and the President specifically authorized such a traffic in profits. The suggestion is not consistent with historical fact.

The legislative history of the Emergency Shipping Fund Act furnishes no support for the contention that in conferring upon the President authority to enter into contracts for the construction of ships, Congress thereby commanded the courts to enforce all contracts that were made, without regard to their provisions and the circumstances under which they were negotiated. On the contrary, the debates contain many indications that Congress expected that the shipbuilders of the nation would provide their services for a reasonable compensation, and that the power conferred upon the President to take over shipyards would not be exercised. See remarks of Senator Knox, 55 Cong. Rec. 2518; Senator Calder, 55 *id.* 2529; Rep. Fitzgerald, 55 *id.* 3018. Indeed, the Act itself specified that ships should be built "at such reasonable price as shall be determined by the President". 40 Stat. 182, 183.

The National Defense Act, 39 Stat. 166, 213, specifically provided that "The compensation to be paid to any individual, firm, . . . for its products or material, or as rental for use of any manufacturing plant while used by the United States, shall be fair and just." There can be no clearer indication that Congress did

not authorize or approve any policy of trafficking in profits. The fact that Congress took care to ascertain whether the war agencies were letting contracts under which excessive profits were being made, see Hearings before subcommittee of the House Committee on Appropriations on H. R. 3971, 65th Cong., 1st Sess., especially pp. 15-17, shows very plainly that Congress in no way countenanced exploitation for exorbitant private profit of the necessities of the Government.

Authority given to make contracts does not imply authority to make unconscionable contracts. Suppose that Congress in authorizing the contracts in question had written into its legislation: "Provided, that no agency of government shall be authorized to enter into unconscionable contracts." Can it be that because Congress did not expressly provide that "unconscionable contracts" are unauthorized it impliedly sanctioned the making of "unconscionable contracts"? Or suppose the estimated costs in the contracts were so inflated by Bethlehem that its profits were 200% rather than 22%. Would this Court still be bound to enforce these contracts on the ground that Congress had commanded their enforcement? Surely Congress did not impliedly repeal historic legal principles and prohibit this Court from exercising its duty to withhold relief when the particular circumstances disclose an unconscionable arrangement in the making of which the Government's contracting officers had no practical choice.

The suggestion that President Wilson authorized a "traffic in profit" is refuted, if explicit proof be needed, by his utterances. For example, addressing a meeting of mine operators and manufacturers on July 12, 1917, he spoke as follows:

"I hear it insisted that more than a just price, more than a price that will sustain our industries, must be paid; that it is necessary to pay very liberal and unusual profits in order to "stimulate production"; that nothing but pecuniary rewards will do it—rewards paid in money, not in the mere liberation of the world.

"I take it for granted that those who argue thus do not stop to think what that means. Do they mean that you must be paid, must be bribed, to make your contribution, a contribution that costs you neither a drop of blood nor a tear, when the whole world is in travail and men everywhere depend upon and call to you to bring them out of bondage and make the world a fit place to live in again, amidst peace and justice?

"Do they mean that you will exact a price, drive a bargain, with the men who are enduring the agony of this war on the battlefield, in the trenches, amidst the lurking dangers of the sea, or with

the bereaved women and the pitiful children, before you will come forward to do your duty and give some part of your life, in easy, peaceful fashion, for the things we are fighting for, the things we have pledged our fortunes, our lives, our sacred honor to vindicate and defend—liberty and justice and fair dealing and the peace of nations! Of course you will not.

"It is inconceivable. Your patriotism is of the same self-denying stuff as the patriotism of the men dead or maimed on the fields of France, or else it is no patriotism at all.

"Let us never speak, then, of profits and of patriotism in the same sentence, but face facts and meet them.

"Let us do sound business, but not in the midst of a mist. Many a grievous burden of taxation will be laid on this Nation, in this generation and in the next, to pay for this war. Let us see to it that for every dollar that is taken from the people's pockets it shall be possible to obtain a dollar's worth of the sound stuffs they need." Public Papers of Woodrow Wilson, Vol. 3, pp. 75-6; 65 Cong. Rec. 4995.

Mr. Justice Holmes has said that "Men must turn square corners when they deal with the Government." *Rock Island &c. R. R. v. United States*, 254 U. S. 141, 143. His admonition has particular relevance when this Court is called upon to enforce agreements made with the Government at war for the production of supplies essential to the prosecution of the war. During wartime the bargaining position of Government contracting officers is inherently weak, no matter how conscientious they may be. If they are to deal on equal terms with private contractors, particularly where the subject matter of contracts is so intricate and so specialized as the building of ships, they must have available to them not only detailed information but also the time within which to study the data and the freedom to exercise a real choice. In the last war, at least, this was not generally true. See Sen. Rep. No. 944, 74th Cong., 1st Sess., pt. 4, p. 30. It is not difficult in these days to appreciate the position of negotiators for the Government in time of war and to realize how much the pressures of war deprive them of equality of bargaining power in situations where bargaining with private contractors is the only practicable means of securing necessary war supplies. Because the Government is in such a dependent position, and because those who deal with it on a cost-plus arrangement or some similar basis are assured of a profit, it is wholly consistent with practicalities and makes no unduly idealistic demand for the law to judge the arrangements of such wartime contractors by standards not unlike those by which a fi-

duciary's conduct is judged. Those upon whom the nation is dependent for its supplies in the defense of its life would hardly wish to be judged by lower standards.

The modes are vast and varied by which the nation obtains its war supplies. What will best supply war needs in amplest measure in the quickest time and least wastefully—whether by private letting and, if so, under what restrictions and safeguards; under what circumstances the Government should do its own supplying either by taking over old plants or building new ones or a combination of the two; to what extent and through what means peacetime habits and traditions may be displaced and disregarded—these are questions of policy for the wisdom and responsibility of the Congress and the Executive. The very limited scope of inquiry to which a litigation on a particular transaction is confined is hardly the basis for judgment on such far-flung issues. If the history of this Court permits one generalization above all others, it is the unwisdom of entering the domain of policy outside the very narrow legal limits presented by the record of a particular litigation. Such intrusion into the executive and legislative domains is not conducive to the just disposition of the immediate controversy. We are much less likely to go wrong if we do not depart from the well-grooved path of judicial competence.

This Court should not permit Bethlehem to recover these unconscionable profits, and thereby "make the court the instrument of this injustice." *Thomas v. Brownville, & Co. R. R. Co.*, 109 U. S. 522, 526.

Mr. Justice DOUGLAS.

On the point of duress and coercion I thoroughly agree with the views expressed by Mr. Justice BLACK and join in the opinion of the Court. For the reasons stated by Mr. Justice BLACK, the claim that Bethlehem's profits were unconscionable in the legal sense would likewise fail.

There is, however, one aspect of the case on which I take a somewhat different view.

The United States does not contest here the right of Bethlehem to retain its "fixed fee" of approximately \$12,000,000 for the construction of the ships. The dispute revolves around an additional sum of \$12,000,000 which Bethlehem claims under the so-called

"bonus-for-savings" provision of the contracts. That provision in the several contracts was the same except for the amount of the fixed fee. Thus a typical contract provided: "Should the actual cost be less than the estimated . . . cost . . . the Contractor shall be allowed as profit on each vessel in addition to said fixed sum for profit of . . . \$210,000 one-half the amount by which such actual cost of each vessel falls short of the estimated cost . . ."

I agree that the consummation of the bargain depended upon the inclusion of this "savings" clause and that in each instance there was but one contract, not several. My view, however, is that each contract was divisible or severable. ". . . the essential feature of such a contract is that a portion of the price is by the terms of the agreement set off against a portion of the performance and made payable for that portion, so that when an apportioned part of the performance has been rendered a debt for that part immediately arises." Williston on Contracts, § 861 (Rev. Ed.). In other words, the whole performance of each contract was divided "into two sets of partial performances, each part of each set being the agreed exchange for a corresponding part of the set of performances to be rendered by the other promisor". *Id.*, § 860A. (1) The promise of the Fleet Corporation to pay the actual cost plus the fixed fee was exchanged for Bethlehem's undertaking to construct the ships. (2) The promise of the Fleet Corporation to pay one-half the amount by which the actual cost fell short of the estimated cost was exchanged for Bethlehem's promise (which is implied) to effect the savings by increasing efficiency.

Although I am clear that the contracts would not have been made but for the inclusion of the "savings" provision, I do not believe that there is a "necessary dependency" between these two sets of promises within the rule of *Philadelphia, W. & B. R. Co. v. Howard*, 13 How. 307, 339. And see *Pollak v. Brush Electric Assoc.*, 128 U. S. 446, 455; *Fullmer v. Post*, 155 Pa. 275, 278; Restatement, Contracts, § 266(3). Precedents, to be sure, are of little aid since each case turns on its special circumstances. But the construction of divisibility seems warranted by the facts, though here as in other cases considerable reliance must be placed on implications.

Bethlehem's argument against divisibility rests on such testimony of Piez, who represented the Fleet Corporation, as follows:

"The price had to be placed for actual cost, if we knew the cost, plus an allowance for contingencies, plus an allowance for incentive, plus the fee. So we start out with the bare cost; then in order to meet any contingencies that may happen, add some allowance for contingencies; in order to give a proper incentive, add an incentive allowance; and then add the fee." That is to say the "savings" clause was deemed to be valuable from the Fleet Corporation's viewpoint as an "incentive" to keep the costs down and to expedite the work. And Powell, the author of the "savings" clause in this case and the representative of Bethlehem, testified that the savings to be obtained would be sufficient to "wipe out the excess profits taxes", so that the fixed fee would be "net" to Bethlehem.

But Powell's testimony also indicated that while the "savings" clause was an "incentive", Bethlehem was to earn the "savings":

"Q. Then I take it that one of your great problems, as the driving force of this organization, was to improve your labor conditions, or first to prevent labor conditions from getting worse and then to try to improve them?

"A. Yes.

"Q. Over what they were in December of 1917?

"A. Yes.

"Q. And if you were able to do that, then there was a possibility of some profit in these contracts under the half savings clause?

"A. Yes.

"Q. Was there any likelihood, or did you at that time foresee any likelihood, of any substantial saving in your material items?

"A. No, I should not have expected at that time to make any saving of any amount in the materials.

"Q. So that, if Bethlehem was to make any money out of these contracts in excess of the fixed fee, it was your judgment that the only way to do it was by increasing the efficiency of the yards?

"A. Exactly."

Powell also testified:

"The estimate was a figure which we had to shoot at that in my judgment gave us a reasonable profit or a chance of making a substantial saving. To make that saving, we had to operate more efficiently than what we might say was average efficiency under conditions that then existed. If we were going to make that saving, we had to overcome any increased cost due to decreased efficiency, and increase efficiency beyond what it was at that time."

And Piez testified that the provision was to give the ship-

builders an "incentive" to "use their ingenuity to make a larger profit."

The Special Master found that the estimates designated as "base prices" in the contracts "would afford Bethlehem a reasonable opportunity to effect 'savings' as a result of its efforts and ability to increase efficiency of management and labor as compared with average efficiency then existing." He also found that "it was understood that participation in 'savings' was supposed to represent a bonus or additional compensation to be earned by Bethlehem as consideration for its special efforts and ability to reduce cost by increasing efficiency of management and labor as compared with efficiency then existing." Yet he further found that "Bethlehem was to participate in savings however earned, but expected to produce savings by increased efficiency."

My difficulty is with that last finding. If Bethlehem was to share half of the savings "however earned", then its right to receive the bonus might well depend on a wholly fortuitous circumstance or it might accrue as petitioner suggests "simply as a reward for the inaccuracy of its estimate of actual costs." Under that view Bethlehem would be entitled to \$12,000,000 additional compensation merely because the wholesale price index fell. Yet that would be tantamount to a gift by public officers of property of the United States. The same result would follow if the clause be read as containing merely a "best efforts" provision. The contract already provided that Bethlehem "in all its acts hereunder, shall use its best efforts to protect and subserve the interest of the Owner." Even in the absence of such a provision, one would be implied. *United States v. A. Bentley & Sons Co.*, 293 Fed. 229, 235; *United States v. George A. Fuller Co.*, 296 Fed. 178, 180. Hence it is difficult for me to imply that this additional \$12,000,000 was offered as a reward for performing an obligation which the law would impose on the contractor in any event. *Burke & James, Inc. v. United States*, 63 C. Cls. 36, 57. That, too, would be a grant of public funds for which the United States would receive no *quid pro quo*.

Hence it seems more reasonable to imply that Bethlehem was to render an additional performance for the additional compensation of \$12,000,000. Such a construction of the contracts avoids the difficulties I have mentioned, as it gives the United States a *quid pro quo* for its promise to pay an additional \$12,000,000. Cf. *Dayton Airplane Co. v. United States*, 21 F. 2d 673, 682-683.

And it is supported by the testimony of the representatives of the two contracting parties who negotiated the contracts.

In that view of the matter Bethlehem would be put to its proof that it effected the savings which it now claims. Mere guesswork would not be enough. *J. J. Preis & Co. v. United States*, 58 C. Cls. 81, 86. Precise proof of each dollar saved might not be possible. But a reasonable approximation of Bethlehem's contribution to the savings would be necessary. Such burden of proof has been sustained in other cases involving similar contracts. *Cohen, Endel & Co. v. United States*, 60 C. Cls. 513; *F. Jacobson & Sons v. United States*, 61 C. Cls. 420. The Circuit Court of Appeals stated that there was "some evidence tending to show that savings resulted, in part at least, from increased efficiency." 113 F. 2d 301, 307. But there was no clear showing that special efforts were made to reduce costs and that the savings which resulted were traceable to such efforts. The necessary findings on that issue were not made.

February 23, 1942

George Buffington
Secretary Morgenthau

Please find out from the New York Times if you can get me a dozen copies of that insert in the Magazine Section on Donald Duck. Who was responsible for getting that in the New York Times? Write me a memo on it please.

TREASURY DEPARTMENT

100

INTER OFFICE COMMUNICATION

DATE February 23, 1942.

TO Secretary Morgenthau
FROM George Buffington *G.B.*

The publicity referred to in your memorandum of today on "The New Spirit" was arranged by Miss Antoinette Spitzer of the Walt Disney Productions in New York.

I heard much favorable comment regarding it yesterday on the train coming down from Boston.

I will have the twelve copies of the insert in the New York Times for you the first thing tomorrow morning.

TREASURY DEPARTMENT
INTER OFFICE COMMUNICATION

102

DATE February 23, 1942

TO Secretary Morgenthau
FROM George Buffington G.F.B.

Some time ago you told me, in connection with a discussion of "The New Spirit", you did not want to ask any favors of the Bank of America. I am told by Mr. John Hay Whitney that the Bank of America has indicated a willingness to guarantee up to 50% of the liability in our contemplated Disney project. While the suggestion to the Bank came from Whitney and not from the Treasury, our interest in the project contains implications with which you may not want to be identified.

Mr. Whitney's representative is in California and I understand expects an answer from the Bank tomorrow. If you consider it undesirable to permit the Bank to participate, I should like to advise Whitney.

Daily changes in the stock of Series E savings bonds on hand ^{1/}
(In thousands of pieces)

	: Number of : pieces sold: : this day :	: Number of pieces : manufactured : this day :	: Stock on hand : at close of : day :	: IBM : deliveries : this day :
Feb. 10	193	705	17,712	2,000
11	159	695	18,248	-
12	220	640	18,668	-
13	144	370	18,894	-
14	87	none-closed	18,807	-
15	none-closed	none-closed	18,807	-
16	363	535	18,979	2,500
17	89	800	19,690	1,000
18	218	800	20,272	1,000
19	160	800	20,912	1,000
20	193	800	21,519	1,000
21	200	none-closed	21,319	-

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

February 23, 1942

^{1/} Includes stock in hands of (1) Federal Reserve Banks and branches, (2) Post offices, (3) Federal Reserve Bank issuing agents, and (4) Treasury vaults in Washington.

UNITED STATES SAVINGS BONDS

Comparative Statement of Sales During
First Eighteen Business Days of February and January 1942 and December 1941
(February 1-21, January 1-21, December 1-20)
On Basis of Issue Price

(Amounts in thousands of dollars)

Item	Sales			Amount of Increase or Decrease (-)		Percentage of Increase or Decrease (-)	
	February 1942	January 1942	December 1941	February over January	January over December	February over January	January over December
	Series B - Post Offices	\$ 70,449	\$112,704	\$ 54,284	-\$ 42,295	\$ 58,420	- 37.9%
Series B - Banks	<u>257,910</u>	<u>327,031</u>	<u>106,487</u>	- <u>69,121</u>	<u>220,544</u>	- <u>21.1</u>	<u>207.1</u>
Series B - Total	328,359	439,735	160,770	- 111,376	278,965	- 25.3	173.5
Series F - Banks	41,214	48,178	16,298	- 6,964	31,880	- 14.5	195.6
Series G - Banks	<u>201,058</u>	<u>197,817</u>	<u>92,300</u>	<u>3,241</u>	<u>105,417</u>	<u>1.6</u>	<u>114.3</u>
Total	<u>\$570,631</u>	<u>\$685,730</u>	<u>\$259,368</u>	- <u>\$115,099</u>	<u>\$416,362</u>	- <u>16.5%</u>	<u>154.6%</u>

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

February 23, 1942.

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

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

UNITED STATES SAVINGS BONDS.

Daily Sales - February 1942

On Basis of Issue Price

(In thousands of dollars)

Date	Post Office Bond Sales Series E	Bank Bond Sales				All Bond Sales			
		Series E	Series F	Series G	Total	Series E	Series F	Series G	Total
February 1942									
2	\$ 8,435	\$ 34,150	\$ 6,191	\$ 19,795	\$ 60,136	\$ 42,585	\$ 6,191	\$ 19,795	\$ 68,571
3	3,572	7,887	2,793	19,518	30,199	11,459	2,793	19,518	33,770
4	4,893	16,537	3,937	18,515	38,989	21,430	3,937	18,515	43,882
5	4,257	16,149	2,367	14,640	33,156	20,406	2,367	14,640	37,413
6	4,310	23,510	3,829	18,620	45,958	27,820	3,829	18,620	50,269
7	3,023	10,039	2,019	6,174	18,233	13,062	2,019	6,174	21,256
9	5,486	25,354	3,071	16,265	44,690	30,839	3,071	16,265	50,176
10	3,902	11,794	1,109	12,679	25,581	15,695	1,109	12,679	29,483
11	3,279	9,782	1,487	7,637	18,906	13,061	1,487	7,637	22,185
12	3,293	14,670	1,584	7,781	24,035	17,963	1,584	7,781	27,328
13	2,710	9,026	1,047	4,385	14,458	11,736	1,047	4,385	17,168
14	1,714	5,740	113	1,152	7,005	7,454	113	1,152	8,719
16	5,741	22,405	3,212	13,748	39,365	28,147	3,212	13,748	45,107
17	2,639	4,285	690	3,211	8,187	6,924	690	3,211	10,825
18	2,992	13,911	1,715	14,118	29,745	16,903	1,715	14,118	32,737
19	3,147	9,167	1,401	9,401	19,969	12,313	1,401	9,401	23,115
20	3,231	11,769	1,455	6,138	19,362	14,999	1,455	6,138	22,592
21	3,827	11,733	3,193	7,282	22,808	15,561	3,193	7,282	26,035
Total	\$ 70,449	\$257,910	\$ 41,214	\$201,058	\$500,181	\$328,359	\$ 41,214	\$201,058	\$570,531

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

February 23, 1942.

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

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

TREASURY DEPARTMENT

106

INTER OFFICE COMMUNICATION

DATE February 23, 1942

TO Secretary Morgenthau

FROM W. N. Thompson

Major General Harley B. Ferguson, a retired Engineer Officer restored to active duty for assignment to the Treasury, reported here last week. In the mean time we have pretty well completed our protective measures against possible air raids or sabotage in Treasury buildings in Washington. Instructions also have gone to all of our field officers in charge of Treasury buildings and reports indicate that appropriate precautions have been taken. I think it would be well, however, to have an inspection made of some of our larger field office buildings and if you approve, I will send General Ferguson to visit the Mint Buildings in Philadelphia, Denver, and San Francisco. While on the Coast, he can also look over the Customs House and other buildings housing Treasury personnel.

General Ferguson has quite a distinguished record. A biographical sketch of the General is attached.

Attachment



BIOGRAPHY OF GENERAL HARLEY B. FERGUSON. Copied from Cullum's Register.

3748 (Born N.C.)

HARLEY B. FERGUSON

(Ap'd N.C.)7

Military history - Cadet at the U.S.M.A., from June 15, 1893 to June 11, 1897, when he was graduated and promoted in the army to (Add. Second Lieut., Corps of Engineers, June 11, 1897). Served: At Charleston, S.C., under Major Ruffner, from Oct. 1, 1897 to April 11, 1898. - At Engineer School, Willets Point, N.Y. from April 11, to 28, 1898 (Second Lieut., Corps of Engineers, July 5, 1898) - With Company E. Battalion of Engineers in Cuba during Santiago campaign, and at West Point, N.Y., from Sept. 4, to Dec. 11, 1898. - At Engineer School, Willets Point, N.Y., from Dec. 11, 1898 to July 5, 1899. - En route to and in Philippines to June 26, 1900: (First Lieut., Corps of Engineers, Jan. 29, 1900): Enroute to and in China, to May 27, 1901; at Peitsang Yangtsun and Peking, Chief Engineer officer, China Relief Expedition; in Philippine Islands and en route to the U.S., to Dec. 1, 1901; in Information Bureau, Adjutant General's Office, Washington to Aug. 1903; at U.S. Military Academy, Instructor in Engineering, Aug. 23, 1903 to Aug. 31, 1904 (Captain Corps of Engineers, April 25, 1904) - At Fort Leavenworth, Kas., Student. Staff College to July, 1905; Instructor in Engineering Department, Infantry and Cavalry School, to July, 1907; at Montgomery, Ala., as Assistant to Oct. 9, 1907; in charge of Engineer District, from Oct. 9, 1907 to September 1910; at Havana, Cuba, supervising the work of raising the Battleship Maine, September, 1910 to (Major, Corps of Engineers, Feb. 27, 1911) August, 1912; at Army War College, Washington, D.C., August 1912; to July 1913; at Milwaukee, Wis., in charge of Engineer District, July 1913, to March 1917; at New London, Conn., March to (Lieut. Colonel, Corps of Engineers, May 15, 1917) June, 1917; at Boston, Mass., Department Engineer, June to (Colonel, of Engineers, National Army, Aug. 5, 1917) August, 1917; at Camp Sevier, Greenville, S.C., en route to and in France, and commanding 105th Engineers, 30th Division, American

Expeditionary Forces, to June 1918; Corps Engineers, 2d Corps, June 16 to (Brig. General, U.S.A., Aug. 8, 1918) October 3, 1918; at Newport News, Va., Commanding part of Embarkation, Nov. 10, 1918 to May 1919; (Returned to Grade of Lieut. Colonel June 15, 1919)(Colonel, Corps of Engineers July 1, 1920). At Pittsburgh Pa., District Engineer, Pittsburgh River and Harbor District, July 1919 to July 1920; at Washington, D. C., student officer, Army War College, Aug. 1920 to June 1921, when he was graduated; Office, Assistant Secretary of War, in charge of supervising plans for industrial mobilization, April, 1921 to Jan., 1927; Director of Army Industrial College, Feb. 25, 1925 to Jan. 1927; at Washington, D.C; Division Engineer, Gulf Division, Jan., 1927, to May, 1927; at Cincinnati, Ohio, Division Engineer Central Division, May, 1927, to Oct., 1929; at Norfolk, Va., Division Engineer South Atlantic Division, Oct., 1929 to June 1932; Division Engineer, Lower Mississippi Valley Division June 1932 to ~~date~~ ^{June 15, 1932}. Appointed President, Mississippi River Commission, June 15, 1932. Served as President of the Mississippi River Commission until August 31, 1939 when he retired for age.

Distinguished Service Medal

"For exceptionally meritorious and distinguished services. As chief Engineer of the 2d Army Corps and later of the 2d Army, he demonstrated high professional attainments and marked initiative. Through his foresight and skill in directing important technical operations he was a notable factor in the successes of the combat troops, rendering invaluable services to the American Expeditionary Forces."

NOTE:

General Ferguson received the rank, pay, and allowances of a retired Major General under the authority of Public Law 228, August 18, 1941.

MEMBERSHIP ON BOARDS.

Lake Michigan Water Commission, 1914.

Board of Officers to Review Fire Control Installations
Coast Defenses of Long Island, 1917.

Federal Purchasing Board, 1921.

Board of Bridges across Mississippi River at New Orleans, 1928.

Board on Bridges over Hudson River between New York and
New Jersey, 1930.

St. Lawrence Waterway Board, 1930.

Board of Engineers for Rivers and Harbors, 1930-1932.

Board on Waterway from Cumberland Sound, Ga. and Fla.,
to Mississippi River, 1931 (Cross Florida Canal).

Muscle Shoals Commission to Represent Federal Government, 1931.

Board on Review of Flood Control on Mississippi River, 1931.

TREASURY DEPARTMENT

110

INTER OFFICE COMMUNICATION

DATE February 23, 1942

TO Secretary Morgenthau
FROM W. N. Thompson

Under the agreement for the removal of his force from the Procurement Division Building, Commissioner Reynolds was to vacate on or about March 5th. Last week Mr. Reynolds indicated that this move would have to be postponed until April or May, as his present plan was to move into the Farm Credit Administration Building, at Thirteenth and E Streets, when that Administration moves to Kansas City. I told Mr. Reynolds that any such delay would seriously endanger the Lend-Lease operations of Procurement and he finally agreed that he would adhere to the original plan. He is therefore going to move into the Longfellow Building on Connecticut Avenue on or about March 14th. That is later than originally estimated but the REA will not be vacating the Longfellow Building before then.

Mr. Reynolds' decision to move to the Longfellow Building may enable the Treasury to obtain the Farm Credit Building in April or May. Mr. Reynolds has promised to give us every consideration for that space and if we do get it, it will materially aid us in other pressing space demands, particularly Public Debt and Foreign Funds.



TREASURY DEPARTMENT

INTER-OFFICE COMMUNICATION

CONFIDENTIAL

DATE February 23, 1942

TO Secretary Morgenthau
FROM Mr. Haas
Subject: The Business Situation,
Week ending February 21, 1942.

Summary

(1) The conversion of industry to war-time production is being accompanied by a temporary levelling-out in the trend of industrial output after allowance for seasonal factors. Both the New York Times and Barron's weekly indexes of business activity have been declining in February, after advancing to record high levels in the latter part of last month.

(2) Recent developments, such as tanker sinkings, and further deterioration of the Far Eastern supply situation, foreshadow severe pressure on the country's transportation and shipping facilities. In the face of augmented war needs, and a prospective seasonal expansion in freight car requirements between now and October, the number of surplus freight cars in early February totaled only 60,000, as compared with 103,000 a year earlier.

(3) The general price level continues to move higher. As a result of a gain of 0.5 percent in the week ended February 14, the BLS all-commodity index advanced to 96.2. This is the highest level since August 1929, and is 28.3 percent above that in the pre-war month of August 1939.

(4) The amount of goods sold in department stores during the first half of February, in actual volume, showed little gain over year-earlier levels. Although the value of goods sold in the first and second weeks of the month ran 20 and 19 percent respectively above the corresponding weeks of 1941, average prices at the beginning of the month were 17 percent higher than a year earlier.

(5) Consumption of Great Lakes iron ore last month reached the highest levels on record. Although current ore stocks are said to be adequate until the opening of the shipping season, a WPB official recently indicated that a diversion of Great Lakes grain shipments to the railroads appears inevitable, as part of a program to obtain additional shipping space for iron ore.

The general business situation

Associated with the current conversion of industry to an all-out war program is a levelling-out in the trend of total industrial output (after allowance for seasonal factors), accompanied by some temporary unemployment. Basic commodity prices have also tended to level out, although previous increases in prices of basic commodities are continuing to force prices of manufactured goods and retail prices toward higher levels. Consumer buying in retail stores has declined from the high levels of early January.

These influences, it must be emphasized, are no more than temporary. Income payments continue to increase rapidly, while the supply of consumer goods is becoming more and more restricted. Ample stocks of most goods in retail stores, built up in the second half of last year, have tended to restrain price advances, but as these become depleted and replacements must be made it will be increasingly difficult to keep wholesale and retail prices under control.

The Federal Reserve adjusted index of industrial production, at 170 (preliminary) in January, seems likely to flatten out for a time, registering only minor changes during the first half of this year while conversion to full war production is getting under way. Seasonal allowances will also tend to hold down the adjusted index between January and early summer. During the second half of the year, however, a marked advance is in prospect, accompanied by a heavy demand for raw materials and skilled labor, which will require a further diversion from the production of civilian goods. Since the important war material components of the Federal Reserve index -- notably machinery, aircraft, shipbuilding, chemicals, and output of the automobile industry -- are measured in terms of man-hours, and since labor requirements are particularly heavy in the production of war equipment, the Federal Reserve index would doubtless advance even if there were no increase in the total tonnage of goods produced for both war and civilian uses. Wage payments to individuals may be expected to increase accordingly, but at an even more rapid rate due to rising wage scales and increased overtime payments.

Weekly business indexes lower

Weekly business indexes recently have receded from the highs reached near the end of January. The rate of decline in the week ended February 14, however, was noticeably slower than that of the previous week. Barron's index of business activity in the second week of the current month declined 0.7 point, while the New York Times index declined 1.7 points to

134.9. The principal factor in the decline in the Times index, as in the previous week, was a contra-seasonal decrease in freight carloadings. However, most of the other adjusted components of the index also showed declines.

Serious transportation problems looming

Although freight carloadings have declined since the third week in January, recent developments foreshadow severe pressure on the country's transportation and shipping facilities. Tanker sinkings, disrupted coastal shipping, tire rationing and probable gasoline rationing, all will tend to further swell the traffic burdens of railroads already taxed with a heavy volume of freight and passenger traffic, resulting from the war effort.

Although last year's fall peak in freight carloadings failed to come up to earlier expectations, this appears to have been due in no small measure to increased efficiency in carloading and utilization, rather than to an over-estimate of the freight volume. Thus, freight carried last October soared 32 percent above year-earlier levels when measured in ton-miles, although the corresponding gain in cars loaded was only 15 percent. Due to this increased efficiency, together with a moderate increase in new cars owned and a decrease in cars waiting repair, the railroads managed to handle last fall's peak traffic without a shortage, but surplus cars were reduced to the uncomfortably low figure of only 41,000. (See Chart 1.)

Need for favorable priorities for railroad materials

Due to seasonal factors, surplus cars by the early part of February had risen to 60,000, but this figure was still 43,000 below year-earlier levels. Furthermore, on the basis of normal seasonal expectations alone freight traffic should rise around 21 percent by October, hence the current car surplus is very low in view of probable traffic requirements.

New freight cars put into service last month were 25 percent greater than in January 1941, and 68,000 new freight cars were on order at the beginning of February, as compared with 42,000 a year earlier. However, despite some apparent improvement in the priorities status of materials for railroad equipment, complaints continue to be heard.

Commodity prices unchanged at high level

The BLS index of prices of 28 basic commodities remained stable last week, continuing the sidewise movement of early February. (See Chart 2.) Hope of passage of farm bloc

legislation was offset by fear of a Presidential veto. On February 17 the Department of Agriculture announced that it would guarantee parity income to growers of 1941 wheat, corn, cotton, and tobacco, by payments in amounts sufficient to make up the difference between the prices received from these crops and parity. This was interpreted in the press as an effort to prevent passage of legislation pending in Congress to prohibit the sales of Government owned commodities at less than parity.

Among the individual commodities in the foodstuffs group, prices for hogs, wheat, corn, cottonseed oil, and cocoa advanced moderately. Prices for steers, barley, and butter declined. Among the industrial raw materials, flaxseed prices continued to rise, and print cloth prices were moderately higher. Rosin and wool prices declined.

In the cotton market, the threat of hedges against sales of Commodity Credit cotton tended to restrict futures buying. Warning said to have been given meat packers by the Surplus Marketing Administration that it would not pay more than prices prevailing on January 29 for pork and lard probably kept hog prices from reaching even higher levels.

All-commodity price index resumes rise

The BLS all-commodity index advanced 0.5 percent in the week ended February 14 to the highest point since August 1929. At 96.2, the index was 28.3 percent higher than the pre-war level of August 1939, and 4.3 percent higher than in the week ended December 6. (See Chart 3.)

The general wholesale price level is still substantially below that of the first World War, however, as will be noted in Chart 3, but food prices at wholesale continue to follow closely the trend in that period.

Shipping stringency affecting agricultural imports

Stocks of some imported foods and other agricultural imports are declining noticeably as a result of Far Eastern developments and the general shortage of shipping space. Since more roundabout routes and uneconomical methods of shipping doubtless are being substituted, pressure on prices to cover such costs may be expected in addition to the influence of inadequate supplies.

Sales of tea are far in excess of imports and on one day last week wholesale prices advanced as much as 4 to 6 cents a pound, to a price reported as above the ceiling.

Brazilian coffee supplies in this country are fairly ample at present, but stocks of fine Colombian coffee are reported as being low. Since January 1, less than one-fourth of the quantity of cocoa received in the corresponding period last year has been received.

The importance of open shipping lanes in the case of wool is indicated by mill consumption in 1941, which consisted of 57 percent of wool of foreign origin. This compares with 32 percent in 1940, and an average of 19 percent in 1935-39. Although our wool stocks are believed to be the highest in 20 years, the 1942 supply must be supplemented by imports.

Diversion of ships is accentuating the tightness of sugar supplies, and reports are current that the rationing may be as low as 8 ounces a week. In the first five and a half weeks of 1942 less than one-quarter of the quantities received in the corresponding period last year have arrived. Inasmuch as the shortage of raw sugar has reduced refining operations, the resulting increase in overhead costs may force further price advances.

Lend-lease purchases of farm products in 1941

Deliveries of agricultural commodities to the British Government for lend-lease shipment up to January 1 reached a total of 3,311,000,000 pounds, at a cost of \$367,000,000. December deliveries alone amounted to more than 650,000,000 pounds, costing over \$67,000,000. About two-thirds of the physical volume of deliveries consisted of the following items:

<u>Commodity</u>	<u>Pounds</u>
Corn	685,000,000 (12,200,000 bushels)
Milk, evaporated and skimmed	472,900,000
Meat products	312,100,000
Beans	255,800,000
Lard	243,100,000
Cotton	233,000,000 (487,500 bales)

The approximate value of individual groups of products was as follows:

<u>Commodity groups</u>	<u>Value</u>
Dairy products and eggs	\$114,000,000
Meat, fish and fowl	90,000,000
Fruits, vegetables, nuts	39,000,000
Lard, and other fats, and oils	26,000,000
Grain and cereal products	18,000,000
Other foodstuffs, including concentrates and vitamins	2,200,000
	<u>\$289,200,000</u>
Non-foodstuffs, such as cotton, tobacco, vegetable seeds, and naval stores	77,000,000
Total	<u>\$367,000,000</u>

Stock prices decline in New York and London

The accumulation of adverse war news climaxed by the fall of Singapore was followed by a further gradual sag in industrial stock prices in the New York market last week. Although the decline for the week was only around 2 percent, this was sufficient to carry the Dow-Jones industrial average down to the lowest level since 1938. The volume of trading, however, was very light and ran below 400,000 shares a day throughout the week. In addition to unfavorable war news, the market also was confronted with reductions in quarterly dividend rates by the Chrysler Corporation and du Pont. The former cut the quarterly dividend rate to \$1.00 from \$1.50, while the latter company reduced the dividend rate to \$1.25 from \$1.75.

Reference to Chart 4 will disclose that industrial stock prices in London also declined last week, and on the whole showed a slightly weaker tendency than in New York. Industrial stock prices in London have now declined about 9 percent since the outbreak of war in the Pacific, about the same as the decline at New York.

Department store sales gain moderating

The recent upsurge in department store sales has moderated to the extent that, on a unit volume basis, sales in the first half of the current month were little above the corresponding period of 1941. During the week ended February 14, sales ran 19 percent above year-earlier levels, while in the previous week the gain was 20 percent. (See Chart 5.) Since retail prices of typical department store

items at the beginning of the month were about 17 percent above year-earlier levels, it follows that the year-to-year sales gain was very largely accounted for by the rise in prices. In other words, the expanded consumer demand has been reflected almost entirely in a bidding up of prices rather than an increased volume of purchases.

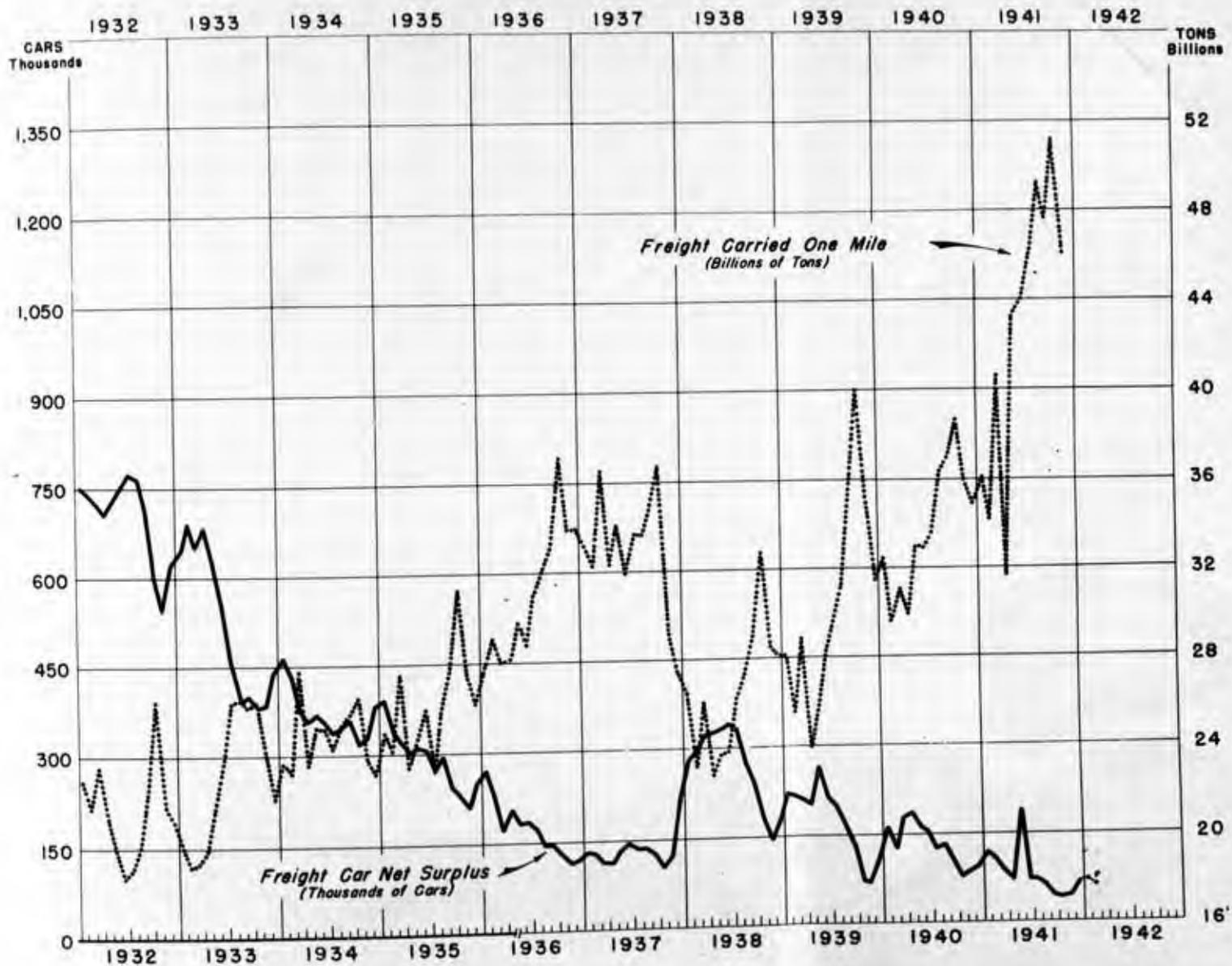
Iron ore consumption at record high

Consumption of Great Lakes iron ore last month reached the highest level on record, with an increase of nearly 100,000 tons over the previous record set in December. At the January rate, iron ore consumption for the full year would total nearly 86,000,000 gross tons, or more than 4,000,000 tons above the amount carried by lake vessels during last year's record-breaking shipping season.

On February 1, iron ore on hand at furnaces and Lake Erie docks totaled nearly 34,000,000 tons, and the Lake Superior Iron Ore Association regards this supply as adequate until the opening of the new shipping season. Nevertheless, a WPB official recently characterized the need for shipping facilities for iron ore on the Great Lakes as a paramount problem. Moreover, he indicated that in order to save shipping space, diversion of Great Lakes grain shipments to the railroads appeared inevitable.

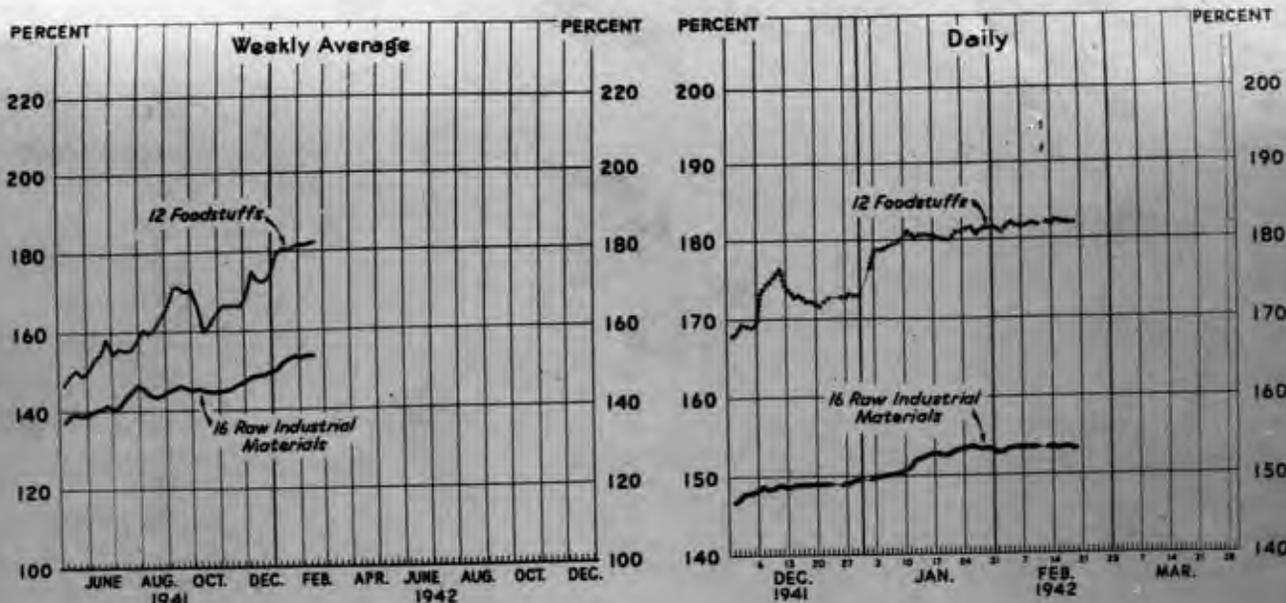
FREIGHT CAR NET SURPLUS COMPARED WITH FREIGHT TRAFFIC

Monthly



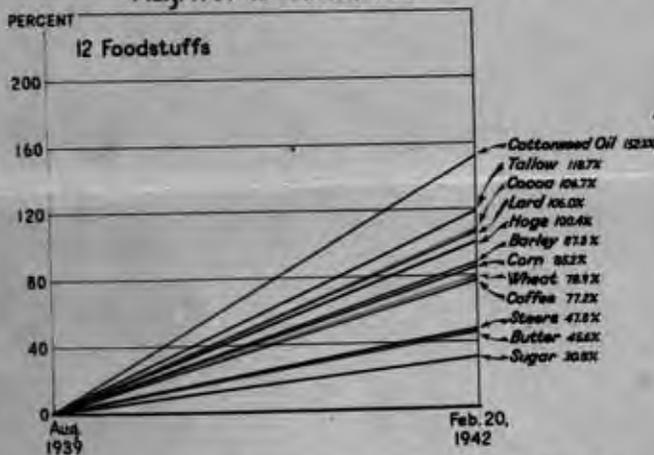
MOVEMENT OF BASIC COMMODITY PRICES

AUGUST 1939 = 100

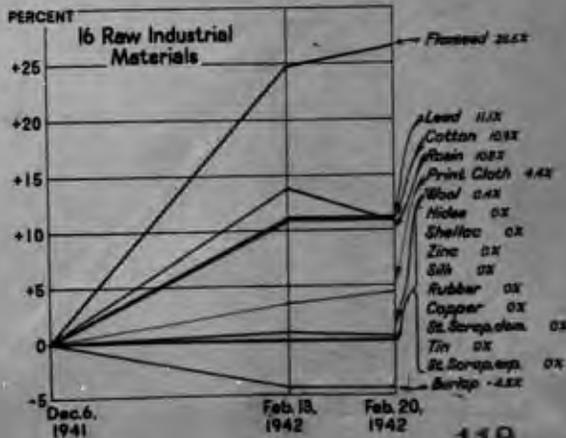
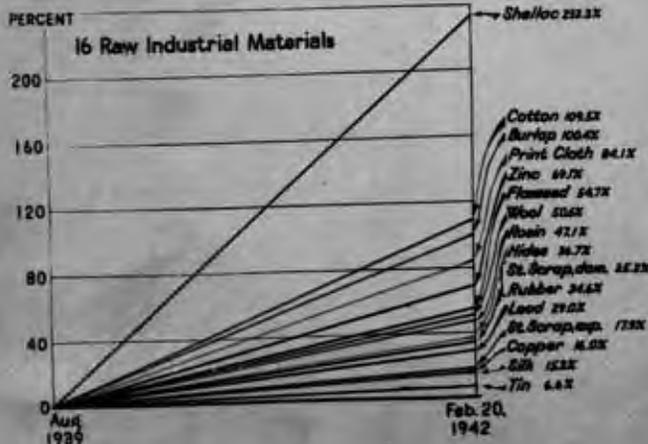
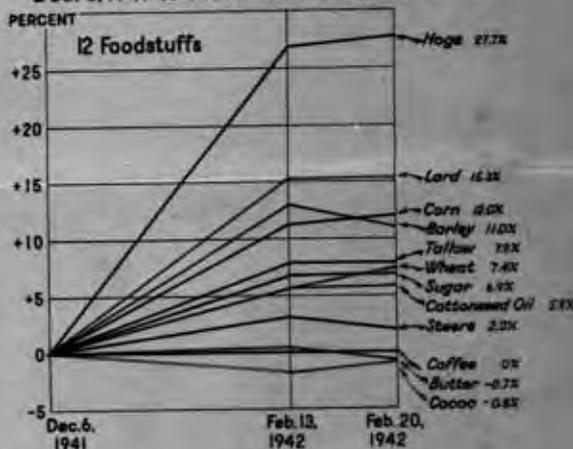


PERCENTAGE CHANGE FOR INDIVIDUAL COMMODITIES

Aug. 1939 to Feb. 20, 1942

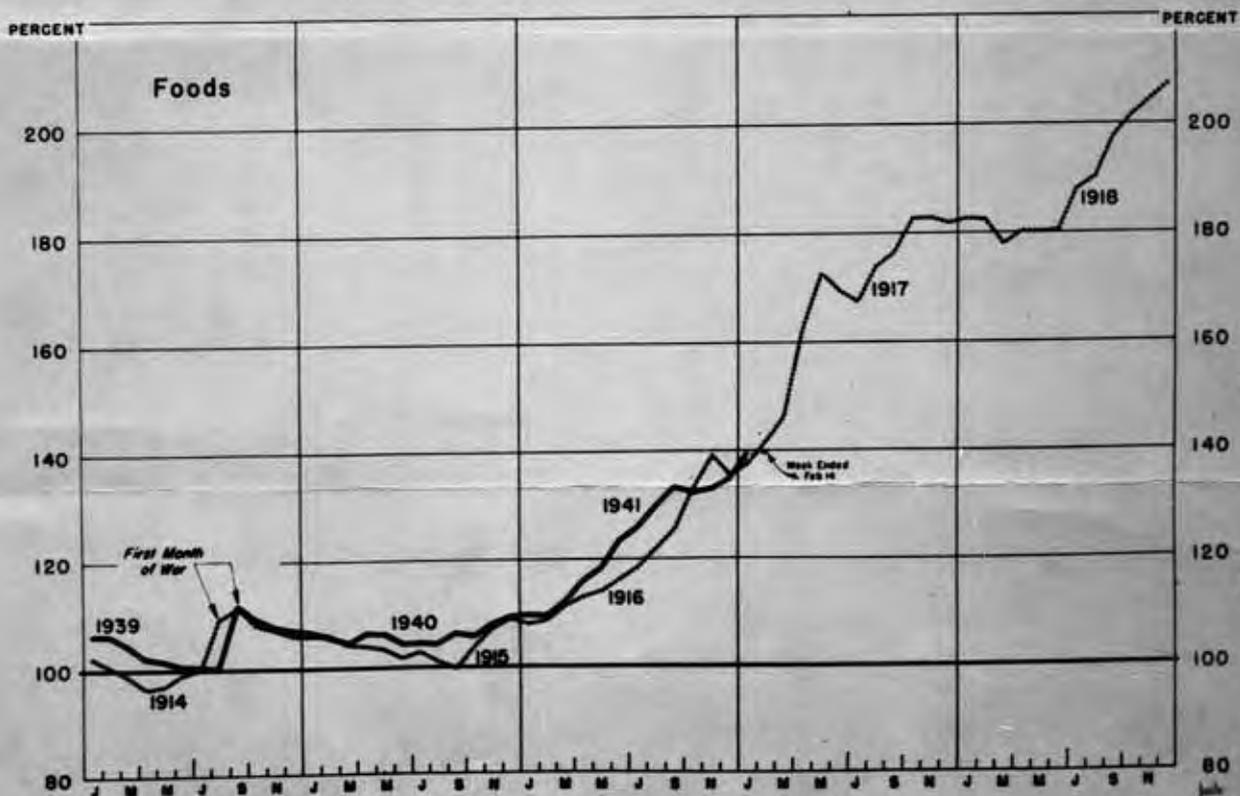
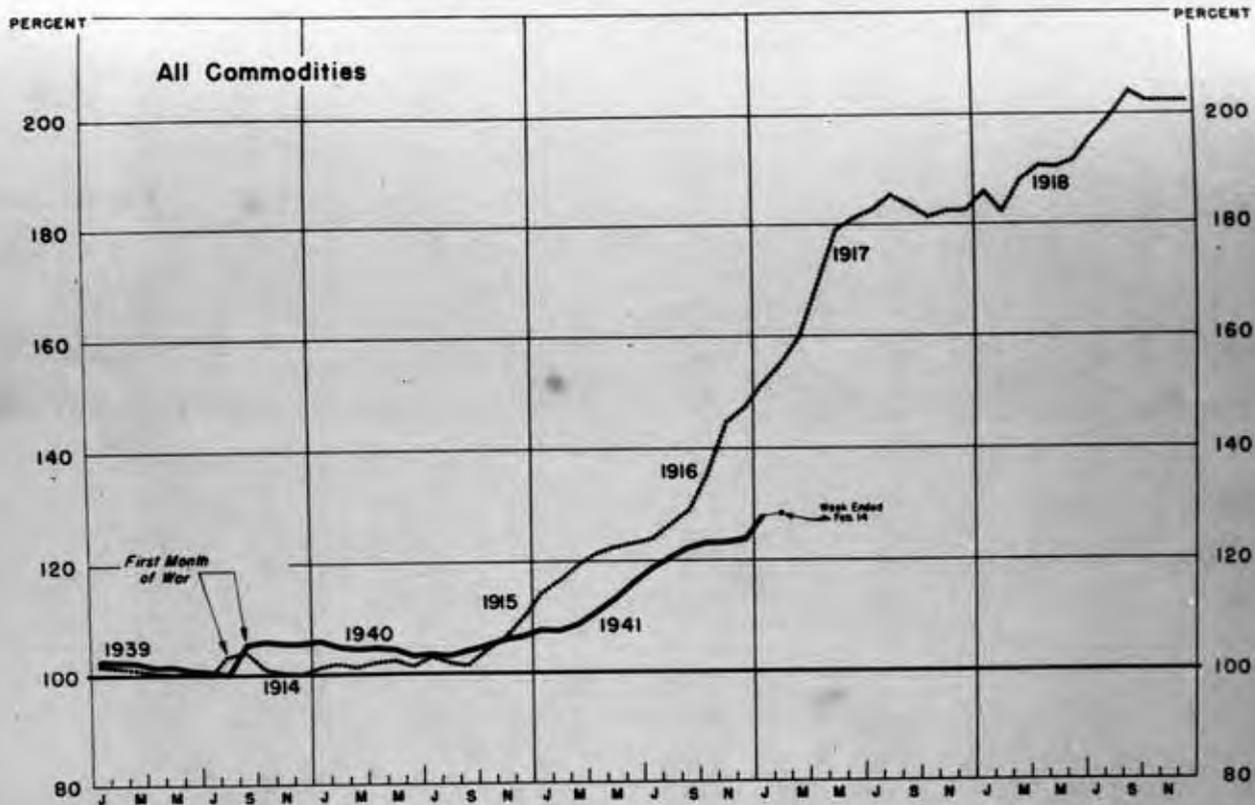


Dec. 6, 1941 to Feb. 13 and Feb. 20, 1942



PRICES, 1939 TO DATE COMPARED WITH 1914 TO 1918

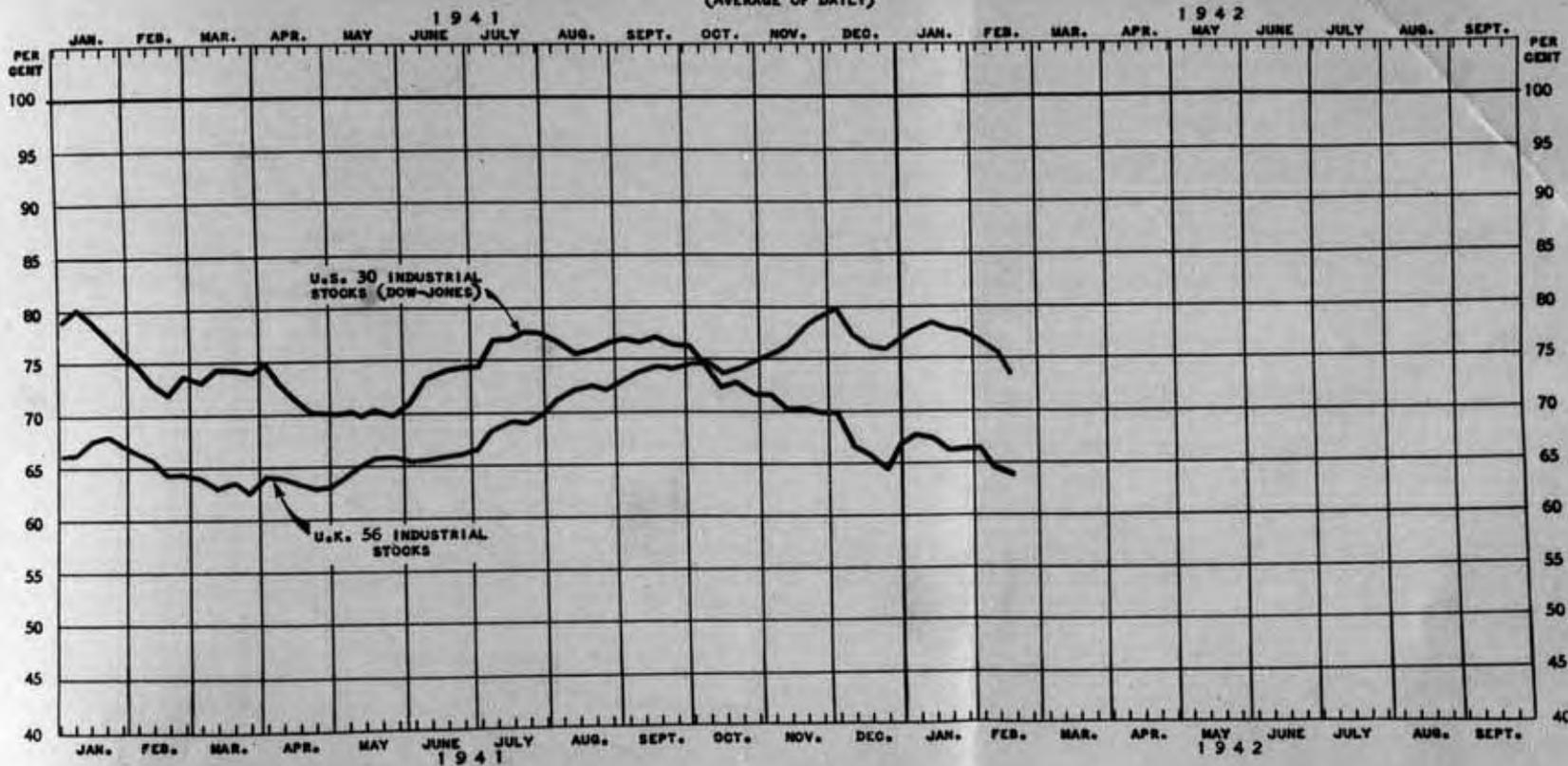
July 1914 = 100 World War Period; Aug. 1939 = 100 Present Period



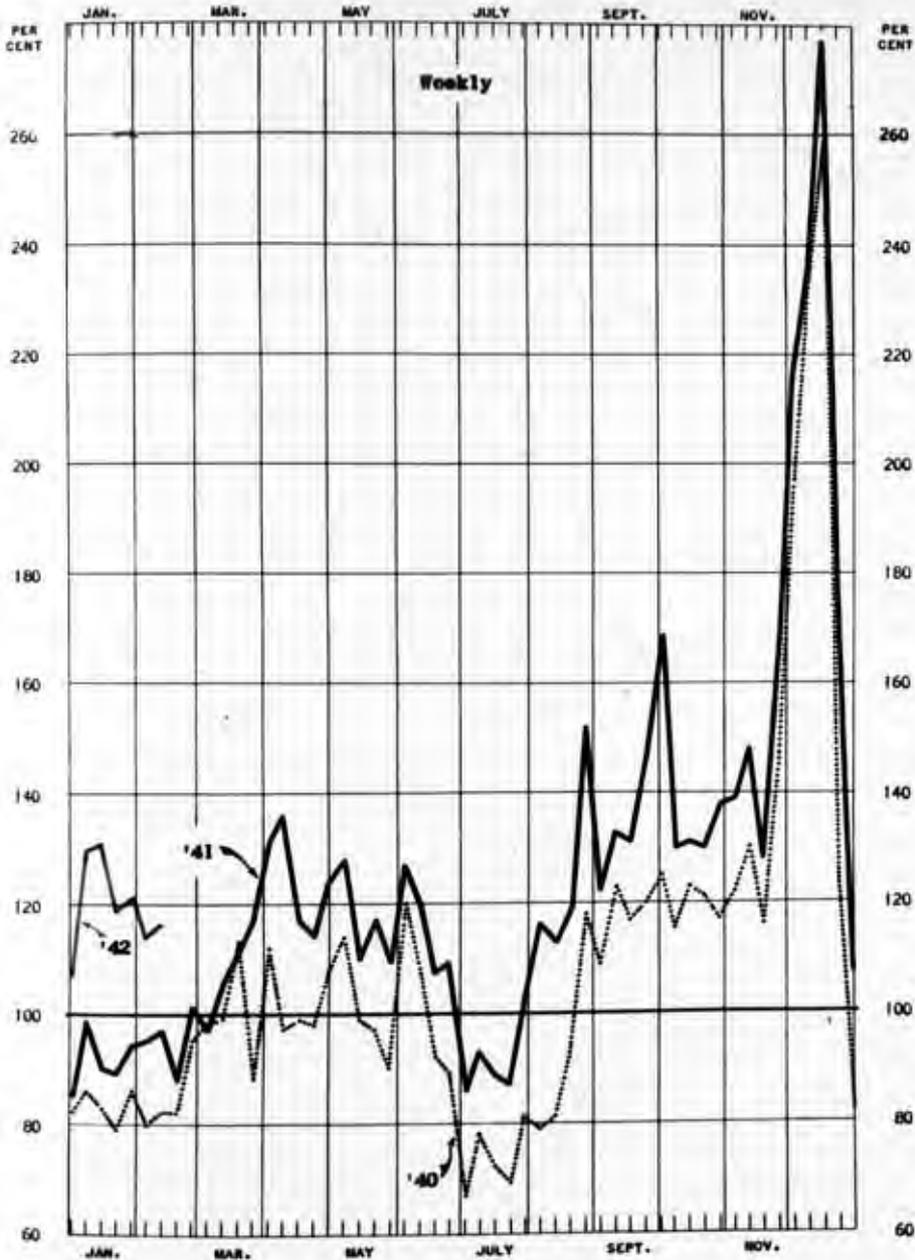
Source: B.L.S.

INDUSTRIAL STOCK PRICES IN U.S. AND U.K. AUGUST 1936 - 100

Weekly
(AVERAGE OF DAILY)



DEPARTMENT STORE SALES
1935 - '39 = 100, UNADJUSTED



Treasury Department
Division of Monetary Research **123**

Date.....19

To: Miss Chauncey

This is the best I could
do on a copy of the Lend-Lease Agreements,
which I understand was signed by
Sumner Welles and Lord Halifax on
Feb. 23rd.

L. Shanahan

MR. WHITE
Branch 2058 - Room 214

2/27/42
124

Agreement Between the Governments of the United States of America and of the United Kingdom on the Principles Applying to Mutual Aid in the Prosecution of the War Against Aggression, Authorized and Provided for by the Act of March 11, 1941.

Whereas the Governments of the United States of America and the United Kingdom of Great Britain and Northern Ireland declare that they are engaged in a co-operative undertaking, together with every other nation or people of like mind, to the end of laying the bases of a just and enduring world peace securing order under law to themselves and all nations;

And whereas the President of the United States of America has determined, pursuant to the Act of Congress of March 11, 1941, that the defense of the United Kingdom against aggression is vital to the defense of the United States of America;

And whereas the United States of America has extended and is continuing to extend to the United Kingdom aid in resisting aggression;

And whereas it is expedient that the final determination of the terms and conditions upon which the Government of the United Kingdom receives such aid and of the benefits to be received by the United States of America in return therefor should be deferred until the extent of the defense aid is known and until the progress of events makes clearer the final terms and conditions and benefits which will be in the mutual interests of the United States of America and the United Kingdom and will promote the establishment and maintenance of world peace;

And whereas the Governments of the United States of America and the United Kingdom are mutually desirous of concluding now a preliminary agreement in regard to the provision of defense aid and in regard to certain considerations which shall be taken into account in determining such terms and conditions and the making of such an agreement has been in all respects duly authorized, and all acts, conditions and formalities which it may have been necessary to perform, fulfil or execute prior to the making of such an agreement in conformity with the laws either of the United States of America or of the United Kingdom have been performed, fulfilled or executed as required;

The undersigned, being duly authorized by their respective Governments for that purpose, have agreed as follows:

ARTICLE I

The Government of the United States of America will continue to supply the Government of the United Kingdom with such defense articles, defense services, and defense information as the President shall authorize to be transferred or provided.

- 2 -

ARTICLE II

The Government of the United Kingdom will continue to contribute to the defense of the United States of America and the strengthening thereof and will provide such articles, services, facilities or information as it may be in a position to supply.

ARTICLE III

The Government of the United Kingdom will not without the consent of the President of the United States of America transfer title to, or possession of, any defense article or defense information transferred to it under the Act or permit the use thereof by anyone not an officer, employee, or agent of the Government of the United Kingdom.

ARTICLE IV

If, as a result of the transfer to the Government of the United Kingdom of any defense article or defense information, it becomes necessary for that Government to take any action or make any payment in order fully to protect any of the rights of a citizen of the United States of America who has patent rights in and to any such defense article or information, the Government of the United Kingdom will take such action or make such payment when requested to do so by the President of the United States of America.

ARTICLE V

The Government of the United Kingdom will return to the United States of America at the end of the present emergency, as determined by the President, such defense articles transferred under this Agreement as shall not have been destroyed, lost or consumed and as shall be determined by the President to be useful in the defense of the United States of America or of the Western Hemisphere or to be otherwise of use to the United States of America.

ARTICLE VI

In the final determination of the benefits to be provided to the United States of America by the Government of the United Kingdom full cognizance shall be taken of all property, services, information, facilities, or other benefits or considerations provided by the Government of the United Kingdom subsequent to March 11, 1941, and accepted or acknowledged by the President on behalf of the United States of America.

ARTICLE VII

In the final determination of the benefits to be provided to the United States of America by the Government of the United Kingdom in return for aid furnished under the Act of Congress of March 11, 1941, the terms and conditions thereof shall be such as not to burden commerce between the two countries, but to promote mutually advantageous economic relations between them and the betterment of world-wide economic relations. To that end, they shall include provision for agreed action by the United States of America and the United Kingdom, open to participation

- 3 -

by all other countries of like mind, directed to the expansion, by appropriate international and domestic measures, of production, employment, and the exchange and consumption of goods, which are the material foundations of the liberty and welfare of all peoples; to the elimination of all forms of discriminatory treatment in international commerce, and to the reduction of tariffs and other trade barriers; and, in general, to the attainment of all the economic objectives set forth in the Joint Declaration made on August 12, 1941, by the President of the United States of America and the Prime Minister of the United Kingdom.

At an early convenient date, conversations shall be begun between the two Governments with a view to determining, in the light of governing economic conditions, the best means of attaining the above-stated objectives by their own agreed action and of seeking the agreed action of other like-minded Governments.

ARTICLE VIII

This Agreement shall take effect as from this day's date. It shall continue in force until a date to be agreed upon by the two Governments.

Signed and sealed at Washington in duplicate this 23rd day of February, 1942.

HOLD FOR RELEASE

HOLD FOR RELEASE

HOLD FOR RELEASE

FEBRUARY 26, 1942

2185

NOTE: The following statement is for release to editions of all newspapers appearing on the streets NOT EARLIER THAN 8:00 A.M., E.W.T., Tuesday, February 24, 1942. The same release also applies to radio announcers and news commentators.

CARE MUST BE EXERCISED TO PREVENT PREMATURE PUBLICATION.

STEPHEN EARLY
Secretary to the President

An agreement between the Governments of the United States and Great Britain on the principles applying to mutual aid in the prosecution of the war was signed yesterday (Monday) by the Acting Secretary of State and the British ambassador.

The agreement is made under the provisions of the Lend-Lease Act of March 11, 1941. By this Act of the Congress and the great appropriations by which it has been supported this nation is able to provide arms, equipment, and supplies to any country whose defense is vital to our own defense.

On December 7, 1941, we were attacked. We are now one of the twenty-six United Nations devoting all of their united strength to the winning of this war and to the establishment of a just and lasting peace. The vast resources which Providence has given us enable us to insure that our comrades in arms shall not lack arms. Congress has granted the authority and the means. United and equipped by the overwhelming productive power of their resources and ours, we shall fight together to the final victory.

Recent developments in the war have shown, if proof was required, the wisdom and necessity of the policy of lend-lease supplies to the United Nations. That policy continues, and is expanding to meet the expanding needs of the fighting fronts. The agreement signed yesterday reaffirms our purpose to supply aid to Great Britain. The British Government will supply this country with such reciprocal aid as it is in a position to give.

As to the terms of settlement between the two countries, the agreement states that it is too early in this struggle to foresee or define the precise and detailed terms. Instead the agreement lays down certain of the principles which are to prevail. These principles are broadly conceived, for the scale of aid is so vast that narrow conceptions of the terms of settlement would be as disastrous to our economy and to the welfare of our people as to the welfare of the British people. Articles which at the end of the war can be returned to us, and which we wish to have back, will be returned. Full account will be taken of all reciprocal aid.

The fundamental framework of the final settlement which shall be sought on the economic side is given in Article VII. It shall be a settlement by agreement open to participation by all other nations of like mind. Its purpose shall be not to burden but to improve worldwide economic relations. Its aim will be to provide appropriate national and international measures to expand

production, employment, and the exchange and consumption of goods, which, the agreement states, are the material foundations of the liberty and welfare of all peoples, to eliminate all forms of discriminatory treatment in international commerce, to reduce tariffs and other trade barriers, and, generally, to attain the economic objectives of the Atlantic Charter.

To that end Article VII provides for the early commencement of conversations, within the framework which it outlines, with a view to establishing now the foundations upon which we may create after the war a system of enlarged production, exchange, and consumption of goods for the satisfaction of human needs in our country, in the British Commonwealth, and in all other countries which are willing to join in this great effort.

Agreement Between the Governments of the United States of America and of the United Kingdom on the Principles Applying to Mutual Aid in the Prosecution of the War Against Aggression, Authorized and Provided for by the Act of March 11, 1941.

Whereas the Governments of the United States of America and the United Kingdom of Great Britain and Northern Ireland declare that they are engaged in a co-operative undertaking, together with every other nation or people of like mind, to the end of laying the bases of a just and enduring world peace securing order under law to themselves and all nations;

And whereas the President of the United States of America has determined, pursuant to the Act of Congress of March 11, 1941, that the defense of the United Kingdom against aggression is vital to the defense of the United States of America;

And whereas the United States of America has extended and is continuing to extend to the United Kingdom aid in resisting aggression;

And whereas it is expedient that the final determination of the terms and conditions upon which the Government of the United Kingdom receives such aid and of the benefits to be received by the United States of America in return therefor should be deferred until the extent of the defense aid is known and until the progress of events makes clearer the final terms and conditions and benefits which will be in the mutual interests of the United States of America and the United Kingdom and will promote the establishment and maintenance of world peace;

And whereas the Governments of the United States of America and the United Kingdom are mutually desirous of concluding now a preliminary agreement in regard to the provision of defense aid and in regard to certain considerations which shall be taken into account in determining such terms and conditions and the making of such an agreement has been in all respects duly authorized, and all acts, conditions and formalities which it may have been necessary to perform, fulfill or execute prior to the making of such an agreement in conformity with the laws either of the United States of America or of the United Kingdom have been performed, fulfilled or executed as required;

The undersigned, being duly authorized by their respective Governments for that purpose, have agreed as follows:

ARTICLE I

The Government of the United States of America will continue to supply the Government of the United Kingdom with such defense articles, defense services, and defense information as the President shall authorize to be transferred or provided.

- 2 -

ARTICLE II

The Government of the United Kingdom will continue to contribute to the defense of the United States of America and the strengthening thereof and will provide such articles, services, facilities or information as it may be in a position to supply.

ARTICLE III

The Government of the United Kingdom will not without the consent of the President of the United States of America transfer title to, or possession of, any defense article or defense information transferred to it under the Act or permit the use thereof by anyone not an officer, employee, or agent of the Government of the United Kingdom.

ARTICLE IV

If, as a result of the transfer to the Government of the United Kingdom of any defense article or defense information, it becomes necessary for that Government to take any action or make any payment in order fully to protect any of the rights of a citizen of the United States of America who has patent rights in and to any such defense article or information, the Government of the United Kingdom will take such action or make such payment when requested to do so by the President of the United States of America.

ARTICLE V

The Government of the United Kingdom will return to the United States of America at the end of the present emergency, as determined by the President, such defense articles transferred under this Agreement as shall not have been destroyed, lost or consumed and as shall be determined by the President to be useful in the defense of the United States of America or of the Western Hemisphere or to be otherwise of use to the United States of America.

ARTICLE VI

In the final determination of the benefits to be provided to the United States of America by the Government of the United Kingdom full cognizance shall be taken of all property, services, information, facilities, or other benefits or considerations provided by the Government of the United Kingdom subsequent to March 11, 1941, and accepted or acknowledged by the President on behalf of the United States of America.

ARTICLE VII

In the final determination of the benefits to be provided to the United States of America by the Government of the United Kingdom in return for aid furnished under the Act of Congress of March 11, 1941, the terms and conditions thereof shall be such as not to burden commerce between the two countries, but to promote mutually advantageous economic relations between them and the betterment of world-wide economic relations. To that end, they shall include provision for agreed action by the United States of America and the United Kingdom, open to participation

- 3 -

by all other countries of like mind, directed to the expansion, by appropriate international and domestic measures, of production, employment, and the exchange and consumption of goods, which are the material foundations of the liberty and welfare of all peoples; to the elimination of all forms of discriminatory treatment in international commerce, and to the reduction of tariffs and other trade barriers; and, in general, to the attainment of all the economic objectives set forth in the Joint Declaration made on August 12, 1941, by the President of the United States of America and the Prime Minister of the United Kingdom.

At an early convenient date, conversations shall be begun between the two Governments with a view to determining, in the light of governing economic conditions, the best means of attaining the above-stated objectives by their own agreed action and of seeking the agreed action of other like-minded Governments.

ARTICLE VIII

This Agreement shall take effect as from this day's date. It shall continue in force until a date to be agreed upon by the two Governments.

Signed and sealed at Washington in duplicate this 23rd day of February, 1942.

HOLD FOR RELEASE

HOLD FOR RELEASE

HOLD FOR RELEASE

FEBRUARY 25, 1942

CAUTION: The following address of the President MUST BE HELD IN CONFIDENCE until released.

2185

1738

NOTE: Release to editions of all newspapers appearing on the streets NOT EARLIER THAN 10:00 P.M., E.W.T., February 25, 1942. The same release of the text of the address also applies to radio announcers and news commentators.

CARE MUST BE EXERCISED TO PREVENT PREMATURE PUBLICATION.

STEPHEN EARLY
Secretary to the President

Washington's Birthday is a most appropriate occasion for us to talk with each other about things as they are today and things as we know they shall be in the future.

For eight years, General Washington and his Continental Army were faced continually with formidable odds and recurring defeats. Supplies and equipment were lacking. In a sense, every winter was a Valley Forge. Throughout the thirteen states there existed fifth columnists — selfish men, jealous men, fearful men, who proclaimed that Washington's cause was hopeless, that he should ask for a negotiated peace.

Washington's conduct in those hard times has provided the model for all Americans ever since — a model of moral stamina. He held to his course, as it had been charted in the Declaration of Independence. He and the brave men who served with him knew that no man's life or fortune was secure, without freedom and free institutions.

The present great struggle has taught us increasingly that freedom of person and security of property anywhere in the world depend upon the security of the rights and obligations of liberty and justice everywhere in the world.

This war is a new kind of war. It is different from all other wars of the past, not only in its methods and weapons but also in its geography. It is warfare in terms of every continent, every island, every sea, every air-lane in the world.

That is the reason why I have asked you to take out and spread before you the map of the whole earth, and to follow with me the references which I shall make to the world-encircling battle lines of this war. Many questions will, I fear, remain unanswered; but I know you will realize I cannot cover everything in any one report to the people.

The broad oceans which have been heralded in the past as our protection from attack have become endless battlefields on which we are constantly being challenged by our enemies.

We must all understand and face the hard fact that our job now is to fight at distances which extend all the way around the globe.

We fight at these vast distances because that is where our enemies are. Until our flow of supplies gives us clear superiority we must keep on striking our enemies wherever and whenever we can meet them, even if, for a while, we have to yield ground. Actually we are taking a heavy toll of the enemy every day that goes by.

We must fight at these vast distances to protect our supply lines and our lines of communication with our allies -- protect these lines from the enemies who are bending every ounce of their strength, striving against time, to cut them. The object of the Nazis and the Japanese is to separate the United States, Britain, China and Russia, and to isolate them one from another, so that each will be surrounded and cut off from sources of supplies and reinforcements. It is the old familiar Axis policy of "divide and conquer".

There are those who still think in terms of the days of sailing-ships. They advise us to pull our war ships and our planes and our merchant ships into our own home waters and concentrate solely on last ditch defense. But let me illustrate what would happen if we followed such foolish advice.

Look at your map. Look at the vast area of China, with its millions of fighting men. Look at the vast area of Russia, with its powerful armies and proven military might. Look at the British Isles, Australia, New Zealand, the Dutch Indies, India, the Near East and the Continent of Africa, with their resources of raw materials and of peoples determined to resist Axis domination. Look at North America, Central America and South America.

It is obvious what would happen if all these great reservoirs of power were cut off from each other either by enemy action or by self-imposed isolation:

1. We could no longer send aid of any kind to China -- to the brave people who, for nearly five years, have withstood Japanese assault, destroyed hundreds of thousands of Japanese soldiers, and vast quantities of Japanese war munitions. It is essential that we help China in her magnificent defense and in her inevitable counter-offensive -- for that is one important element in the ultimate defeat of Japan.

2. If we lost communication with the southwest Pacific, all of that area, including Australia and New Zealand, would fall under Japanese domination. Japan could then release great numbers of ships and men to launch attacks on a large scale against the coasts of the Western Hemisphere, including Alaska. At the same time, she could immediately extend her conquests to India, and through the Indian Ocean, to Africa and the Near East.

3. If we were to stop sending munitions to the British and the Russians in the Mediterranean and Persian Gulf areas, we would help the Nazis to overrun Turkey, Syria, Iraq, Persia, Egypt and the Suez Canal, the whole coast of North Africa and the whole coast of West Africa -- putting Germany within easy striking distance of South America.

4. If, by such a fatuous policy, we ceased to protect the North Atlantic supply line to Britain and to Russia, we would help to cripple the splendid counter-offensive by Russia against the Nazis, and we would help to deprive Britain of essential food-supplies and munitions.

Those Americans who believed that we could live under the illusion of isolationism wanted the American eagle to imitate the tactics of the ostrich. Now, many of those same people, afraid that we may be sticking our necks out, want our national bird to be turned into a turtle. But we prefer to retain the eagle as it is -- flying high and striking hard.

I know that I speak for the mass of the American people when I say that we reject the turtle policy and will continue increasingly the policy of carrying the war to the enemy in distant lands and distant waters — as far as possible from our own home grounds.

There are four main lines of communication now being travelled by our ships: the North Atlantic, the South Atlantic, the Indian Ocean and the South Pacific. These routes are not one-way streets — for the ships which carry our troops and munitions out-bound bring back essential raw materials which we require for our own use.

The maintenance of these vital lines is a very tough job. It is a job which requires tremendous daring, tremendous resourcefulness, and, above all, tremendous production of planes and tanks and guns and of the ships to carry them. And I speak again for the American people when I say that we can and will do that job.

The defense of the world-wide lines of communication demands relatively safe use by us of the sea and of the air along the various routes; and this, in turn, depends upon control by the United Nations of the strategic bases along those routes.

Control of the air involves the simultaneous use of two types of planes — first, the long-range heavy bomber; and, second, light bombers, dive bombers, torpedo planes, and short-range pursuit planes which are essential to the protection of the bases and of the bombers themselves.

Heavy bombers can fly under their own power from here to the southwest Pacific; but the smaller planes cannot. Therefore, these lighter planes have to be packed in crates and sent on board cargo ships. Look at your map again; and you will see that the route is long — and at many places perilous — either across the South Atlantic around South Africa, or from California to the East Indies direct. A vessel can make a round trip by either route in about four months, or only three round trips in a whole year.

In spite of the length and difficulties of this transportation, I can tell you that we already have a large number of bombers and pursuit planes, manned by American pilots, which are now in daily contact with the enemy in the Southwest Pacific. And thousands of American troops are today in that area engaged in operations not only in the air but on the ground as well.

In this battle area, Japan has had an obvious initial advantage. For she could fly even her short-range planes to the points of attack by using many stepping stones open to her — bases in a multitude of Pacific islands and also bases on the China, Indo-China, Thailand and Malay coasts. Japanese troop transports could go south from Japan and China through the narrow China Sea which can be protected by Japanese planes throughout its whole length.

I ask you to look at your maps again, particularly at that portion of the Pacific Ocean lying west of Hawaii. Before this war even started, the Philippine Islands were already surrounded on three sides by Japanese power. On the west, the Japanese were in possession of the coast of China and the coast of Indo-China which had been yielded to them by the Vichy French. On the North, are the islands of Japan themselves, reaching down almost to northern Luzon. On the east, are the Mandated Islands — which Japan had occupied exclusively, and had fortified in absolute violation of her written word.

These islands, hundreds of them, appear only as small dots on most maps. But they cover a large strategic area. Guam lies in the middle of them -- a lone outpost which we never fortified.

Under the Washington Treaty of 1898 we had solemnly agreed not to add to the fortification of the Philippine Islands. We had no safe naval base there, so we could not use the islands for extensive naval operations.

Immediately after this war started, the Japanese forces moved down on either side of the Philippines to numerous points south of them -- thereby completely encircling the Islands from north, south, east and west.

It is that complete encirclement, with control of the air by Japanese land-based aircraft, which has prevented us from sending substantial reinforcements of men and material to the gallant defenders of the Philippines. For forty years it has always been our strategy -- a strategy born of necessity -- that in the event of a full-scale attack on the Islands by Japan, we should fight a delaying action, attempting to retire slowly into Bataan Peninsula and Corregidor.

We knew that the war, as a whole would have to be fought and won by a process of attrition against Japan itself. We knew all along that, with our greater resources, we could outbuild Japan and ultimately overwhelm her on sea, on land and in the air. We knew that, to obtain our objective, many varieties of operations would be necessary in areas other than the Philippines.

Nothing that has occurred in the past two months has caused us to revise this basic strategy -- except that the defense put up by General MacArthur has magnificently exceeded the previous estimates; and he and his men are gaining eternal glory therefor.

MacArthur's army of Filipinos and Americans, and the forces of the United Nations in China, in Burma and the Netherlands East Indies, are all together fulfilling the same essential task. They are making Japan pay an increasingly terrible price for her ambitious attempts to seize control of the whole Atlantic world. Every Japanese transport sunk off Java is one less transport that they can use to carry reinforcements to their army opposing General MacArthur in Luzon.

It has been said that Japanese gains in the Philippines were made possible only by the success of their surprise attack on Pearl Harbor. I tell you that this is not so.

Even if the attack had not been made, your map will show that it would have been a hopeless operation for us to send the Fleet to the Philippines through thousands of miles of ocean, while all those island bases were under the sole control of the Japanese.

The consequences of the attack on Pearl Harbor -- serious as they were -- have been wildly exaggerated in other ways. These exaggerations come originally from Axis propagandists; but they have been repeated, I regret to say, by Americans in and out of public life.

- 5 -

You and I have the utmost contempt for Americans who, since Pearl Harbor, have whispered or announced "off the record" that there was no longer any Pacific Fleet -- that the Fleet was all sunk or destroyed on December 7th -- that more than 1,000 of our planes were destroyed on the ground. They have suggested slyly that the government has withheld the truth about casualties -- that eleven or twelve thousand men were killed at Pearl Harbor instead of the figures as officially announced. They have even served the enemy propagandists by spreading the incredible story that shiploads of bodies of our honored American dead were about to arrive in New York harbor to be put in a common grave.

Almost every Axis broadcast directly quotes Americans who, by speech or in the press, make damnable misstatements such as these.

The American people realize that in many cases details of military operations cannot be disclosed until we are absolutely certain that the announcement will not give to the enemy military information which he does not already possess.

Your government has unmistakable confidence in your ability to bear the worst, without flinching or losing heart. You must, in turn, have complete confidence that your government is keeping nothing from you except information that will help the enemy in his attempt to destroy us. In a democracy there is always a solemn pact of truth between government and the people; but there must also always be a full use of discretion -- and that word "discretion" applies to the critics of government as well.

This is war. The American people want to know, and will be told, the general trend of how the war is going. But they do not wish to help the enemy any more than our fighting forces do; and they will pay little attention to the rumor-mongers and poison peddlers in our midst.

To pass from the realm of rumor and poison to the field of facts: the number of our officers and men killed in the attack on Pearl Harbor on December seventh was 2,340, and the number wounded was 946. Of all the combatant ships based on Pearl Harbor -- battleships, heavy cruisers, light cruisers, aircraft carriers, destroyers and submarines -- only three were permanently put out of commission.

Very many of the ships of the Pacific Fleet were not even in Pearl Harbor. Some of those that were there were hit very slightly; and others that were damaged have either rejoined the Fleet by now or are still undergoing repairs. When those repairs are completed, the ships will be more efficient fighting machines than they were before.

The report that we lost more than a thousand airplanes at Pearl Harbor is as baseless as the other weird rumors. The Japanese do not know just how many planes they destroyed that day, and I am not going to tell them. But I can say that to-date -- and including Pearl Harbor -- we have destroyed considerably more Japanese planes than they have destroyed of ours.

We have not certainly suffered losses -- from Hitler's U-Boats in the Atlantic as well as from the Japanese in the Pacific -- and we shall suffer more of them before the turn of the tide. But, speaking for the United States of America, let me say once and for all to the people of the world: We Americans have been compelled to yield ground, but we will regain it. We and the other United Nations are committed to the destruction of the militarism of Japan and Germany. We are daily increasing our strength. Soon, we and not our enemies, will have the offensive; we, not they, will win the final battles; and we, not they, will make the final peace.

Conquered nations in Europe know what the yoke of the Nazis is like. And the people of Korea and of Manchuria know in their flesh the harsh despotism of Japan. All of the people of Asia know that if there is to be an honorable and decent future for any of them or for us, that future depends on victory by the United Nations over the forces of Axis enslavement.

If a just and durable peace is to be attained, or even if all of us are merely to save our own skins, there is one thought for us here at home to keep uppermost -- the fulfillment of our special task of production -- uninterrupted production. I stress that word uninterrupted.

Germany, Italy and Japan are very close to their maximum output of planes, guns, tanks and ships. The United Nations are not -- especially the United States of America.

Our first job then is to build up production so that the United Nations can maintain control of the seas and attain control of the air -- not merely a slight superiority, but an overwhelming superiority.

On January sixth of this year, I set certain definite goals of production for airplanes, tanks, guns and ships. The Axis propagandists called them fantastic. Tonight, nearly two months later, and after a careful survey of progress by Donald Nelson and others charged with responsibility for our production, I can tell you that those goals will be attained.

In every part of the country, experts in production and the men and women at work in the plants are giving loyal service. With few exceptions, labor, capital and farming realize that this is no time either to make undue profits or to gain special advantages, one over the other.

We are calling for new plants and additions to old plants and for plant conversion to war needs. We are seeking more men and more women to run them. We are working longer hours. We are coming to realize that one extra plane or extra tank or extra gun or extra ship completed tomorrow may, in a few months, turn the tide on some distant battlefield; it may make the difference between life and death for some of our fighting men. We know now that if we lose this war it will be generations or even centuries before our conception of democracy can live again. And we can lose this war only if we slow up our effort or if we waste our ammunition sniping at each other.

Here are three high purposes for every American:

1. We shall not stop work for a single day. If any dispute arises we shall keep on working while the dispute is solved by mediation, conciliation or arbitration -- until the war is won.

2. We shall not demand special gains or special privileges or advantages for any one group or occupation.

3. We shall give up conveniences and modify the routine of our lives if our country asks us to do so. We will do it cheerfully, remembering that the common enemy seeks to destroy every hope and every freedom in every part of our land.

This generation of Americans has come to realize, with a present and personal realization, that there is something larger and more important than the life of any individual or of any individual group -- something for which a man will sacrifice, and gladly sacrifice, not only his pleasures, not only his goods, not only his associations with those he loves, but his life itself. In time of crisis when the future is in the balance, we come to understand, with full recognition and devotion, what this nation is, and what we owe to it.

The Axis propagandists have tried in various evil ways to destroy our determination and our morale. Failing in that, they are now trying to destroy our confidence in our own allies. They say that the British are finished -- that the Russians and the Chinese are about to quit. Patriotic and sensible Americans will reject these absurdities. And instead of listening to any of this crude propaganda, they will recall some of the things that Nazis and Japanese have said and are still saying about us.

Ever since this nation became the arsenal of democracy -- ever since enactment of Lend-lease -- there has been one persistent theme through all Axis propaganda.

This theme has been that Americans are admittedly rich, and that Americans have considerable industrial power -- but that Americans are soft and decadent, that they cannot and will not unite and work and fight.

From Berlin, Rome and Tokyo we have been described as a nation of weaklings -- "playboys" -- who would hire British soldiers, or Russian soldiers, or Chinese soldiers to do our fighting for us.

Let them repeat that now!

Let them tell that to General MacArthur and his men.

Let them tell that to the sailors who today are hitting hard in the far waters of the Pacific.

Let them tell that to the boys in the Flying Fortresses.

Let them tell that to the Marines!

The United Nations constitute an association of independent peoples of equal dignity and importance. The United Nations are dedicated to a common cause. We share equally and with equal zeal the anguish and awful sacrifices of war. In the partnership of our common enterprise, we must share in a unified plan in which all of us must play our several parts, each of us being equally indispensable and dependent one on the other.

We have unified command and cooperation and comradeship.

We Americans will contribute unified production and unified acceptance of sacrifice and of effort. That means a national unity that can know no limitations of race or creed or selfish politics. The American people expect that much from themselves. And the American people will find ways and means of expressing their determination to their enemies, including the Japanese Admiral who has said that he will dictate the terms of peace here in the White House.

We of the United Nations are agreed on certain broad principles in the kind of peace we seek. The Atlantic Charter applies not only to the parts of the world that border the Atlantic but to the whole world; disarmament of aggressors, self-determination of nations and peoples, and the four freedoms -- freedom of speech, freedom of religion, freedom from want, and freedom from fear.

The British and the Russian people have known the full fury of Nazi onslaught. There have been times when the fate of London and Moscow was in serious doubt. But there was never the slightest question that either the British or the Russians would yield. And today all the United Nations salute the superb Russian Army as it celebrates the twenty-fourth anniversary of its first assembly.

Though their homeland was overrun, the Dutch people are still fighting stubbornly and powerfully overseas.

The great Chinese people have suffered grievous losses; Chungking has been almost wiped out of existence -- yet it remains the capital of an unbeatable China.

That is the conquering spirit which prevails throughout the United Nations in this war.

The task that we Americans now face will test us to the uttermost.

Never before have we been called upon for such a prodigious effort. Never before have we had so little time in which to do so much.

"These are the times that try men's souls".

Tom Paine wrote those words on a drum-head, by the light of a campfire. That was when Washington's little army of ragged, rugged men was retreating across New Jersey, having tasted nothing but defeat.

And General Washington ordered that these great words written by Tom Paine be read to the men of every regiment in the Continental Army, and this was the assurance given to the first American armed forces:

"The summer soldier and the sunshine patriot will, in this crisis, shrink from the service of their country; but he that stands it now, deserves the love and thanks of man and woman. Tyranny, like hell, is not easily conquered; yet we have this consolation with us, that the harder the sacrifice, the more glorious the triumph".

So spoke Americans in the year 1776.

So speak Americans today!

February 23, 1942

Dear Dr. Soong:

This will acknowledge receipt of your letter of February 21st enclosing a confidential report received from Switzerland, which I read with much interest. Thank you for sending it to me.

Yours sincerely,

(Signed) H. Morgenthau, Jr.

Dr. T. V. Soong,
Minister for Foreign Affairs
Republic of China,
1801 V Street,
Washington, D. C.

Filed M.C.
By Messenger *Johnson 3-50*

MINISTER FOR FOREIGN AFFAIRS
REPUBLIC OF CHINA

February 21, 1942

Dear Mr. Morgenthau:

I am sending you for your information
a report which we have received from our Military
Intelligence in Switzerland.

Yours sincerely,

T. V. Soong

*Signed in absence of
Mr. Soong by
Henry Su
Sent by Dr. T.V. Soong.*

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

SECRET

142

REPORT FROM OUR MILITARY INTELLIGENCE IN SWITZERLAND, FEBRUARY 20, 1942

"As you know, prior to the invasion of France in an effort to avert war, there was a plot by some of the German army officers and members of the Deutsch National Party to get rid of Hitler and install in his place Beck, the former Chief of Staff. This plot never materialized because the higher officers were afraid to launch it, and after the collapse of France Beck was inactive.

"The defeat sustained by Germany at the hands of Soviet Russia has undermined the confidence of the high military officers in Hitler, so that the plot has been revived. Whether the plot will succeed or fail depends on the ability of ranking army officers to oust Hitler before the force of the German Army is lowered. The plot calls for the cooperation of Great Britain; according to their view, Great Britain is unable to score any decisive victory over Germany within the next two years, even with the assistance of the United States. Influenced by the general distrust of Soviet Russia prevailing among all nations in western Europe, Great Britain is expected to react favorably to this German overture. The German officers are of the opinion that the war has created a national crisis which transcends all considerations of the Nazi Party.

"The following is reported to be Hitler's war plan:

"(1) As soon as weather conditions become favorable, the Germans will invade the Caucasus. Later, when a general offensive is launched on the central and northern sectors, the Germans hope that Japan will simultaneously attack Siberia and that the Russian supply routes from Great Britain and the United States will be cut.

"(2) After the reorganization of the Italian Army has been completed, the Axis will stage a full scale attack in the Mediterranean. Air attacks will be made on Malta and Gibraltar, while, in cooperation with the Axis troops in North Africa, a combined attack by land and sea will be made against the Suez Canal, making a junction with the Japanese navy in the Indian Ocean. It is further reported that the German army may go through Turkey at the end of March with the aim of reaching the Persian Gulf."

TREASURY DEPARTMENT

143

INTER OFFICE COMMUNICATION

DATE February 23, 1942

TO Secretary Morgenthau

FROM Mr. White

Subject: Shipment of Gold from Germany to Switzerland

1. At least \$70 million in gold has been transferred from Germany to Switzerland since March 1941, according to fragmentary information received from the British Embassy in Washington and the American Consulate in Bern.

In the latter part of March 1941, Germany sold to various Swiss banks about \$8 million in gold.

In the early part of April 1941, an unspecified number of bars of Czechoslovakian gold was disposed of by the Reichsbank to private Swiss banks.

From the end of October to the beginning of December 1941, more than 21 tons (over \$23 million) of gold passed through Basle en route from Berlin to the Swiss National Bank at Bern.

On December 7, 1941, 7.5 tons (over \$8 million) in gold arrived at Bern from Berlin.

During the week ending December 27, 1941, 20 tons (about \$22 million) in gold entered Switzerland from Germany consigned to the Swiss National Bank.

On January 23, 1942, 5 tons of gold (about \$5.5 million) passed through Basle en route to Bern.

2. We cannot account for the disposition of all this gold. We do know that up to January 1, 1942, at least \$12 million worth had been converted into escudo credits in Portugal in favor of the Reichsbank. Part of the credits so secured has been used by Germany to pay for purchases of Portuguese tungsten ore and other materials imported by Portugal.

Another part of these gold shipments has possibly been for the purpose of effecting capital transactions for ultimate German account through Swiss intermediaries.

The rest of the gold may have been used to pay for various other imports and services or to increase balances held by the Reichsbank in Switzerland or in other countries.

Treasury Department
Division of Monetary Research

144

Date February 23, 1942

To: Secretary Morgenthau

From: Mr. White

France - North Africa - Gold

On February 6, 1942, you sent a letter to the President suggesting the possibility of intercepting one of the planes carrying gold from Algiers to Marseille and thus forcing the discontinuance of these shipments.

The American Consulate General in Algiers suggests again that one of these planes should be intercepted or, if such interception is impractical, that the BBC give publicity to what is going on and thus, perhaps, frighten the French authorities into stopping it, at least temporarily.

From Consulate, Algiers,
No. 96, February 15, 1942

C
O
P
Y

145

DEPARTMENT OF STATE
WASHINGTON

February 21, 1942

In reply refer to
FD 855.51/840

The Secretary of State presents his compliments to the Honorable the Secretary of the Treasury and encloses copies of a paraphrase of telegram no. 96, dated February 15, 1942, from the American Consulate General, Algiers, Algeria, concerning gold shipments from North Africa to Europe.

Enclosure:

From Consulate, Algiers,
no. 96, February 15, 1942.

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Consulate General, Algiers, Algeria

DATE: February 15, 1942, 3 p.m.

NO.: 96

The message is from Mr. Murphy and refers to telegram no. 47, dated January 24, 1942, sent by the Consulate.

Surprise was indicated by one of the officials by whom information from time to time has been supplied concerning shipments of gold to Europe from North Africa that nothing has been done to bring these shipments of gold to Marseille from Algiers to an end. He stated that as explained in the telegram under reference these shipments are being made regularly. (This gold was referred to as Belgian gold by him.)

He wanted to know why the British Broadcasting Corporation could not refer to these gold shipments several times and thus frighten the authorities at Vichy and Paris to cease at least temporarily this activity if the suggestion made in the telegram under reference to intercept one of the planes was not practical. The Department's comment on the foregoing would be appreciated.

The telegram was repeated to London and to Vichy for repetition to Tangier for Mr. Eddy.

COLE

Copy:vw:2-21-42

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE February 23, 1942

TO Secretary Morgenthau

FROM Mr. White

SUBJECT: Ecuadoran Stabilization Agreement

The Draft Stabilization Agreement we want to turn over to Dr. Salazar as soon as possible contains the following major provisions:

1. The commitment to Ecuador is \$5 million.
2. The interest charge is 1 1/2 percent per annum on the dollars drawn.
3. Repayment is required after a notice period of 180 days and is to be made in six equal instalments spread over a second period of 180 days.

Dr. Salazar made strong representations for liberalization both of the notice and repayment periods. After considerable discussion, it was decided that, if you approve, a compromise might be reached under which Ecuador would still be required to begin repayments after notice of 180 days but would be allowed to repay in 12 equal instalments spread over a period of 360 days instead of six payments over 180 days.

4. The Banco Central del Ecuador is not a signatory to this agreement and therefore does not guarantee repayment. In this respect it differs from other Stabilization Agreements.

Dr. Salazar strongly resisted the inclusion of the Banco Central as a signatory. He felt it would weaken the position of the Ecuadoran Treasury vis-a-vis the Banco Central and raise a difficult political problem within Ecuador before the Bank's signature could be obtained. We agree with him on this point.

Before giving Dr. Salazar the draft we would like your approval of point 4 and of the change proposed in point 3.

OK [Signature]

148

BRITISH EMBASSY
WASHINGTON, D.C.

PERSONAL AND SECRET

February 23rd, 1942.

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.

BRITISH MOST SECRET

(U.S. SECRET)

OPTEL No. 63

Information received up to 7 A.M., 22nd February, 1942.

1. NAVAL

An enemy force reported as two battleships, 3 cruisers and destroyers steering north was sighted on 21st by a Hudson aircraft on reconnaissance at 11.15 A.M. off the west coast of DENMARK. At 7.28 this morning Beaufighter reported 2 battleships and 3 destroyers about 15 miles north-west of STAVANGER steering north-east. 2 striking forces of Beauforts were despatched yesterday afternoon but neither force reached its objective owing to extremely bad visibility. A 5,000 ton Greek vessel was sunk yesterday by mine off HARWICH. A British 8,000 ton tanker was shelled and torpedoed on 21st off TRINIDAD and has been abandoned. A 4,000 ton British motor ship has been bombed and beached off WYNDHAM (AUSTRALIA).

2. MILITARY

LIBYA. Our patrols have been active in the TIDMI-MEKILI area and as far as MEUS. Air reconnaissance revealed about 2,000 enemy motor vehicles in the DERNA-CAMUSA area.

BURMA. Severe fighting behind the river BILIN continues, casualties have been heavy on both sides. Our main positions are intact.

3. AIR OPERATIONS

WESTERN FRONT. 21st. Our fighters on shipping reconnaissance attacked a 3,000 ton vessel at BOULOGNE, a 1,000 ton vessel of PECAMP and an A.A. ship off CALAIS. Spitfires damaged a German bomber over LIVERPOOL BAY.

21st/22nd. Forty-two aircraft were sent on roving commissions over north-west GERMANY and 6 others were mine laying. Weather was good over the RUHR. 3 aircraft are missing.

LIBYA. 20th. Bad weather restricted operations. A German bomber was probably destroyed near MERSA MATRUH.

MALTA. 20th/21st, and 21st. A total of 55 enemy aircraft attacked our aerodromes. Damage was caused to a hangar at KALAFRANA and 2 barracks at HAL FAR and LUQA. 1 aircraft on the ground was destroyed and 7 more were damaged. 1 German bomber was probably destroyed by our fighters.

150
BRITISH EMBASSY
WASHINGTON, D.C.

February 23rd, 1942.

PERSONAL AND SECRET

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.

Copy No. 13

BRITISH MOST SECRET

(U.S. SECRET)

OPTEL No. 62

Information received up to 7 A.M. 21st February, 1942.

1. NAVAL

The Fres French submarine SURCOUF is overdue in the Panama Canal Zone. A U.S. Transport reported that on the night of the 18th she accidentally rammed and sank a craft believed to be a submarine in the Canal Zone. A report has been received giving incomplete information regarding a Naval action in the LOMBOK Strait. It is probable that we lost two destroyers and sank or damaged one enemy cruiser and a destroyer. During the air attack on DARWIN on the 19th a U.S. destroyer and six Merchant ships were sunk. An Australian minesweeper and two Merchant ships were seriously damaged. A U.S. 8,000 ton tanker and a medium sized U.S. Merchant vessel have been torpedoed off the East Coast of Florida and West of MARTINIQUE respectively. A British merchant vessel of medium tonnage is reported torpedoed and sunk off MADRAS on the 15th.

2. MILITARY

Libya. 18th. Enemy columns with tanks were again active between our GAZALA-BIR HAKEIKY position and their forward TWIMI - MEXILI Area. Three of these columns advanced but were later forced to withdraw by our light forces. Our armoured cars have been active in this area. 1,500 dispersed M.T. were reported in MEXILI Area.

Burma. 19th. Severe close fighting has continued on the River BILIN during the last two days. There has been little change in positions. Two of our Gurkha Battalions have made successful counter-attacks.

Russia. Heavy fighting continues in the DONETS Area where the Russians are effectively holding German attacks.

3. AIR OPERATIONS

Western Front. 20th. Six small offensive fighter operations were successfully carried out against minor military objectives in Northern France. One enemy fighter was destroyed and one Spitfire is missing.

Malta. 20th. Nineteen enemy aircraft attacked TAKALI Aerodrome and KALAFRANA dockyard without causing serious damage. Two bombers were damaged by Hurricanes.

- 2 -

Burma. 19th. Seventeen Blenheims escorted by Hurricanes successfully attacked enemy concentrations in the battle area and two Hurricanes attacked enemy transport on the Road North of THATON. Enemy aircraft bombed YYINMAND (forty miles North of TOUNGOO) and MANDALAY.

Australia. North DARWIN. Two attacks were made by a total of ninety three bombers and twelve fighters. The wharves and also R.A.F. buildings were severely damaged. Six Hudsons, two Tomahawks and one Liberator were destroyed on the ground. Five enemy aircraft were shot down and five others probably destroyed. Ten Tomahawks were lost in air fighting.

5. It is reported that in exchange for the use of the LIBYA supply route of requisitioned Allied ships, the Germans are allowing the French to retain for their own use until 11/42, the total production of Military aircraft in the Unoccupied Zone. This is unlikely to exceed 400 aircraft.

TREASURY DEPARTMENT

153

INTER OFFICE COMMUNICATION

DATE February 23, 1942

TO Secretary Morgenthau
FROM Mr. Kamsrck
Subject: Summary of Military Reports

Spain

Two Spanish ships have been allowed to take on cargoes of gas oil in the United States. Colonel Donovan's office states that "it appears likely that ...these vessels will be allowed to proceed in return for Spanish assurances regarding final disposition of the oil...."

(C.O.I., "The War This Week," February 12-19, 1942)

German Navy

The German battleship, Tirpitz, was sighted under way in Trondheim fjord on the 19th of February.

(U.K. Operations Report, February 20, 1942)

Mediterranean

The Germans have concentrated 700 or more planes in Crete and southern Italy. (This concentration of German planes, the presence of a large number of German submarines in the Mediterranean, the continuous attacks on Malta, and the reinforcement of Rommel with men and equipment, all point to the great importance the Germans place on the Libyan sector.)

(C.O.I., "The War This Week," February 12-19, 1942)

French Collaboration with the Axis

According to a well-placed French source, "the 1942 programme of the Secretariat of industrial production includes the construction of 3,000 aircraft

(250 per month), of which four-fifths are earmarked for the Germans and one-fifth for the French."

(C.O.I., February 23, 1942)

It is reported that the French Vichy Government has agreed to German demands that 120,000 tons of Allied shipping lying in French ports be requisitioned. These ships are to be used under the French flag for transporting supplies to the Axis forces in Libya.

(U.K. Operations Report, February 20, 1942)

Blockade of the Axis

There are clear indications that arrangements are being made to send blockade runners from European waters to the Far East. Japan is showing particular interest in machinery for steel plants and coke ovens, and precision instruments.

(With the Germans making use of the entire Western European coast line and all the ports of northwest Africa, and with the Japanese having free access into the Indian Ocean, the blockade of the Axis countries must inevitably become considerably less effective, at least in the near future.)

(U.K. Operations Report, February 20, 1942)



UNITED STATES GOVERNMENT
COORDINATOR OF INFORMATION
WASHINGTON, D. C.

155

February 23, 1942

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

Dear Henry:

We have just received the information in the attached memorandum which may be of interest.

Sincerely,

Bill
William J. Donovan

It has been learned that on January 21, 1942, Sr. Doctor Alberto Zerega Fombona, Enviado Extraordinario and Ministro Plenipotenciario de los Estados Unidos de Venezuela, Madrid, Spain, received a circular letter from his government which calls attention to the fact that, since the breaking off of diplomatic relations with Germany, Italy and Japan, the Diplomatic and Consular officials of Venezuela in Germany and Japan have been removed from their official seats and their whereabouts are unknown, but that Italy has, so far, continued to treat the Venezuelan representatives with accustomed courtesy.

Extracts from the letter are as follows:

"The Ministry has received information from certain South American Governments to the effect that, consequent on the breaking off of diplomatic relations with the Governments of Germany, Italy and Japan, Dr. Rafael Angarita Arvelo, Diplomatic Representative of Venezuela in Berlin; Sr. Eduardo Marturet, Civil Attache to the Legation in France, who was discharging his Consular office in Paris; Sr. Pedro Alfonso Acero, the official in charge of the Archives of the Consulate General of Venezuela in Hamburg, and Dr. Carlos Rodriguez Jimenez, Consul General of Venezuela in Tokyo, have been taken away from their respective posts and sent to other destination, thus finding themselves cut off entirely from all contact with the Government of Venezuela.

With regard to our representatives in Italy, the

-2-

Venezuelan Government has received guarantees which prove that they have been and are continuing to be treated with all due courtesy and are able to communicate with this Ministry without any hindrance whatsoever. The Government of Venezuela has, therefore, reciprocated and granted freedom of action, in so far as circumstances permit, to the diplomatic and consular representatives of Italy".



UNITED STATES GOVERNMENT
COORDINATOR OF INFORMATION
WASHINGTON, D. C.

158

February 23, 1942

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

Dear Henry:

The attached, is a report made by
Axel Paulin, of the Swedish Legation in
Santiago, Chile, on January 28, 1942, to his
government.

Sincerely,

Bill
William J. Donovan

The Rio Conference is now over, its convocation can be ascribed to the present Foreign Minister of Chile, Dr. Rossetti. Some details about this man may be of interest and throw light on the above-mentioned conference. Dr. Rossetti, lawyer and journalist - he owns a paper "La Opinion" - is a relatively young man, intelligent, ambitious and of a particularly dynamic personality. About four months ago he started rising towards great heights, when he was appointed Foreign Minister without having previously held any official post. He is the first Chilean Foreign Minister who does not belong to the circle from which such officials have so far been drawn. Contrary to these, who usually come from the Chilean oligarchy, he descends from Italian immigrants. Shortly after taking over his present position he unexpectedly got wind into his sails. In November a Eucharistic conference was held here with great pomp and a week later there followed the visit of the Brazilian Foreign Minister. As the President of the Republic, already desperately ill, was unable to attend, Dr. Rossetti had to take his place. This gave impetus to his ambitions. He then conceived the idea of convening the American Foreign Ministers in order to discuss the situation created by the Japanese aggression. It was expected that Chile should to a certain degree follow Argentine's lead rather than follow in the wake of the States dominated by the U. S. Dr. Rossetti advocates a policy of neutrality rather than a hazardous jump into the tangles of war.

This country's relatively friendly attitude towards the Axis powers may up to a point be ascribed to their particularly well-chosen representatives here, as well as to the large admixture of German blood in the population. The German Ambassador here, Baron Von Schoen, and his American-born wife, are the most highly respected foreign representatives by both friends and adversaries, and their hospitable home has always been a centre of social life in Santiago.

About a week ago about ten large North American planes arrived and settled down in the Chilean marine airport. They show no signs of continuing their journey. The Chileans are by no means enthusiastic about this prolonged visit. In official circles the subject of the presence of these North Americans is avoided as much as possible.

He also sent a communication to Harald Fallenius, Kungl. Utrikesdepartementet, Stockholm, dated 28th January, 1942, as follows:

"Should Chile and Argentine sell themselves to their sister republics and break off relations with the Axis powers, then the direct sea traffic from Sweden to these countries would automatically cease..I wish to inform you that the German Ambassador here has told me that it is his intention, should Chile be obliged to break off diplomatic relations with his country, a possibility which is not remote and may only be a question of time, to ask that the Swedish representatives be entrusted with the care of the German interests.



UNITED STATES GOVERNMENT
COORDINATOR OF INFORMATION
WASHINGTON, D. C.

161

February 23, 1942

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

Dear Henry:

The attached, is a memorandum on the
German order of battle in France as of the
beginning of February.

Sincerely,

Bill
William J. Donovan

ARMY GROUP D (S'Germain en Laye) (Includes 3 Armies)

XV Army (Tourcoing) includes:

221 D.I. (Bruges) consisting of Inf. Regts:	265, 412, 497
208 (Hazebrouk)	308, 309, 337
322 (Montreuil)	588, 589, 590
302 (Dieppe)	570, 571, 572
336 (Le Havre)	685, 686, 687
323 (Caen)	591, 593, 594
711 (Countances)	721, 731
319 (Dinan)	582, 583, 584
320 (Lannion)	585, 586, 587
716 (?)	

TOTAL 10

VII Army (Bordeaux)

165,335 (Brest)	682, 683, 684
305 (Vannes)	576, 577, 578
327 (La Rochelle)	595, 596, 597
708 (Bordeaux)	718, 728
333 (Biarritz)	679, 680, 681
715 (Angouleme)	725, 735
332 (Le Mans)	676, 677, 678

TOTAL 8

I (Fontainebleau)

337 (Bourges)	688, 689, 690
211 (Auxerre) ?	
8 (Beaune)	28, 38, 84
28 light (Besancon)	49, 83
202 ? (Camp Mailly)	233, 235, 286
71 ? (Reims)	191, 194, 211

TOTAL 6

-2-

- Notes: 1. In the occupied zone (eastern part) there are numerous Ersatz units.
2. The following Armored Divisions are probably being formed in the regions indicated:
- PARIS region, 23rd Division (Armored)
NIORT region, 22nd Division (Armored)
3. The following divisions have left France:

225	246
216	88
83	205
41	5 (light)
81	

The following information is from a very well-placed French source:

"The 1942 programme of Secretariat of industrial production includes the construction of 3000 aircraft, of which four-fifths are earmarked for the Germans and one-fifth for the French."

[C.O.I. February 23, 1942]

RESTRICTED

MID 319.1 No. 659 M.I.D., W.D. 11:00 A.M., February 23, 1942.
Situation 8-11-41

SITUATION REPORTI. Pacific Theater.

Philippines: Little activity reported on the fronts.
Burma: After heavy fighting the British were forced to withdraw in certain sectors to avoid encirclement. Japanese bombers were active as allied aircraft sought to stem the advance of enemy ground troops. Japanese pressure toward north Burma continues.
N.E.I.: The Japanese have effected a landing on Bali and have achieved control of one airfield. The Netherlands Government in London states that the greater part of the Japanese fleet used for the invasion of Bali has been destroyed. Tokyo reports Japanese air units attacked Baven Island north of Soerabaja. The N.E.I. High Command states Netherlands planes attacked Japanese in Palembang area. Australia: No new developments to report.

II. Western Theater.

R.A.F. bombers attacked ports and other objectives on the night of February 22/23 in Northwest Germany.

III. Eastern Theater.

No change in the situation has been reported. (A situation map will not be issued today.)

IV. Middle Eastern Theater.

Libya: Cairo communique indicates that British patrols operating east of TMIMI and south of TMIMI and MEKILI are meeting "heavier resistance" from Axis columns operating in the same area. The communique also indicates that Axis activity is on an increasing scale. German High Command reported on February 22 that 2 British Merchant vessels had been sunk as a result of German attacks off Sidi Barrani, Egypt.

RESTRICTED

February 24, 1942
9:35 a.m.

HMJr: Hello.

Operator: Secretary Knox.

HMJr: Hello.

Secretary Knox: Hello, Henry.

HMJr: Good morning.

K: Knox talking.

HMJr: Morgenthau talking.

K: (Laughs) All right, Henry. That luncheon for Thursday is okay.

HMJr: And you'll come here?

K: Yes.

HMJr: I'll have a mat out for you.

K: (Laughs) That's good.

HMJr: That includes King.

K: That does. I know who you're asking me for. I'm not deluded at all.

HMJr: What's that?

K: (Laughs)

HMJr: What's that?

K: I say I know why you're asking me. I'm not deluded at all.

HMJr: Now, listen, how many times have I asked you and nobody else.

K: (Laughs) I know.

HMJr: What?

- 2 -

K: I know. I'm just kidding you. All right, Henry.

HMJr: And I needn't call him.

K: No. No, you don't need to call him.

HMJr: I'll look forward to seeing you and King.

K: All right, Henry.

HMJr: Thank you.

K: Good-bye.

February 24, 1942
9:40 a.m.

LOAN TO ECUADOR

Present: Mr. Bell
Mr. White
Mrs. Klotz

H.M.JR: This is what I call service, Professor White. I will read it out loud. This is from Mr. White, entitled, "Frantic."

"The Draft Stabilization Agreement we want to turn over to Dr. Salazar as soon as possible contains the following major provisions:

"1. The commitment to Ecuador is \$5 million."

Well, we have agreed on that.

"2. The interest charge is 1 1/2 percent per annum."

That is what surprised me. I thought we charged a half a percent above the Federal Reserve rate.

MR. WHITE: We started that way, and then in the last two agreements we decided to make it a fixed rate which we could change each year if necessary.

H.M.JR: I thought it sounded better. What do you think?

MR. BELL: The trouble with making it a half percent above the discount rate, all of these people object. They say, "How do we know, it may be six percent one year from now." We started including just the rate.

H.M.JR: What do you think?

- 2 -

MR. BELL: I think it is all right.

H.M.JR: O.K.

"3. Repayment is required after a notice period of 180 days and is to be made in six equal instalments spread over a second period of 180 days."

MR. WHITE: That is what the Mexicans want.

H.M.JR: "Dr. Salazar made strong representations for liberalization both of the notice and repayment periods. After considerable discussion, it was decided that, if you approve, a compromise might be reached under which Ecuador would still be required to begin repayments after notice of 180 days but would be allowed to repay in 12 equal instalments spread over a period of 360 days instead of six payments over 180 days."

MR. WHITE: There is a special reason for that that might be weighty. This amount of five million dollars, if they do borrow it, is, compared with Ecuador's balance of payments, very large; and, if they are called upon to repay, they would have an extremely difficult time to pay that back within six months; and since, if they are making payments each month, it is not a serious matter to wait a year instead of six months.

MR. BELL: How do you think we are going to get by with all of these different provisions in these different agreements? Argentine is on a different basis.

MR. WHITE: Argentine has already indicated that if there is going to be an agreement, she wants to re-examine the terms in the light of the more liberal terms given to Mexico, and I think there will be a tendency for every one who has got shorter terms and who is bound to learn about the longer terms to try to get the better ones. The only thing that can be said in respect to that is that in many cases longer terms are justified on the basis of repayment; and, where it isn't, I think we can make a strong case and take a position that each agreement,

as far as its terms are concerned, depends upon the country and the conditions.

MR. BELL: Certainly you have got to give Argentine equal to Mexico.

MR. WHITE: I think so, and I think if Argentine comes up again, they have every intention of reopening the subject and getting as good terms as Mexico got.

H.M.JR: What has Mexico got?

MR. WHITE: Six months.

H.M.JR: But Ecuador is three hundred sixty days.

MR. WHITE: That is six months. Six months notice and six months repayment.

H.M.JR: That is Mexico?

MR. WHITE: Both Mexico and Ecuador. They are the same.

H.M.JR: No. Ecuador, a hundred and eighty days will be allowed to repay twelve equal payments.

MR. WHITE: What we are suggesting for Ecuador is an additional six months to repay it.

H.M.JR: Yes, that is what I say, so that we give a six months' notice, and then she has a year to pay.

MR. WHITE: Yes, but she has to pay - begin paying at the end of the first month, in monthly instalments.

H.M.JR: Oh, at the end of the first month?

MR. WHITE: Well, six months' notice, she doesn't pay anything. After that she begins each month to make a payment.

H.M.JR: Well, there is six months' notice and a year

- 4 -

to pay.

MR. WHITE: That is right, eighteen months from the day of notice to the final completion, if she meets her obligations.

H.M.JR: And Mexico has twelve months.

MR. WHITE: That is right.

H.M.JR: Well, in fairness, don't you think you ought to have a most-favored-nation clause?

MR. WHITE: I don't think so, because it seems to me that the situation differs in each country, and we can make out - Ecuador can make out a much better case than Mexico could on the basis of that.

H.M.JR: Would Mexico agree to that, that Ecuador has a better case? I like to be a one-price house.

MR. WHITE: I think it is going to be difficult if we take that position all the way around. China, for example, has an entirely different price. I think we had better maintain flexibility. The answer is that Ecuador is not entitled to five million dollars on the basis of her setup.

MR. BELL: They upped us a couple of million, didn't they?

MR. WHITE: Yes. In other words, Ecuador is getting more than her economy would justify.

MR. BELL: I am wondering if we could stick to the form that we started out with, say with Mexico, and then promise a renewal in the Ecuadorian situation.

MR. WHITE: We could.

- 5 -

MR. BELL: Which you would have to give anyhow if they couldn't make it.

MR. WHITE: I think, from a technical point of view, if a country is making payments and reducing its debt, it is all right to give them a little more time because five million dollars amounts to half her trade, practically, and to expect her to make that up in six months is to expect too much.

H.M.JR: It is a lot.

MR. BELL: I agree it is too much, and I agree they can't pay it.

H.M.JR: What is your suggestion?

MR. BELL: I thought maybe we could put them all on the same basis, but in the case of those countries like Ecuador we could promise maybe a renewal or an extension of six months.

H.M.JR: That wouldn't help any.

The point is, supposing we want to terminate it? We would only give the six months' notice if we want to terminate, and also toward Congress we have got to have something.

- 6 -

MR. WHITE: Well, if you give them the six months notice, then it is terminated and they have a year to pay it, so eighteen months from the day you make up your mind the thing will be over. You see, our chief answer to them would have been that they don't - I am sure they will accept six months. They have no choice but he made pretty strong representations. I didn't commit you. I said I had my doubts whether you would want to make the change.

H.M.JR: Do you object to the six?

MR. BELL: No, I don't object. I think when you make better terms in Ecuador you are going to have to change the others, which is probably not justified.

MR. WHITE: I think we have been a little bit too tough in the terms of repayment. I mean, I think in all these cases where you make a large loan to a country, unless you want to put the screws on for some political reason, that it is much better economy to allow them a longer period of payment provided they make payments as they go along. That is, not give them a long term in which to begin. I think that is true in Mexico and the Argentine. I think it is true in all of them.

MR. BELL: The chances are the six months in the other cases will not be long enough, and we will have to give them renewals or extensions.

MR. WHITE: I think that is true of Mexico and less true of Argentina.

H.M.JR: Well, what do we--

MR. WHITE: So that even if Mexico were to make another presentation next time and demand longer terms, and they are not likely to do that unless they renew the agreement, I still think they could make a good case for stretching the period of repayments.

- 7 -

H.M.JR: Now, these things run indefinitely? I mean, they have no - or do they run for two years?

MR. WHITE: Well, they have a termination date if they don't buy the dollars. The termination date would be the legal date of the existence of the stabilization fund, but if they want to get around that then at the last minute, they buy the dollars. From then on it has no termination date other than your demand for their repayment.

H.M.JR: In other words, if the thing expired and Congress directed me to terminate it, I could give them six months notice when this agreement terminates, is that right?

MR. WHITE: That is right, if you wish to.

H.M.JR: I think this is all right. Then the Central Bank of Equador "is not a signatory of this agreement and therefore does not guarantee repayment. In this respect it differs from other Stabilization Agreements.

"Dr. Salazar strongly resisted the inclusion of the Banco Central as a signatory. He felt it would weaken the position of the Ecuadorian Treasury vis-a-vis the Banco Central and raise a difficult political problem within Ecuador before the Bank's signature could be obtained."

That is going to be bad when you say we agree with them on this thing. That establishes something.

MR. WHITE: That establishes a precedent which we think is in the right direction, but it is a particularly difficult case, Ecuador, because if we demand a guarantee on her part, then she is injected right into the loan--

H.M.JR: Who is she?

MR. WHITE: The bank. I think the Government should

- 8 -

be she in this case. (Facetiously) We talked it over a good deal, and Bernstein and Viner and Southard and I, we all felt that this is a case where we oughtn't to do it, we oughtn't to push them. The lawyers say that the guarantee is just as good. You are dealing with a sovereign government, and the terms of this agreement are going to be such that the currency which we buy has to be set aside, either in a deposit account in the Central Bank or in actual currency set aside in vaults.

MR. BELL: I don't see that it makes any difference because what you are always looking to is a guarantee of the Government anyhow in these cases.

MR. WHITE: The difference is where the Central Bank comes up for the loan with the Government or where the Central Bank is owned largely by the Government. Then, we can work with them as we did with Mexico, because they are willing, but in this case it is not true.

H.M. JR: I have been for Treasury versus Treasury right along. Do you object?

MR. BELL: No, I don't object. I think it is all right.

H.M. JR: Now, where is the State Department on this?

MR. WHITE: Well, the State Department has been informed up to the minute, and as soon as you approve this draft, we will send Salazar a draft and the State Department a draft, though they have been in the discussion up to this point.

H.M. JR: Do you want to raise anything else?

MR. WHITE: No, those are the only points at issue. The draft has been sent to Bell, and we will send this to Salazar and he will communicate with his Government.

H.M. JR: You say you sent a draft to Bell?

- 9 -

MR. WHITE: Yes, this morning. They had to run off some copies.

H.M.JR: All right. That is fast enough, isn't it?

MR. BELL: O. K.

February 25, 1942

Secretary Morgenthau

Mr. White

Subject: Ecuadoran Stabilization Agreement

The Draft Stabilization Agreement we want to turn over to Dr. Salazar as soon as possible contains the following major provisions:

1. The commitment to Ecuador is \$5 million.
2. The interest charge is 1 1/2 percent per annum on the dollars drawn.
3. Repayment is required after a notice period of 180 days and is to be made in six equal instalments spread over a second period of 180 days.

Dr. Salazar made strong representations for liberalization both of the notice and repayment periods. After considerable discussion, it was decided that, if you approve, a compromise might be reached under which Ecuador would still be required to begin repayments after notice of 180 days but would be allowed to repay in 12 equal instalments spread over a period of 360 days instead of six payments over 180 days.

4. The Banco Central del Ecuador is not a signatory to this agreement and therefore does not guarantee repayment. In this respect it differs from other Stabilization Agreements.

Dr. Salazar strongly resisted the inclusion of the Banco Central as a signatory. He felt it would weaken the position of the Ecuadoran Treasury vis-a-vis the Banco Central and raise a difficult political problem within Ecuador before the Bank's signature could be obtained. We agree with him on this point.

Before giving Dr. Salazar the draft we would like your approval of point 4 and of the change proposed in point 3.

EM:meb
2/25/42

February 24, 1942

MEMORANDUM FOR THE SECRETARY'S FILES

The Secretary called in Mr. Bell and Mr. White to discuss the memorandum on the Ecuador Stabilization Agreement submitted to the Secretary by Mr. White on February 23. Mrs. Klotz was present.

1. The Secretary said that we had already agreed on No. 1 in the memorandum, referring to the sum.

2. On Item 2, the Secretary raised the question whether in the past, we hadn't preferred to state the interest at one-half percent above the Federal Reserve Bank of New York re-discount rate. White replied that we had started that way in the earlier agreements, but that owing to the objections which the Mexicans raised as to the uncertainty of the rate, it was decided to fix the rate at 1-1/2 percent, which is 1/2 percent higher than the prevailing re-discount rate, with the arrangement that the rate could be re-examined at semi-annual conferences if necessary. The Secretary asked Bell's opinion and Bell said he favored the fixed rate.

3. The Secretary asked whether the year period for repayment in the Ecuadorian Agreement wasn't better treatment than provided for in other agreements. White replied that it was, but that the special circumstances of the Ecuadorian economy made it sounder economics to provide Ecuador with a longer term of repayment. If Ecuador purchased the whole \$5 million, the sum constituted so large a portion of the total annual exchange availabilities as to warrant a year period for repurchase.

The Secretary asked whether the granting of more favorable terms to Ecuador would not cause the other countries to demand readjustment of their terms. White replied that that was quite likely; that Argentina had already indicated that she would like the terms reconsidered in the event Argentina was to renew discussions of an agreement, and it was quite likely that Mexico would want terms as liberal as Ecuador, if she found out about it, as she doubtless would. White felt, however, that we could, in general, move in the direction of being more liberal with respect to the time of repayment, so long as the monthly installments were being received. The Secretary stated that he, in general, would prefer to have "one-price" policy and make all the agreements alike as possible to meet all the terms. White expressed the view that each country presented a different situation and that it would seem to be preferable to maintain flexibility in the arrangements.

Division of Monetary
Research

- 2 -

The Secretary asked how long the arrangement was to run and White explained that it would come to an end with the cessation of the Stabilization Fund, but that prior to that date, Ecuador could offer to buy all the dollars up to \$5 million and from then on, the repurchase of the dollars would begin six months from the time the Secretary requested such repurchase. The Secretary finally agreed to the 360 days term of repayment, in addition to the 180 days notice provision, and Mr. Bell likewise approved.

4. The Secretary said that the absence of a guarantee by the Central Bank did make some difference. White said that the relationship between the Central Bank and government in Ecuador justified, in our opinion, the elimination of the Central Bank as a guarantor in the agreement. He stated that it was different where the Central Bank came up with the government to negotiate the arrangement, or where the bank was controlled by the government, or owned by the government. In this instance, it was felt that the request that the Central Bank guarantee the loan would make difficulties in Ecuador. Bell commented that, in the last analysis, we depended on the word of the government for repayment and that he felt it would be all right to have merely the government's guarantee of the repayment. The Secretary stated that he had always favored dealing with Treasuries and, therefore, he would approve the draft, even though it did not include the guarantee of the Central Bank.

It was agreed that the draft, in its present form, should be submitted to Dr. Salazar with the terms of repayment changed in accordance with the decision indicated above.

HAW

AGREEMENT made as of the _____ day of _____ 1942, at the City of Washington, District of Columbia, between the Secretary of the Treasury of the United States of America (hereinafter called the Secretary), and the Government of the Republic of Ecuador (hereinafter called Ecuador).

WHEREAS, the monetary and financial cooperation of the United States of America and the Republic of Ecuador and the stabilization of the United States dollar-Ecuadoran sucre rate of exchange are important factors in promoting trade and in fostering the welfare and friendly relationships of the two countries;

NOW, THEREFORE, in order to further such objectives and in consideration of the promises and of the mutual covenants herein contained, it is agreed as follows:

1. The Secretary, through the Federal Reserve Bank of New York as Fiscal Agent of the United States (hereinafter in its capacity as Fiscal Agent of the United States called the Federal), shall, as hereinafter provided, purchase Ecuadoran sucres from Ecuador from time to time as requested by Ecuador, the United States dollars paid therefor to be used exclusively for the purpose of stabilizing the exchange value of the Ecuadoran sucre with respect to the United States dollar. The total amount of sucres thus purchased by the Secretary, exclusive of accrued interest thereon and of any sucres repurchased, shall not at any time exceed in the aggregate the equivalent of United States \$5,000,000 computed at the rate at which such sucres are purchased as hereinafter provided. The sucres so purchased shall be deposited in the form of sucre notes in the Treasury of Ecuador in a special account to the credit of the Federal, to be opened in the name of "Federal Reserve Bank of New York as Fiscal Agent of the United States" (hereinafter referred to as Special Account T), or shall be credited to such an account in the Banco Central del Ecuador (hereinafter referred to as Special Account B). Upon receipt by the Federal Reserve Bank

+ 2 +

of New York of advice from Ecuador by telex cable that a stated amount of sucres has been deposited in or credited to Special Accounts T or B, the Federal will in turn, in payment therefor, credit Ecuador in a special account to be opened by the Federal in the name of "Government of the Republic of Ecuador, Special Account", in an amount in United States dollars equivalent, at the then prevailing buying rate of exchange in New York as determined by the Federal for cable transfers on Ecuador payable in sucres, to the amount in sucres deposited in or credited to Special Accounts T or B.

2. Ecuador shall deposit interest in Special Account T or instruct the Banco Central del Ecuador to credit interest in Special Account B on the last day of each successive month from and after the date hereof. Such interest shall be computed at the rate of $1\frac{1}{2}\%$ (one and one-half percent) per annum on the daily balance of such sucres in such Special Accounts as were purchased by the Secretary under this Agreement. The matter of the rate at which such interest shall be deposited in or credited to such Special Accounts may be reconsidered at any meeting provided for in paragraph 5 of this Agreement.

3. (a) One hundred and eighty days after the receipt of notice from the Secretary or the Federal containing such request, Ecuador shall repurchase, or cause to be repurchased (and in the case of accrued interest, purchase, or cause to be purchased), in ¹² ~~six~~ equal instalments at the end of each thirty-day period during the next succeeding ~~one hundred and eighty~~ ^{three hundred and sixty} days, in United States dollars by payments at the Federal Reserve Bank of New York:

(1) Any or all of the sucres purchased by the Secretary through the Federal at the same rate or rates of exchange at which such sucres were purchased; and

- 3 -

(11) Any or all of the sucres representing interest accrued on, and whether or not deposited in or credited to, Special Accounts T or B at the average rate of exchange at which the sucres, upon which such interest has accrued, were purchased by the Secretary through the Federal.

(b) Notwithstanding the foregoing, in the absence of such a request by the Secretary or the Federal, sucres in the amount of such accrued interest shall be purchased or caused to be purchased by Ecuador by payment in United States dollars at the Federal Reserve Bank of New York on the last day of each successive three-months' period from and after the date hereof and upon the termination of this Agreement, at the rate of exchange described in subdivision (a)(11) of paragraph 3.

(c) The aforementioned Special Accounts, the sucres deposited therein or credited thereto (including interest), and all transactions respecting such accounts, and the other obligations of Ecuador under this Agreement shall, in so far as the rights, powers, and privileges of the Secretary or the Federal may thereby be affected, be exempt and immune from any taxes, fees, charges, restrictions, and controls of any nature under the laws of Ecuador or any political subdivision or taxing authority thereof.

4. Ecuador may also at any time by making payments at the Federal Reserve Bank of New York in United States dollars at the rate of exchange provided in paragraph 3, repurchase the sucres described in paragraph 3.

5. In the event of any failure to repurchase (or, in the case of interest, purchase) the sucres as provided in paragraph 3 or of any other act, done or omitted, not in accordance with the provisions of this Agreement, Ecuador shall, if and when the Secretary, acting directly or

through the Federal, so elects by giving notice to Ecuador to such effect, become forthwith obligated to repurchase or cause to be repurchased, or in the case of interest, purchase or cause to be purchased, all of the sucres at a total purchase price in United States dollars determined as provided in paragraph 3 by payment at the Federal Reserve Bank of New York and the dollars remaining in the "Government of the Republic of Ecuador, Special Account" shall be retained by the Federal and applied by the Secretary or the Federal as a payment on account of such purchase price. No failure or delay on the part of the Secretary in exercising any of his rights, powers, or privileges, in whole or in part, under this Agreement shall constitute a waiver thereof, or of any other rights, powers, or privileges granted to the Secretary under this Agreement. It is understood that the Federal Reserve Bank of New York will act only as fiscal agent of the United States in carrying out this Agreement and in doing and performing any acts or transactions in connection with this Agreement, and that it will not incur any liability for any acts done or omitted pursuant to instructions of the Secretary. The Federal is authorized to accept and act upon any writing relating to the purchase of sucres under this Agreement or to the "Government of the Republic of Ecuador, Special Account" which is received by the Federal in the name of Ecuador and which is believed by the Federal to be genuine, and upon any cablegram, radiogram, or telegram relating to the foregoing which is received by the Federal in the name of Ecuador and which conforms to existing or future arrangements agreed upon between Ecuador and the Federal Reserve Bank of New York, or to arrangements hereafter agreed upon between Ecuador and the Federal with regard to the authentication of cablegrams, radiograms, or telegrams by the use of test numbers, and all such writings, cablegrams, radiograms, and telegrams shall be binding upon Ecuador.

- 3 -

6. In carrying out this Agreement Ecuador may act through the Banco Central del Ecuador in its capacity as Fiscal Agent of Ecuador.

7. Any notice given by the Secretary or the Federal to Ecuador or to the Banco Central del Ecuador, if acting as Fiscal Agent of Ecuador in carrying out this Agreement, shall be deemed and taken as full notice to Ecuador, and such notice may be given by the Secretary or the Federal to Ecuador at the office of the Minister of Finance of Ecuador at Quito, Ecuador, the Banco Central del Ecuador at its head office in Quito, Ecuador, or to the Ecuadoran Embassy at Washington, D. C. Ecuador hereby waives diligence, protest, notice, and demand of every kind, except as expressly provided for in this Agreement.

8. Ecuador and the Secretary agree that at periodic intervals of approximately six months from and after the date on which this Agreement becomes effective (the precise dates to be agreed upon) there shall be held a conference to be attended by the representatives of each of such parties to discuss and consider the United States dollar-Ecuadoran sucre rate of exchange, problems of mutual interest in connection therewith, and all other monetary, financial, and economic problems of mutual interest. At such consultation due consideration will be given to all relevant factors, including comparative price levels. Ecuador agrees that, without providing the Secretary with an opportunity for consultation, no substantial change in the United States dollar-Ecuadoran sucre rate of exchange will be made, and no important modification of exchange control measures will be introduced.

9. Ecuador agrees that the dollars made available under this Agreement will be used as a revolving fund for the stabilization of the exchange value of the Ecuadoran sucre with respect to the United States dollar, and that due diligence will be exercised to prevent the permanent exhaustion of the fund. In particular, Ecuador agrees to take all reasonable measures to prevent unwarranted internal currency and credit expansion such as would cause an undue drain on the dollars made available hereunder.

Ecuador further agrees to exercise or cause to be exercised such diligence in the issuance of import permits or exchange approvals as will avoid, so far as possible, any undue delay in payments for imports from the United States or in other remittances to the United States.

10. Each of the parties to this Agreement shall take and cause to be taken all the necessary measures to effectuate the purposes and intent of this Agreement and to provide each other with such information in their possession relative to foreign exchange transactions, stabilization operations and other matters of mutual interest as is relevant to the proper functioning of this Agreement.

11. Any obligation of the Secretary pursuant to this Agreement shall be conditional and dependent upon the prior performance by Ecuador of any obligations to be performed or liabilities to be discharged by them, or either of them, under this Agreement and any arrangements made pursuant thereto.

12. Any obligation of the Secretary to purchase sucres under this Agreement shall terminate on June 30, 1943, subject to earlier termination at any time thirty days after receipt by Ecuador of a written communication or cable from the Secretary or the Federal to that effect. The termination of any such obligation of the Secretary shall not affect any of the rights, powers, or privileges of the Secretary or of the Federal, or any of the duties, liabilities, or obligations of Ecuador hereunder, all of which shall continue in effect until Ecuador shall have fully performed its said duties and obligations and discharged said liabilities. If an extension of the Agreement is agreed upon, the Agreement shall continue in full force and effect during the period thus agreed upon. In the event that Ecuador wishes an extension of this Agreement, it will give the Secretary notice to that effect in writing or by cable at least thirty days prior to the termination of the Agreement.

- 7 -

13. This Agreement shall come into operation and effect as between the parties hereto when Ecuador shall file with the State Department of the United States appropriate documents satisfactorily evidencing the authority of Ecuador under the constitution, laws, statutes, decrees, and regulations of Ecuador, to enter into this Agreement, or satisfactorily evidencing ratification of the action of Ecuador in entering into this Agreement. Ecuador represents and agrees that upon the delivery of the aforementioned documents, the execution and delivery of this Agreement shall have in all respects been duly authorized or ratified, and that all acts, conditions, and legal formalities which should have been completed prior to this Agreement becoming effective shall have been completed as required by the constitution, laws, statutes, decrees, and regulations of Ecuador, and in conformity therewith.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement in duplicate.

SECRETARY OF THE TREASURY OF THE UNITED STATES

GOVERNMENT OF THE REPUBLIC OF ECUADOR

By _____

February 24, 1942
10:29 a.m.

HMJr: Hello.

Operator: Mr. MacLeish.

HMJr: Hello.

Archibald
MacLeish: Hello, Henry.

HMJr: How are you?

M: Fine, Henry.

HMJr: Archie, you seem to like to take on squabbles.....

M: (Laughs)

HMJr:and do very well on them - especially
versus Jesse Jones.

M: (Laughs)

HMJr: And I don't know whether you saw in today's paper
that the Department of Commerce got out a weekly
bulletin more or less leading up to - that all
the Government should have paid advertising.

M: No, I didn't see that.

HMJr: Well, it's in their weekly bulletin and it was
in the New York Times today. Well, of course,
that hits us particularly hard.....

M: Oh, well, it hits a lot of people.

HMJr:and I wondered if you wouldn't kind of
look into it, because you people can move as
a committee.

M: I will, indeed.

HMJr: And don't forget that Jesse owns a newspaper.

M: (Laughs) All right, Henry.

HMJr: What?

- 2 -

- M: I'm obliged to you for calling that to my attention, because the Committee on War Information has had that thing up three times. It's a very important issue for a lot of people, primarily for you, but for a lot of other people too.
- HMJr: Well, I think it's most unfortunate that Jones and the Department of Commerce have to come out that way. The Times has a whole article on it and, of course, love it. And we started with our troubles with the "Editor and Publisher". They were the first, you see. Now, we are getting a few letters from publishers saying why should they run this stuff free for us. And, on the other hand, today they had a two-page spread in the New York Times which was paid for by concerns in New York who had established a payroll deduction plan. You might like to take a look at it. It's a two-page spread in the New York Times today which is paid for. Hello.
- M: Yeah.
- HMJr: Which gives the New York Times enough money to pay them for a couple of months for what they've done for us for nothing.
- M: Yeah.
- HMJr: Well, if you'll take it on, that'll be swell.
- M: All right, Henry, we'll wade into that one.
- HMJr: Thank you.
- M: Thank you.

February 24, 1942
10:45 a.m.

Ganson
Purcell: Hello.

HMJr: Yes.

P: Good morning, Mr. Secretary.

HMJr: Good morning, Purcell.

P: I had a talk with Hopkins this morning.

HMJr: Oh, yes.

P: Briefly stated, he recognizes pretty clearly that the job with Leon would be a permanent one.

HMJr: Yeah.

P: He also recognizes that the President would not order Pike to leave the Commission.....

HMJr: Yeah.

P:and, however, he thinks it's an important job and he left me by saying that he would speak to the President about it. I told him that I'd appreciate any speed he could make on that because you were quite anxious to have the matter settled.....

HMJr: Yeah.

P:and to get Pike's services as soon as you could.

HMJr: Yeah.

P: He indicated that he would; but I feel, under the circumstances, since he said he was going to speak to the President about it, I'll pretty well have to wait until I hear from him.

HMJr: That's right.

P: But in the meantime, I'll get things all ironed

- 2 -

out so that we can put the thing through
at a moment's notice.

HMJr: Okay.

P: All right, sir.

HMJr: Thank you.

P: I'll let you know as soon as I hear.

HMJr: Please.

P: All right, sir. Good-bye.

February 24, 1942
11:18 a.m.

Eugene Sloan: Yes, sir.

HMJr: Look, Gene, these little things which take so terrifically long to settle - I mean - get my goat. Hello.

S: Yes, sir.

HMJr: Now, can't - I don't - I'm not going to wait until Harold Graves gets back, and it isn't a major thing about taking on Olin Dows.

S: Yes, sir.

HMJr: Hello.

S: Yes, sir.

HMJr: I don't know anything about an agreement, but Mrs. Morgenthau tells me she just doesn't know where the matter stands. Now I want Olin Dows taken on.

S: All right, sir.

HMJr: As Consultant.

S: All right, sir.

HMJr: So that he can go to work.

S: All right, sir.

HMJr: I'd like you to do it today.

S: All right. I'll get on it right away.

HMJr: Now, he's coming in at two.

S: Yes, sir.

HMJr: I don't know - I mean, he isn't a man that wants a lot of money or anything, you see. You can take him on a per diem basis or something like

- 2 -

that. I don't know.

S: Yes.

HMJr: But I'd like to take him on. We need him, I want him, I worked with him before, and he's an exceptionally able fellow.

S: Yes, I know.

HMJr: Now, will you take care of it?

S: Yes, sir. I'll get on it right away.

HMJr: The man's in town. Maybe you - what I'd like to have it done is before they meet at two o'clock.

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

HMJr: If you would. And let me - whatever you do tell Lieutenant Stephens and then he can tell me.

S: All right, sir.

HMJr: And it's entirely agreeable to you that we put Buffington on as my eyes on that.

S: Oh, entirely, sir. I'll be very glad; because I'd like to have you have the information direct and then you can tell us what you want.

HMJr: Well, then I think it would be helpful to you.

S: So do I. I think it would be very helpful, and I'm working with George and Ferdie right now in making up a list and the procedure and what he wants to do to find out.....

HMJr: You're working with them now.

S: Yes, sir.

HMJr: Well, clean up this Olin Dows thing if you can

- 3 -

before two.

S: I'll try to do it right away.

HMJr: And if not - he'll be over here at two - you might even drop over and fix it then.

S: All right, sir.

HMJr: If you would.

S: I will. I'll get on it right away.

HMJr: Thank you.

S: Yes, sir.

TREASURY DEPARTMENT

194

INTER OFFICE COMMUNICATION

DATE February 24, 1942.

TO Secretary Morgenthau
FROM Gene Sloan

I have just talked with Mr. Graves by telephone at Jacksonville, Florida.

He advises me that the question of appointment for Olin Dows was, by agreement with Mrs. Morgenthau, set for discussion upon Mr. Graves' return to Washington on Thursday.

February 24, 1942
11:55 a.m.

Operator: Mr. Bell.

HMJr: Dan.

Daniel
Bell: Yes.

HMJr: Are you familiar with what we're proposing to do in connection with the insurance companies - their tax-exempt income?

B: No, I'm not very much.

HMJr: Well, now, listen, we're moving awfully fast and Tarleau and Blough are here. Would you be free at twelve o'clock?

B: Yes.

HMJr: Will you?

B: Yes.

HMJr: Well, they'll move from my office into yours.

B: Uh huh.

HMJr: At twelve.

B: All right.

HMJr: I just want to make sure we're not going to do something which would adversely affect the bond market.

B: Well.....

HMJr: What?

B: It's awfully hard to.....

HMJr: Well, at least you'll know what they're proposing.

B: Yeah. I think that all of that stuff affects

- 2 -

your bond market a little.....

HMJr:

Yeah.

B:

.....at least temporarily until it gets down to a level.

HMJr:

Well, don't you think.....

B:

The same way with the banks and.....

HMJr:

Well, do you want to hear about it?

B:

Yeah.

HMJr:

Well, they'll be in there at sharp twelve.

B:

All right.

HMJr:

You're ready?

B:

Yeah, ready right now.

HMJr:

They'll be in at twelve.

B:

All right.

February 24, 1942
2:50 p.m.

HMJr: What progress are you making on cost of living?

George Haas: Well, we're working on that today.

HMJr: You are?

H: Yes, sir.

HMJr: Good. Are you contacting the various agencies?

H: Yes. I talked to Gilbert, you know, following up your suggestion.

HMJr: Yeah.

H: And he was thinking about the same thing I was, you know, that ELS study.

HMJr: Yeah.

H: It was the same thing.

HMJr: Yeah.

H: But they have somebody over there working on it, and my men are going to work with them and Daggett and Wagner are going out to Chicago, and at three o'clock - in ten minutes - I'm meeting with Sears, Roebuck and Montgomery Ward on this.

HMJr: And are you finding out what the Department of Agriculture is doing?

H: No. I've got a report from them, but I haven't checked it up yet.

HMJr: All right, because I think you'll find they do a very good job.

H: I see. I'll run that down myself, personally.

- 2 -

HMJr: Will you do that?
H: Yes, sir. You bet.
HMJr: Thank you, George.
H: Good-bye.

February 24, 1942
3:00 p.m.

TAXES

Present: Mr. Blough
Mr. Tarleau

H.M.JR: Now we will take up the next thing. What did you do with Mr. Bell? Tell me that first.

MR. BLOUGH: Well, we sat down and talked with Mr. Bell and discussed the life insurance business. It was a rather indefinite conclusion, I assume. There seemed to be a general feeling that life insurance would find it more to their advantage to own tax-exempt securities after this legislation is passed than they do now.

H.M.JR: After?

MR. BLOUGH: Since there is now no advantage to them to own tax-exempts, or practically none, the three and three fourths percent being so high that even if they had no tax-exempt interest, they would in most cases pay no tax. On the other hand, if this reduction to three and a quarter percent or thereabouts goes into effect, then the tax-exempt interest would become a matter of substantial importance to them, and they would find it more to their interest to hold than they do now. But aside from that rather general feeling on the part of those present, and Mr. Haas was there and a couple of people from his staff, there was no definite conclusion at all. Wasn't that your feeling?

MR. TARLEAU: Yes.

MR. BLOUGH: We mentioned the bank expense business. He expressed some little concern that if these gentlemen went back and talked, it might start things all over again.

H.M.JR: Well, I think we will settle it while they are here.

MR. TARLEAU: Yes. Of course he did say that. If you settle it while they are here, that would end it.

H.M.JR: I think we will settle it.

Now, what about the bank - oh, he will be there when they are here, Burgess and those, won't he?

MR. BLOUGH: He was going to get Burgess and Stonier to come down.

H.M.JR: What time is it?

MR. BLOUGH: Ten o'clock.

H.M.JR: Well, supposing we say the insurance thing is settled and go on with the next one. I mean the life insurance. We will go on with mutual casualties.

MR. BLOUGH: The mutual casualty situation, as I understand it, is largely this, that the stock casualty companies, stock fire insurance and other types of casualty insurance are now being taxed on their profits as business organizations. A substantial amount of the casualty business is being done by mutuals and many of these mutuals are now exempt under an exemption section of the statute which originally applied only to small local assessment companies, but which was extended to include a large variety of mutual companies some years ago, and even those that are not so exempt pay relatively little tax. The stock casualty people have been urging that the mutual casualty companies be subject to a tax of a similar character to them, similar amounts. In fact, they have gone so far as to urge the inclusion of premiums as part of the taxable income of the mutual casualty companies. People who have studied it for us

and in the course of discussions - they have come to this suggestion. They are now taxable on their investment income, in effect.

MR. TARLEAU: Well, you put the premiums in, but you take them out again.

MR. BLOUGH: Yes, you take them out when they are distributed to policyholders. The idea here was to take the investment income of the company and tax substantially all of it, not deducting that part of it that was paid out to policyholders.

H.M.JR: Now do it all over again.

MR. BLOUGH: The mutual casualty companies at the present time are essentially exempt from taxation because the dividends that are distributed to policyholders are deductible.

H.M.JR: Go ahead.

MR. BLOUGH: And what is proposed is that the investment income - in effect that all of the investment income be subject to tax.

H.M.JR: It isn't now?

MR. BLOUGH: That is not done now because the dividends payable to policyholders have a lot of the investment income attributable to them. I may be off a little.

MR. TARLEAU: It is a little oversimplified, but that is substantially so. Today a mutual casualty company gets, as you pointed out before, premiums and it gets income from its investments, and then during the year - that is what it gets in. During the year it gives back money to its policyholders. It has losses and other expenses.

Now, today we allow them to deduct the losses and their other expenses first against their investment income. We don't charge the losses and expenses, in effect, against

the premium income at all, so that it is somewhat similar to the bank situation in that we are trying to get some of that investment income by having some of those losses and expenses charged against premium income and leaving a base for us on the investment income against which taxes will be charged.

MR. BLOUGH: The premium income doesn't really get reached.

MR. TARLEAU: We charge these losses against them.

MR. BLOUGH: The dividends returned to policyholders are deductible.

MR. TARLEAU: That is right. So that in effect we get a tax on some investment income.

MR. BLOUGH: But not very much. It has been quite small.

H.M.JR: Well, again the concern is whether they are escaping, is that right?

MR. BLOUGH: Yes.

H.M.JR: Now we have got left here--

MR. BLOUGH: Oh, I might say this on the mutual casualties. This will not satisfy the stock companies entirely. The stock companies think we should tax everything, and we don't think that where the premium is paid in and then that premium is returned to the policyholders that that part of what goes back to the policyholders should be subject to tax. The stock companies think it should, but that doesn't seem right to us. It looks just like returning his capital to him.

H.M.JR: Well, the whole theory is, here is a group with part of their income or more than part of their income tax exempt. I have got to have confidence in somebody, and I have got confidence in you, so what the

- 5 -

hell. Let me just get this from you, one of you. If you had to write the ticket on the bank thing, how would you do it.

MR. BLOUGH: I don't know if I quite get your question.

H.M.JR: Well, on this question of taxing. I mean, allowing them what they can deduct for expenses and what they can't.

MR. BLOUGH: Mr. Secretary, from the tax point of view, without regard to any commitments that you may have been considered to have made, I certainly would make the change. Now, whether you feel that you have put yourself in the position that you can't is quite another matter, but so far as the tax policy is concerned, I think it is entirely sound to make the change that is suggested.

H.M.JR: Do you agree with him?

MR. TARLEAU: I thoroughly agree with him.

H.M.JR: Well, what did I say that makes it - what did I--

MR. BLOUGH: I don't think you said anything, Mr. Secretary.

H.M.JR: I don't either.

MR. BLOUGH: You said that you didn't want to tax that income by indirection when you couldn't do it directly, and our position is that you are not taxing it indirectly because you are not taxing it at all. The suggestion is merely to remove an exemption which has heretofore - a deduction which has heretofore been allowed against taxable income. There is no attempt being made here to tax tax-exempt income, but to simply remove a deduction which has been allowed against taxable income which was not deserved.

MR. TARLEAU: Certainly. What you said was, we

- 8 -

weren't going to take the tax-exempt income and directly or indirectly tax it. You said that covers the waterfront. I mean, by reducing the normal tax and the other way. What we are proposing to do is merely do nothing with the tax exempt income, but we are dealing with taxable income and saying, "You cannot deduct from your taxable income the expenses of your tax-exempt income." That is all that we are aiming for.

Now, Mr. Eccles feels that the term "indirection" covers this situation, and I don't think so. Roy doesn't either.

MR. BLOUGH: He thinks that indirection means that any change in the status quo, even to remove the use of the deduction, constitutes taxation by indirection. We don't feel that it does.

H.M.JR: Do you think he ought to be here tomorrow morning?

MR. TARLEAU: I should think he should be here, yes. I think you are doing the wise thing in having him in here and getting the whole thing out. He feels so keenly about it. Don't you think so?

MR. BLOUGH: Yes. We know what he will say, of course.

H.M.JR: Well, that is all right. I had better have him here.

MR. TARLEAU: He has talked so much in regard to your work and your position on the matter.

H.M.JR: Well, we will let that go.

Now, you have done nothing on the individuals, have you?

MR. BLOUGH: Except your decision, tentative or final, as the case may be, about personal exemptions, which

- 7 -

has been taken out of this. This is as you suggested. In other words, we have built up a new rate scale.

H.M.JR: Personal exemption?

MR. BLOUGH: Do you remember--

H.M.JR: Oh, yes.

MR. BLOUGH: ... lowering it. As this stands now, the personal exemptions are not reduced. We have redrawn the rate scale to raise three billion dollars without lowering personal exemptions. It is a very high rate scale, but--

H.M.JR: Now, let's look at it. What is this, increased surtax rates? Exhibits A, B, and C.

MR. BLOUGH: Exhibit A gives you the effective rate. The red line is the proposed effective rate. The other lines are recent tax rates at various levels under various laws.

H.M.JR: The red line shows where she would go.

MR. BLOUGH: The red line shows where it would go, yes.

H.M.JR: Well, it gives quite a swoop up to higher levels, doesn't it?

MR. BLOUGH: Yes, that is true. In fact, the idea was to go to a maximum of ninety percent at the top. This is pretty tough. It will be at the bottom also.

H.M.JR: Does it show how tough it is?

MR. BLOUGH: Well, A shows as much as B, but B gives you the comparative - A is the chart.

H.M.JR: And B are the figures?

MR. BLOUGH: B, now, are the figures on which - these

- 8 -

are the bracket rates themselves. Now, heretofore--

H.M.JR: On ten thousand dollars--

MR. BLOUGH: Well, Mr. Secretary, I would suggest, if you are looking at the amount of tax which a ten-thousand-dollar man would get, that you go on to the next exhibit.

H.M.JR: C?

MR. BLOUGH: Yes, that is C, married person and no dependents. Now you can look at your ten thousand dollars there.

H.M.JR: Why must I look at the other one?

MR. BLOUGH: Well, the other one has the bracket rates. It is perfectly all right to look at them, but the figures given there do not give you the total tax for a man with this much income.

H.M.JR: Present law, thirteen hundred and five.

MR. BLOUGH: That is right.

H.M.JR: Proposed, twenty-three hundred eighty-eight.

MR. BLOUGH: That is right.

H.M.JR: Increase in tax, a thousand eighty-three. What does that thirteen point one mean?

MR. BLOUGH: That is the--

H.M.JR: Effective rate. And the new rate is twenty-

four percent?

MR. BLOUGH: That is the effective rate.

H.M.JR: You mean that is what you pay?

MR. BLOUGH: That portion of your income.

H.M.JR: What do you mean, that portion of your income?

MR. BLOUGH: If you are a ten-thousand-dollar man, you pay twenty-four percent of your income in this tax.

H.M.JR: Is there any other tax?

MR. BLOUGH: This is it.

H.M.JR: You have combined them all?

MR. BLOUGH: That is right.

H.M.JR: What?

MR. BLOUGH: Yes.

H.M.JR: The Attorney General asked me last night how much the increase would be. He wondered if it would be about twenty-five percent. I told him yes. I wasn't far off, was I?

MR. TARLEAU: You were very close to it. If we can only get the Ways and Means Committee to be reconciled to twenty-five percent, that would be fine.

- 10 -

H.M.JR: I think the present law is pretty stiff as it is.

MR. BLOUGH: Yes, indeed, sir. This is not a pink tea.

H.M.JR: Well, on fifteen thousand, my salary, it goes from eighteen to thirty.

MR. BLOUGH: That is right, effective rate.

H.M.JR: It is up twelve percent.

MR. BLOUGH: Which is about two thirds.

H.M.JR: One third.

MR. TARLEAU: No, two thirds increase.

H.M.JR: But the proposal is thirty-five percent. It is right in there, it takes the biggest jumps, isn't it?

MR. BLOUGH: In terms of percentages, yes, because when you get above a hundred thousand dollars the thing begins to narrow down, because otherwise it would go out--

H.M.JR: And you are really going up to ninety percent. What happens to us poor devils that live in New York State?

MR. BLOUGH: Well, you will have about ninety-one or ninety-two.

H.M.JR: Of course, I am not in that bracket, but--

MR. BLOUGH: Well, the state tax is allowed as a deduction in computing your Federal tax, even though they don't allow your Federal tax to be deducted from the state tax. The state tax is allowed--

H.M.JR: That is what Lehman called me up about yesterday. He heard that we weren't going to allow -

- 11 -

he heard something, that you weren't going to allow - it was going to cost him money. What would that be? In making out your state tax can you deduct now for your Federal tax?

MR. TARLEAU: Yes, if you make out your Federal, you can deduct your New York tax, and he was afraid, probably, that--

MR. BLOUGH: The law was changed in New York so it didn't allow the deduction.

MR. TARLEAU: But he was afraid that if, for example, Secretary Morgenthau said, "Let's fix the Federal law so that they can not deduct their New York taxes, then New York would have to go back." Their citizens would clamor so much that they would have to go back and reduce their New York tax by the amount of the Federal tax.

H.M.JR: I see.

MR. BLOUGH: The nearest thing to discussing it was that Mr. Stam said there was some talk on the Hill of putting in a reciprocal provision to the effect that the Federal Government would allow the state tax as a deduction in computing the Federal taxes only if the state also allowed the Federal taxes to be deducted. I am personally opposed to that.

H.M.JR: But now I can deduct my state tax before I pay my Federal?

MR. BLOUGH: That is right.

H.M.JR: But in New York State, do I--

MR. BLOUGH: They recently changed the law so that you could not deduct your Federal tax in computing the state tax. There has been a lot of talk about it, and

- 12 -

I don't whether anything has been done.

H.M.JR: That is the most recent.

MR. BLOUGH: Now, that makes a percent or so difference, maybe two percent.

H.M.JR: Well, that doesn't frighten me.

MR. TARLEAU: No, it is either this bill or one six months from now.

MR. BLOUGH: I think the place where the rub is going to come worst would be down around three thousand and two thousand. It doesn't frighten me down there either, but the proportion of the increase is quite heavy at that level.

H.M.JR: I haven't looked at this. I didn't want to look at it before. I didn't want to be influenced.

MR. BLOUGH: The two thousand dollar man goes from forty-two dollars to sixty-four dollars.

H.M.JR: What do you think about giving out some of this publicity about Donald Duck paying five hundred forty-nine dollars fifty cents in England against thirteen dollars in this country.

MR. TARLEAU: I think it would be a good idea.

MR. BLOUGH: It isn't an entirely comparable situation because Donald Duck pays some other taxes here that he wouldn't pay in England.

MR. TARLEAU: There is no comparison, and those are the people who are going to be affected by the new bill.

MR. BLOUGH: That is right.

MR. TARLEAU: They are the ones who ought to be educated as to what is happening in these countries. I

- 13 -

think it would be a good idea.

MR. BLOUGH: I think I would want to check that figure. It is a little bit high.

H.M.JR: Think about it. I gave it to you, didn't I?

MR. TARLEAU: Yes.

H.M.JR: Well, that is - where are we?

MR. BLOUGH: We are on page two of the program, next page. If you will turn over three pages, you will be at the right place.

H.M.JR: Now, ten, earned income credit. What is that?

MR. BLOUGH: Well, I am not too happy about that change as suggested there, but let me tell you about it. At the present time we assume that the first three thousand dollars of every person's income is earned, whether it is or not, and we assume that nothing is to be counted as earned over fourteen thousand dollars, and then we allow a ten percent deduction - you can call it a credit - for that earned income, but not to exceed the net income. So that a person may have - if he has a ten thousand dollar salary and no deductions against it, he would be allowed a deduction of one thousand dollars earned income credit against the normal tax, which is four percent. So he would get a benefit of forty dollars which he would not get if his income came from investments instead of from his salary. Now, the way that works out is this, that a person who has sixteen hundred dollars of salary at the present time, a married couple, no dependents, would pay a surtax, but will not pay a normal tax, because his earned income credit, about a hundred and sixty dollars, will keep him from paying any normal taxes, so we have the curious situation that several million of our tax payers are going to pay surtaxes, but not normal taxes.

- 14 -

H.M.JR: I see.

MR. BLOUGH: Now, we don't like that set-up. It complicates things and a lot of other things. We are trying to find a way by which we could allow the earned income credit against both normal and surtax - hold it down and make it available more nearly to the small man and not so much to the large man, and not give too much away in money, and still get a differential, and the proposal here is that the earned income credit, a minimum of three thousand, should be eliminated entirely and that you get a five percent earned income credit against your income for normal and surtax purposes, but not on more than twenty-five hundred dollars of income. Of course, fourteen thousand dollars goes out the window there, and so on. It happens that the fourteen-thousand-dollar man will get as much earned income credit relief in taxes as he gets now, because the higher surtax rates will apply to that earned income credit. I am not too happy about it. We are still working on it. We are trying to improve it, but that is the general idea we have there. I don't think we can continue to let the present law continue. If we are going into withholding, it is an immense complication; and in any event, it is an anomaly to have people paying one and not the other. I will make up some illustrations of it for you for the next time.

H.M.JR: Will you do that?

MR. BLOUGH: Yes.

H.M.JR: I wish you would do that. I could understand it better.

MR. BLOUGH: It makes practically no difference in revenue. It won't affect the revenue result, and if you don't like it, you can eliminate it without serious results one way or the other.

H.M.JR: Now, the withholding at the source - you were going to give me some examples.

- 15 -

MR. BLOUGH: Yes.

H.M.JR: Not to exceed ten percent of salary and so forth. Now, I understand that. But is that going to be a sliding scale?

MR. TARLEAU: No, what we did say was that you didn't have to hold it at ten percent, but you could fix it anywhere from one to ten percent, but not to exceed ten percent.

H.M.JR: That is all right. How much does that produce, about a billion and a half?

MR. BLOUGH: That won't produce anything, but it will be advance collections in '42.

H.M.JR: Well, I think that that is all right. I have had that one before. Now, we go - what is the next one?

MR. BLOUGH: Corporation taxes.

H.M.JR: Well, let's skip that because we have been on that so much, and let's do the estate and gift taxes, which I haven't done. What?

MR. BLOUGH: All right.

H.M.JR: We have talked about the other so much, haven't we? What I want to try to do is to get over everything once and then go back on it if necessary.

MR. BLOUGH: Yes. We are getting near the end.

- 16 -

H.M.JR: Yes, let's talk about estate taxes. When we get through, at least we have talked about everything once.

MR. BLOUGH: Well, there are a number of things about estate and gift taxes that aren't down here, and I will leave those, but I will indicate this isn't the whole story. It is all we have to suggest at this time, but there are some other things that probably ought to be done to it.

We suggest an increase in the estate tax rates and the change in the exemptions to raise about two hundred fifty million dollars all together. That will unfortunately bring the rates in many brackets above the British rates, and we will have some difficulty, I am sure, with Congress, because they like to look at the British as a maximum and not as anything else. We do feel the estate tax rate should go up, because with a very high income tax at the present time, as Mr. Tarleau has pointed out, it is very much harder to build up a fortune than it used to be, and it seems to me just as a matter of fairness and equality, that the estates built up in the earlier days ought to pay heavier taxes now, because the incomes being received today are being more heavily taxed. At any rate, it has inherent in it all of the good and bad points, with heavy death taxation, which has been a matter of administration policy.

H.M.JR: Are there any exhibits?

MR. BLOUGH: I am not sure there is an exhibit yet in your book. There is one and I have a copy here which is the chart for "E."

- 17 -

H.M.JR: Am I looking at it?

MR. BLOUGH: It is the next one there. "F" will give you the effective rates instead of the bracket rates.

H.M.JR: Are you cutting it down from forty to ten?

MR. TARLEAU: What we plan to do, now you have forty specific exemptions and forty thousand for life insurance, which is eighty you can get all together.

Well, we are cutting out the life insurance entirely. We are combining the two into one flat exemption of sixty without any particular treatment for life insurance. Wasn't that the way you have it set up?

MR. BLOUGH: Yes. Mr. Stam seemed to be willing to go along with that. I should like to have seen it even lower.

H.M.JR: You mean the first sixty thousand--

MR. TARLEAU: Will be exempt.

H.M.JR: That your estate leaves?

MR. TARLEAU: Yes.

MR. BLOUGH: At the present time, if you left cash or securities, you would have the forty thousand and nothing more, but on the other hand you would be allowed also an additional forty thousand insurance which would bring you to eighty thousand. We have felt that there was no particular reason why insurance should be exempt any more than anything else.

H.M.JR: Are you going to sell them an insurance policy? What is the inducement?

MR. TARLEAU: That is probably what we are going to hear. We gave a flat sixty instead of the combined eighty.

MR. BLOUGH: Which means that some people will have their exemptions increased and for that reason there will be some decreases in tax, and that is where that minus five hundred dollars comes in the first line, assuming there is no insurance.

H.M.JR: That is what the estate has to pay itself?

MR. BLOUGH: Yes.

H.M.JR: You get up kind of steep, don't you.

MR. BLOUGH: We get up very steep.

H.M.JR: The President will like this. Now, this means what? You haven't got an estate with a million dollars, have you?

MR. BLOUGH: No, but I can give you - oh yes, the thousand there is a million.

H.M.JR: Where is that?

MR. BLOUGH: This is a million dollars.

H.M.JR: Well now, just run through that for me.

MR. BLOUGH: At the present time the total tax, and this is the tax before the deduction or credit allowed for the state tax - you see, New York state, for instance, has a tax and the estate is allowed to credit for that tax up to eighty percent of the tax under the 1926 act, which is pretty complicated. This is the gross before that and at the present time on that million dollar estate the tax is three hundred seven thousand two hundred dollars.

H.M.JR: Before the state tax?

MR. BLOUGH: Yes, which means it is practically the total tax he would have to pay, Federal and state. Under this proposal the total is five hundred twelve thousand five hundred fifty dollars, an increase of two hundred five thousand three hundred fifty, which means that at the present time the effective rate on the million dollar estate is thirty percent. It would be 51 percent, or an increase of about twenty points.

H.M.JR: You don't show how much the estate would give.

MR. BLOUGH: The whole business is at the bottom, two hundred fifty million. It would be a little hard to work. It is almost all in the rates because the exemptions will not effect it very much one way or the other.

H.M.JR: Now that takes care of exemptions, we talked about that, didn't we?

MR. BLOUGH: Yes.

H.M.JR: What about the gift tax?

MR. BLOUGH: We are not proposing, at this time, to make any change in the general set-up under the gift tax. The gift tax rates are three fourths of the estate tax rates, and we suggest that that ratio be continued and we would suggest, however,

some changes in the gift tax exemptions, reducing the present forty thousand dollars to thirty and then making a more important change. At the present time you can give any number of four thousand dollar gifts to different people, four thousand dollars per person to whom you give the money, without any tax being imposed. We suggest that there be a single exemption of five thousand dollars for the man who makes the gifts and if he gives more than five thousand dollars altogether that the tax shall then be imposed on anything in excess of that. Now, if he gives to only one person in the course of the year, this increases his exemption, but if he gives to a hundred, it decreases his exemption.

H.M.JR: Now, supposing a man - the way it is now a man can give to as many people as he wants up to four thousand, can't he?

MR. BLOUGH: That is right, with no gift tax.

H.M.JR: And no gift tax. And what you are proposing is that he could give up to five thousand dollars--

MR. BLOUGH: Altogether.

H.M.JR: Altogether and no gift tax.

MR. BLOUGH: Within that year.

MR. TARLEAU: He could give away five thousand dollars any year without any gift tax. On anything more he would have to pay. Today you can give away an indefinite amount, depending upon how many beneficiaries you give to. You remember Louie Blaustein created sixty-four trusts. He is dead now. He used to be president of the American Oil Company.

H.M.JR: Who did he give it to?

MR. TARLEAU: Oh, daughters and sons-in-law and things like that. Now of course, under our laws he could

only give five thousand.

H.M.JR: But as of last year he could also.

MR. TARLEAU: Yes.

H.M.JR: You people think this is fair?

MR. TARLEAU: Yes. It is all a question of agreeing whether it ought to be five thousand or six thousand or four thousand, but I think it is approximately fair, don't you?

MR. BLOUGH: As I understand, the choice of these specifications was partly determined by getting an agreement with Mr. Stam which he would be willing to support.

H.M.JR: And supposing you gave - under this suggestion you could give five thousand a year for six years?

MR. BLOUGH: No, you could give five thousand a year for as many years as you live. In addition to that, you get a thirty thousand dollar exemption which you can give as you go along. In other words, suppose the first year you gave--

MR. TARLEAU: Thirty-five thousand dollars away. You would pay no tax. The next year if you gave five thousand dollars away you would pay no tax and so on.

MR. BLOUGH: But if you paid ten thousand in the second year after having bestowed the whole thirty thousand the first year you would pay on five.

H.M.JR: I see.

MR. TARLEAU: That is right. Thirty thousand you use up once. The five thousand you can get every year.

MR. BLOUGH: Now, in addition to these there are other things that ought to be done about the estate tax. There is still the question of whether the estate and gift taxes shouldn't be coordinated or integrated into one tax. There is a question whether such things as powers of appointment and certain kinds of trusts and so on might not well be eliminated. Some of the men are working on those, but we are not in a position at this time to make any firm suggestion. Isn't that about the situation?

MR. TARLEAU: That is partly right. We have a lot of technical suggestions with respect to them that I just don't think are of sufficient dignity to put in the Secretary's statement.

MR. BLOUGH: You are quite correct, but in the matter which I mentioned, which isn't technical, but--

MR. TARLEAU: You mean of integration. That is right. That is about as far as we can go now.

MR. BLOUGH: And we thought there might be a sentence in the statement sort of holding the door open for suggestions of that kind, if it is desirable to make them in the course of the executive sessions later, if it were found that we could work some of those things out. .

H.M.JR: Now, let's take a look at the excise taxes. This is where you are going to have trouble.

MR. BLOUGH: I would like to say on the excises, before we begin, how this particular list was arrived at. We set up a committee to which O.P.A. was invited to send representatives and the Budget Bureau, the Bureau of Internal Revenue, The War Production Board, Mr. Tarleau's office and my office and Mr. Stam's office, and there may have been others, but I think that is all of them. They went over the whole list of excises.

H.M.JR: Did you have any Internal Revenue in?

MR. BLOUGH: Yes.

H.M.JR: Who was there?

MR. BLOUGH: Mr. Bogan was there.

H.M.JR: Who is he?

MR. TARLEAU: He is Captain Bliss' right hand man on the excise field.

H.M.JR: Do we still have Captain Bliss with us?

MR. TARLEAU: Yes, we still have him.

H.M.JR: Don't be so sad about it.

MR. TARLEAU: I mean, he is still there.

MR. BLOUGH: Mr. Bogan is a very able fellow.

MR. TARLEAU: Bogan is.

MR. BLOUGH: They went over the whole list.

H.M.JR: What did they say about bootlegging?

MR. BLOUGH: I wasn't there at that session, but Mr. Berkshire came up, and as I recall what he said at that meeting, it was this, that under peacetime conditions you might have a very serious bootlegging problem, but at the present time they can't get any sugar because of the rationing and he isn't particularly worried about it.

MR. TARLEAU: Bootleggers are going to be drafted and you are not going to have sugar. Those are the two points.

MR. BLOUGH: And you can't get copper for stills because of the priorities. An examination of the income stream indicates that there would probably be little, if any, falling off of actual sales at the higher prices.

H.M.JR: Well, that is what they all think. What about gasoline?

MR. BLOUGH: Well, there it is a question of gasoline being a somewhat short commodity anyway, something about which we are worrying somewhat about decreasing the consumption. It is a very good revenue producer. The states won't like this, I assume.

H.M.JR: Has everybody agreed on this? Has Stam?

MR. BLOUGH: That committee agreed, including Stam's man. Stam has not raised any objections to it. That is about all I can say. We haven't sat down - Mr. Paul has not sat down with Mr. Stam, as far as I know, and gone down the list of excises and he will probably want to do that this week. I think cigarettes is likely to be the one on which there will be the most objection. There is a change in policy involved in the cigarette recommendation. At the present time and in the past the rate has always been flat per thousand cigarettes, regardless of price. In the case of cigars there was a variation - many variations because of price. It is recommended here that the tax be different on the ten cent brands than--

H.M.JR: If you can get away with it you're wonderful, but they have got the damndest bunch of lobbyists on that.

MR. TARLEAU: You are right. There will be a big fight on that.

H.M.JR: From the ten-cent boys and the fifteen-cent boys I have heard this argument ever since I have been here. I am not going to fight about it. What about other excise taxes?

MR. BLOUGH: Those are shown in the last exhibit. In fact, the whole list there is recommended by this committee. In fact, Mr. Paul has not personally gone over and made a choice among them.

H.M.JR: "e hasn't been over it either yet?

MR. BLOUGH: He has looked at it and examined it and has raised no objections to it, but I wouldn't say that these are his choice.

H.M.JR: But this is the committee's choice?

MR. BLOUGH: Yes, roughly in the order in which they preferred them.

H.M.JR: Leased wires. Are newspapers exempted from that?

MR. BLOUGH: Yes.

H.M.JR: They raised that question. The tax on the wine is not bad. Most of it is under fourteen percent anyway.

MR. BLOUGH: The great bulk of the table wines are.

H.M.JR: About eleven or twelve percent. Sparkling wines, isn't that kind of low?

MR. BLOUGH: Well, seven cents per half-pint. That is about spirits rate.

H.M.JR: I see.

MR. BLOUGH: Considering the alcohol and all. You see, that is in--

H.M.JR: Now, now, nothing on carbonated drinks?

MR. BLOUGH: No, there is none.

H.M.JR: Oh, but proposed?

MR. BLOUGH: Oh yes.

H.M.JR: That is known as the Bell tax.

MR. BLOUGH: That is the Bell tax.

H.M.JR: If you get that you are good.

MR. BLOUGH: We found that out.

H.M.JR: Chewing gum, cigars, smoking tobacco, cigarettes. O.K., gents.

MR. TARLEAU: A cent a bottle. That is the tax.

MR. BLOUGH: This year they will take a cent a bottle where last year they wouldn't.

H.M.JR: Well, we will start in again tomorrow at ten. Let me just have one Kuhn come in here a minute.

February 24, 1942
3:33 p.m.

HMJr: Hello.
Operator: Miss Tully is with the President.
HMJr: Well, when she's free I want to talk to her.
Operator: All right.
HMJr: Please. Don't let me forget.
Operator: I won't.

February 24, 1942
4:44 p.m.

Grace
Tully: Hello, Mr. Secretary.
HMJr: How is the President feeling?
T: Well, pretty well. He's just had a press
conference. He didn't come over until the
press conference, however; he stayed at the
house all day until then. He's still coughing
a little. He doesn't feel too well.
HMJr: I'm sorry.
T: He's not up to snuff yet.
HMJr: Well, this is my schedule.
T: Yes.
HMJr: Next Tuesday, the third, I testify on the tax
bill.
T: Yes.
HMJr: And Friday of this week, Doughton and George
are coming to the office as a last go over of
our proposals.

T: Yes.

HMJr: So if the President was well enough to see me Thursday.....

T: Yeah.

HMJr:it would help me a lot.

T: All right, fine. Let me ask him if he thinks he can do it by Thursday, and I'll call you back, sir.

HMJr: Thank you.

T: Right, Mr. Secretary.

February 24, 1942

Roy Blough

Secretary Morgenthau

Over the radio I heard that Assistant Secretary of Navy Bard wrote a letter to some Congressman about asking for the exemption of contracts from state taxes. Did he clear that with either Paul or Sullivan in the Treasury? Please get a copy of his letter and let me know.

*Checked with Blough's
office 2/25/42*

Checked again 2/26/42

*3/2 - Blough has copy
of the letter and
will write memo to*

Wright -

*3/6 - Checked with Blough's
office again - has not
had time to present -*

TREASURY DEPARTMENT

Washington

FOR IMMEDIATE RELEASE,
Tuesday, February 24, 1942.

Press Service
 No. 30-46

The Secretary of the Treasury today announced the final subscription and allotment figures with respect to the current offering of 2-1/4 percent Treasury Bonds of 1952-55. Subscriptions for \$5,000 or less where the subscribers specified that delivery be made in registered bonds 90 days after the issue date were allotted in full and amounted to \$13,858,700.

Subscriptions and allotments were divided among the several Federal Reserve Districts and the Treasury as follows:

<u>Federal Reserve District</u>	<u>Total Subscriptions Received</u>	<u>Total Subscriptions Allotted</u>
Boston	\$ 421,663,350	\$ 135,224,800
New York	2,132,610,450	684,191,300
Philadelphia	306,370,700	98,824,400
Cleveland	312,431,500	100,284,750
Richmond	205,568,150	66,374,400
Atlanta	178,212,050	57,424,700
Chicago	499,427,950	161,412,650
St. Louis	130,102,400	42,910,250
Minneapolis	68,152,600	22,677,800
Kansas City	87,987,050	29,106,450
Dallas	101,830,600	32,855,300
San Francisco	251,120,850	80,655,800
Treasury	1,220,900	391,600
TOTAL	\$4,696,698,550	\$1,512,334,200

- o o o -

(137)

February 24, 1942

My dear Mr. President:

Now that our little crisis in the Government bond market seems to have passed, I thought I would tell you about it.

As you know, we offered \$1,500,000,000 in 2-1/4% 1952-55 bonds to the public on Friday, February 13th, which were oversubscribed a little more than three times. Beginning with Monday, February 16th, partly due to the bad war news and partly due to the fact that the allotment was larger than had been expected, we had to begin to support the Government bond market. This continued through Friday, February 20th, at the close of which the market appeared to be in fairly good shape.

The Federal Reserve System was most cooperative.

It is interesting to note that during this period, two sizeable private and municipal financings which had been pending were all postponed and have not yet been offered to the market. It is also interesting to note that this is the largest single cash offering which has been made since I have been in the Treasury and the first since we have been in the war.

Faithfully yours,

(SIGNED) JERRY W. EVANS JR.

The President,
The White House.

*Delivered by S. D. C. to Mr. Montgomery
12-10*



THE SECRETARY OF THE TREASURY
WASHINGTON

230

My dear Mr. President:

Now that our little crisis in the Government bond market seems to have passed, I thought I would tell you about it.

As you know, we offered \$1,500,000,000 in 2½% 1952-55 bonds to the public on Friday, February 13th, which were oversubscribed a little more than three times. Beginning with Monday, February 16th, partly due to the bad war news and partly due to the fact that the allotment was larger than had been expected, we had to begin to support the Government bond market. This continued through Friday, February 20th, at the close of which the market appeared to be in fairly good shape.

The Federal Reserve System was most cooperative ~~during~~
this whole period.

~~Practically all of the big banks took their full share.~~

~~It~~ It is interesting to note that during this period, two sizeable private and municipal financings which had been pending were all postponed and have not yet been offered to the market. It is also interesting to note that this is the largest single cash offering which has been made since I have been in the Treasury and the first since we have been in the war.

Faithfully yours,

The President,

The White House.

My dear Mr. President:

Now that our little crisis in the Government bond market seems to have passed, I thought I would tell you about it.

As you know, we offered \$1,500,000,000 in 2½ 1952-55 bonds to the public on Friday, February 13th, which were oversubscribed a little more than three times. Beginning with Monday, February 16th, partly due to the bad war news and partly due to the fact that the allotment was larger than had been expected, we had to begin to support the Government bond market. This continued through Friday, February 20th, at the close of which the market appeared to be in fairly good shape.

The Federal Reserve System was most cooperative during this whole period.

Practically all of the big banks took their full share.

It is interesting to note that during this period, two sizeable private and municipal financings which had been pending were all postponed and have not yet been offered to the market. It is also interesting to note that this is the largest single cash offering which has been made since I have been in the Treasury and the first since we have been in the war.

Faithfully yours,

The President,

The White House.

RMJr.:nmc:DWB:cc
2-23-42

SWB

My dear Mr. President:

Now that our little crisis in the Government bond market ~~has~~ ^{seems to have} passed, I thought I would tell you about it.

As you know, we offered \$1,500,000,000 in 2 1/4% 1952-55 bonds to the public on Friday, February 13th, ~~and~~ ^{which} ~~and they~~ were oversubscribed a little more than three times. Beginning with Monday, February 16th, partly due to the bad war news and partly due to the fact that the allotment was larger than had been expected, we had to begin to support the market. This continued ^{through} to Friday, February 20th, at which ^{Government bond} ~~time~~ ^{the close is} the market ^{appeared to be in fairly good shape} ~~took care of itself.~~

The Federal Reserve System was most cooperative during this whole period. ~~At no time have we worked in closer unison with them than we have recently.~~

^{Practically} All of the big banks, with the exception of the Guaranty Trust of New York, took their full share.

It is interesting to note that during this period, ~~two~~ ^{two} ~~several large~~ ^{several large} ~~private~~ ^{several large} ~~financings~~ ^{several large} ~~were all postponed and~~ ^{two} ~~have not yet been offered to the market.~~ ^{several large} ~~Therefore, it~~ ^{two} ~~is~~ ^{several large} ~~also~~ ^{two} ~~interesting to note that this is the largest,~~ ^{several large} ~~cash~~ ^{two} ~~offering which has been~~ ^{several large} ~~since I have been in the Treasury~~ ^{two} ~~and the first since we have been in the war.~~ ^{several large}

OFFICE OF
THE SECRETARY OF THE TREASURY

233

February 24, 1942

Memorandum

To: Mrs. Franklin D. Roosevelt
From: Henry Morgenthau, Jr.

I am returning herewith the letter addressed to you by Mrs. Mary Barton, which the President sent to me for reading.

234

TREASURY DEPARTMENT
OFFICE OF THE UNDER SECRETARY

To The Secretary

The President just
wanted you to see
the attached letter.

It has been summarized
on small page, or
typed if you care to
read the whole letter.

After you have
read it, Mrs. Klatz
can return it to
Mrs. Roosevelt. SWB

Under Secretary.

4/21/42, 19.

Mr. Bell:

Mrs. Mary Barton, 603 Cobban Court, S. E., Cedar Rapids, Iowa, wrote to Mrs. Roosevelt under date of January 31, 1942. She enclosed a newspaper clipping which reported a possible 15% pay roll tax on salaries above \$1,000 per annum and one reporting suggested compulsory part payment of salaries and wages in defense bonds and higher taxes. Mrs. Barton is the mother of 3 boys and 2 girls, and her husband's salary is \$1,176 a year. She details her expenses, amounting to \$1,411.23, which do not include medical care, recreation or luxuries of any kind. She is an American, obviously well-educated and very patriotic, but appeals to Mrs. Roosevelt to get the President to help families like their's before it is too late. She feels that the President does not really know what they are up against as he has never experienced anything like it. Her appeal is against withholding taxes, forced bond buying and added taxes on low salaries, and for some action against rising prices.

236

THE WHITE HOUSE
WASHINGTON

February 19, 1942.

MEMORANDUM FOR

THE SECRETARY OF THE TREASURY

I think you should read
the enclosed.

F. D. R.

Cedar Rapids, Iowa
January 31, 1942

Mrs. Franklin D. Roosevelt, Sr.
The White House,
Washington, D. C.

Dear Mrs. Roosevelt:

I realize this may never reach you, never get beyond your secretary's hands, but I am desperately hoping it will reach you! I am asking for no personal favors. I am writing to you knowing my family represents thousands of families in similar plight. And, knowing you are closest to the President's ear. He is called the great humanitarian and I think he is -- in things he understands. But I doubt he has ever lived on such small income with prices rising to endless heights, added taxes and miserably slow wage increases.

Maybe I sound sour. I don't wish to be. Every day our 1935 model radio and our newspaper tells us our diet should be this and that, that our first line of defense is our youngsters with sound teeth and health that can be produced only by consumption of certain quality and quantity of foods that are fast getting out of our reach. All we enjoy is our food, simple clothes and a roof over our heads. Tax others who have more. When you have taken everything but a fair living from everyone then if we still must do without and everyone is sacrificing equally food -- then Mrs. Roosevelt, I can take it! I would gladly eat half as much and give to my children. But I can't believe it is this bad yet.

The United States has never had a war without plenty of representation from our folks in the armed forces. There has never been a Benedict Arnold in our family tree. Our desire to help America win is as strong as our desire to live. But I will fight for my children's health and future just as quickly! Their very stomachs may be empty or nearly so if something isn't done to keep added taxes and higher living costs in line with our wages.

You are Assistant Civilian Defense Director and I firmly believe we civilians in the low income bracket surely need some defense.

- 2 -

My appeal to you comes after great deal of thought. You always seem interested in our youth.

I do not wish to sail under false colors. I have always been a Republican. Up to Dec. 7th, 1941, I have never supported President Roosevelt. After that date, Dr. Roosevelt and I were Americans, not merely a Democrat and a Republican!

My only brother is in this A.E.F. and if I were a man I would be right beside him. God gave me the harder job and worries of a mother. I say "harder" for a mother's worries are more of her children and their future. I could not give much to the Red Cross but I have offered to donate blood. I am cooperating in every way possible to help our country win - contributing in a limited way but through no wilful limitation on my part.

Again, I am asking no personal favor, except of course, that you read this history on my family economics and with the thought that there are many like us in mind, try to help us before a very harmful injustice hits us. Take fishing trips, yearly and semi-yearly vacations away from other folks before the food and clothing are cut for us again. We can't afford any kind of vacation and haven't been able to afford any kind for ten years. We've been feeding a big family while higher income folks had a good time and raised no children or one child and thought three children a large family. They are the same folks who howl that American women are dooming our civilization by refusing to bear children. When we do have five, six or more we find we have been penalized by our own government while men without families escape and have a wonderful life with luxuries, vacations from the money they didn't spend on a family!

To know privation, you must suffer it. To know sickness you must experience it. President Roosevelt's wonderful understanding of human suffering from disease was brought about by personal suffering but he has never known want. If meat, butter, eggs were a dollar a pound and dozen, he could still eat them but people like us can't eat at that price. Since he's so very busy and has had no opportunity to understand the plight of the low income peoples, I have tried to put it plainly.

Mrs. Roosevelt, I am not usually given to compliments but feel I must say this. I haven't agreed politically

- 3 -

with you but you have won my admiration and respect as a person. You are always a lady and with so many irritations today that is a real record!

Thank you sincerely for your time. Best wishes from one American to another.

Sincerely,

(Signed) Mrs. Mary Barton
603 Cobban Court, S. E.
Cedar Rapids, Iowa.

SEE PART PAYMENT OF WAGES IN BONDS

WASHINGTON (AP) — Compulsory part payment of salaries and wages in defense bonds, and even higher taxes, were foreseen Wednesday by the National Resources Planning board in an analysis of the trends of war needs and post-war policy.

The board, a federal agency, squashed any theory that a post-war depression was inevitable.

With respect to the war period, the agency in a special pamphlet released by Arthur H. Hansen, chief and economic professor and chief advisor to the Federal Reserve board, said the following conditions were indicated:

1. High corporate-income and personal income taxes.
2. Sharply increased estate taxes.
3. Broadening of individual income-tax base together with steeply graduated rates.
4. Higher and more extensive taxes on commodities competing with the war program.
5. Part payment of wages and salaries in defense bonds. And 6. Equally a shift in the composition of consumption.

Turning to the post-war era, Dr. Hansen wrote:

"We shall have, when the war is over, the technical equipment, the trained and efficient labor, and the natural resources required to produce a substantially higher real income for civilian needs than any ever achieved before in our history. Whether or not we shall, in fact, achieve that level of income will depend on our intelligence and capacity for cooperative ac-

15 Per Cent Payroll Tax Is Discussed

WASHINGTON (AP)—A 15 per cent payroll tax on all salaries above \$1,000 a year was reported under discussion in administration circles Friday as evidence developed that congressional and treasury officials thus far had failed to agree on fundamental principles of the new revenue bill.

Treasury experts, faced with the necessity of raising \$7,000,000,000 in general taxes if they are to meet President Roosevelt's request, were said to have renewed their suggestions of last year for a 15 per cent levy on payrolls, withheld at the source.

They were understood to have won some influential converts to this proposal, despite what other legislators described as mounting sentiment in congress for imposition of a retail sales tax. The house ways and means committee informally rejected the withholding tax proposal last year and a substantial number of members indicated recently they favored, instead, a sales levy.

As evidence that this trend was spreading to the senate, Senator Brown (D-Mich.) said he was convinced a majority of the members of the finance committee would choose the sales tax, if they became convinced that one of the two must be voted in order to obtain sufficient funds.

As outlined, the payroll proposal would exempt the first \$1,000 of any year's salary as necessary for living expenses, the tax being applied above that point.

THE WHITE HOUSE
WASHINGTON

For the President

This is worth reading and
sending to Henry M.

E. R.

TREASURY DEPARTMENT

243

INTER-OFFICE COMMUNICATION

DATE

Feb 24, 1942.

TO Secretary Morgenthau

FROM Mr. Foley

Re: Robert E. McConnell

The Bureau of Internal Revenue has approved a refund amounting to \$156,190.25 of income taxes to Robert E. McConnell for the years 1933, 1934 and 1935. The refund arises as a result of McConnell's payment to the Commissioner of about \$220,000, which was the amount of the increased tax liability asserted by the Bureau against McConnell. In addition, to this amount a 50 percent fraud penalty had been claimed. However, since there was no foundation to the fraud charge, this penalty was completely abandoned by the Bureau.

The increased tax liability arose chiefly as the result of the creation by McConnell of a management corporation of which he was originally the sole stockholder. The management corporation handled the portfolio of Mayflower Associates, an investment trust. These management services had previously been performed by McConnell himself. Since he continued to perform the same investment advisory services as he had before the management corporation was organized, the Bureau included in McConnell's individual income as well as in management corporation's income the amount paid by Mayflower Associates.

The device used by McConnell was commonly employed in the 1930s and there was no basis for the fraud penalty. The Bureau in sending out the notices of deficiency did not allege fraud, but the attorney handling the case, in preparing his answer to McConnell's petition to the Board of Tax Appeals, alleged fraud, without the prior approval of the responsible officials of the Bureau.

E. W. Fh

ENGINEERS' DEFENSE BOARD

STATEMENT of PURPOSES and
PLAN of ORGANIZATIONPurpose:

In view of the existing national emergency, six national engineering societies have joined to organize the Engineers' Defense Board in order to provide a central agency that will be prepared to assist the various branches of the Government with engineering knowledge and experience connected with military preparedness. Among the functions of this organization will be:

- (1) To serve as a channel to inform engineers generally regarding defense problems, especially those involving shortages of materials;
- (2) To implement and make applicable reports and recommendations of the advisory committees of the National Academy of Sciences;
- (3) To urge engineers (a) to adopt procedures looking toward accomplishment of the objectives of defense agencies; (b) to promote means of increasing production of raw materials in which shortages exist; (c) to conserve the supply of industrial materials; (d) to find substitutes; and (e) to simplify operations and production.
- (4) To act as a clearing house between engineers or engineering groups of information regarding substitute materials, waste prevention and conservation.
- (5) To appoint, on request of the Army, Navy or other defense agency, special committees of engineers to deal with specific engineering problems related to defense.
- (6) To select problems or projects dealing with defense and to study them with due regard to activities of existing agencies.

Organization:

For the purpose of organization, the Engineers' Defense Board shall consist initially of five representatives from each of the following

six national engineering societies (American Society of Civil Engineers, American Institute of Mining and Metallurgical Engineers, American Society of Mechanical Engineers, American Institute of Electrical Engineers, Society of Automotive Engineers, and American Institute of Chemical Engineers) such representatives to be appointed by the governing bodies of such societies. To these may be added one or more representatives of such other national engineering societies as may be invited to participate by the Executive Committee of the Engineers' Defense Board, such representatives to be designated by the governing body of their respective society; and such additional representatives of the six "organizing" societies as may be requested by the Executive Committee of the Engineers' Defense Board.

The activities of the Engineers' Defense Board shall be administered by an Executive Committee consisting of (a) a Chairman, a Vice Chairman and a Secretary, elected by the other members of the Executive Committee and (b) one representative of each of the six societies heretofore named, appointed by the governing body of their respective societies. The officers need not be representatives of any of the participating societies.

The duties of the Executive Committee shall include:

1. To name all standing and special committees, the chairman of which shall be selected from the membership of the Board.
2. To consider reports from special and standing committees and to have exclusive authority to issue reports in the name of the Board.
3. To arrange for appropriate publicity for the work of the Board and its committees.
4. To exercise the full authority of the Board between meetings of the Board.

Meetings:

The Board shall hold an annual meeting during the month of January in each year, at which officers will be elected. Additional meetings of the Board will be held from time to time at the call of the Executive Committee for the purpose of considering reports and transacting other business.

Term of Office:

The officers shall serve for one year but there is no limitation on the number of successive terms any officer may serve.

ENGINEERS' DEFENSE BOARD
 REPRESENTATIVES OF CONSTITUENT BODIES

R. E. McCONNELL, CHAIRMAN : 20 Exchange Place, New York, N. Y.
HARRY S. ROGERS, Vice-Chairman: Pres., Brooklyn Polytechnic Institute.
A. B. PARSONS, Secretary : Secretary, American Institute of
 Mining and Metallurgical Engineers,
 29 West 39th Street, New York, N.Y.

(1) AMERICAN SOCIETY OF CIVIL ENGINEERS

CARLTON S. PROCTOR (EC) : Cons. Engr., 420 Lexington Ave.,
 New York City
 Richard E. Dougherty : Vice Pres., Improvements and
 Developments, New York Central
 System, 230 Park Ave., New York City
 Charles F. Goodrich : Chief Engr., American Bridge Co.,
 Frick Building, Pittsburgh, Penn.
 Robert R. McMath : Chmn Bd., Motors Metal Mfg. Co.,
 5936 Milford Ave., Detroit, Mich.
 J. P. H. Perry : Vice Pres., Turner Construction Co.,
 420 Lexington Ave., New York City

(2) AMERICAN INSTITUTE OF MINING AND METALLURGICAL ENGINEERS

JOHN F. THOMPSON (EC) : Exec. Vice Pres., International Nickel
 Co., 67 Wall Street, New York City
 Zey Jeffries : Tech. Dir., Lamp Dept., General
 Electric Co., Nela Park, Cleveland,
 Ohio
 Wilber Judson : Vice Pres., Texas Gulf Sulphur Co.,
 75 East 45th Street, New York City
 Frederick Laist : Met. Mgr., Anaconda Copper Mining Co.,
 25 Broadway, New York City
 Wilfred Sykes : Pres., Inland Steel Co.,
 38 Dearborn St., Chicago, Ill.

(3) AMERICAN SOCIETY OF MECHANICAL ENGINEERS

R. M. GATES (EC) : Pres., Air Preheater Co.,
 60 East 42nd Street, New York City
 H. V. Coes : Indus. Dept., Ford, Bacon & Davis, Inc.
 39 Broadway, New York City

AMERICAN SOCIETY OF MECHANICAL ENGINEERS, (Continued.)

- K. H. Condit : Dean of Engineering, Princeton University, Princeton, New Jersey
- J. W. Parker : Vice Pres. and Chief Engr., Detroit Edison Co., 2000 Second Ave., Detroit, Michigan
- W. R. Webster : Chmn. of Board, Bridgeport Brass Co., Bridgeport, Connecticut.

(4) AMERICAN INSTITUTE OF ELECTRICAL ENGINEERS

- H. H. BARNES, JR. (EC) : Commercial Vice Pres., General Electric Co., 570 Lexington Ave., N.Y.C.
- C. A. Adams : Cons. Engr., E. G. Budd Mfg. Co., Philadelphia, Pennsylvania
- C. B. Jolliffe : Engr. in Charge, Frequency Bur., Radio Corp'n of America, 30 Rockefeller Plaza, New York City
- R. L. Jones : Dir. of Apparatus Dev., Bell Telephone Labs., 463 West St., N. Y. C.
- Philip Sporn : Vice Pres. in Charge of Engrg., American Gas & Electric Service Corp'n, 30 Church St., New York City

(5) SOCIETY OF AUTOMOTIVE ENGINEERS

- C. L. McCUEN (EC) : Vice Pres. and Chief Engr., General Motors Corp'n, General Motors Bldg., Detroit, Michigan
- Frank W. Caldwell : Dir. of Res., United Aircraft Corp'n East Hartford, Connecticut
- E. E. Frudden : Allis Chalmers Co., Milwaukee, Wisc.
- Arthur Nutt : Vice Pres., Wright Aeronautical Corp'n, Patterson, New Jersey
- N. G. Shidle : Editor, S.A.E. Journal, 29 West 39th Street, New York City
- James C. Zeder : Chief Engr., Chrysler Corp'n, Detroit, Michigan

(6) AMERICAN INSTITUTE OF CHEMICAL ENGINEERS

- F. W. WILLARD (EC) : Pres., Nassau Smelt. & Refin. Co., 170 Fulton St., New York City
- Webster Jones : Carnegie Inst. of Tech., Pittsburgh, Pennsylvania
- R. L. Murray : Vice Pres., Hooker Electrochemical Co., Niagara Falls, New York
- A. J. Weith : Mgr. of Research, Bakelite Corp'n, 230 Grove St., Bloomfield, N. J.
- R. E. Wilson : Pres., Pan American Petroleum & Transport Co., 122 East 42nd St., New York City.

February 24, 1942

Eugene Sloan
Secretary Morgenthau

Please write a letter for me congratulating Dick Patterson and his organization on the two-page ad in today's New York Times. I am delighted with it.

Letter in 1/24/42

Daily changes in the stock of Series E savings bonds on hand ^{1/}

(In thousands of pieces)

	: Number of : pieces sold : this day	: Number of pieces : manufactured : this day	: Stock on hand : at close of : day	: IBM : deliveries : this day
Feb. 10	193	705	17,712	2,000
11	159	695	18,248	-
12	220	640	18,668	-
13	144	370	18,894	-
14	87	none-closed	18,807	-
15	none-closed	none-closed	18,807	-
16	363	535	18,979	2,500
17	89	800	19,690	1,000
18	218	800	20,272	1,000
19	160	800	20,912	1,000
20	193	800	21,519	1,000
21	200	none-closed	21,319	-
22	none-closed	none-closed	21,319	-
23	214	800	21,905	-

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

February 24, 1942

^{1/} Includes stock in hands of (1) Federal Reserve Banks and branches, (2) Post offices, (3) Federal Reserve Bank issuing agents, and (4) Treasury vaults in Washington.

UNITED STATES SAVINGS BONDS
 Comparative Statement of Sales During
 First Fifteen Business Days of February and January 1942 and December 1941
 (February 1-23, January 1-22, December 1-22)
 On Basis of Issue Price

(Amounts in thousands of dollars)

Item	Sales		Amount of Increase or Decrease (-)		Percentage of Increase or Decrease (-)	
	February 1942	January 1942	February 1942	January 1942	February 1942	January 1942
Series M - Post Offices	\$ 74,939	\$ 117,665	\$ 42,926	\$ 52,665	- 36.4%	- 36.4%
Series M - Banks	269,925	349,287	79,362	239,531	- 22.1	- 22.1
Series M - Total	344,863	467,153	122,290	272,198	- 26.2	- 26.2
Series F - Banks	43,917	52,152	8,235	33,364	- 15.8	- 15.8
Series G - Banks	208,842	201,661	100,367	107,300	0.6	0.6
Total	\$597,622	\$726,971	\$129,349	\$412,861	- 17.6%	- 17.6%

Office of the Secretary of the Treasury, Division of Research and Statistics, February 24, 1942.

Source: All figures are deposits with the Treasurer of the United States on account of proceeds of sales of United States savings bonds.
 Note: Figures have been rounded to nearest thousand and will not necessarily add to totals.

UNITED STATES SAVINGS BONDS
 Daily Sales - February 1942
 On Basis of Issue Price
 (In thousands of dollars)

Date	Post Office Bond Sales			Bank Bond Sales			All Bond Sales		
	Series H	Series K	Series Y	Series G	Total	Series H	Series Z	Series Q	Total
2	\$ 8,435	\$ 34,150	\$ 6,191	\$ 19,795	\$ 60,136	\$ 42,585	\$ 6,191	\$ 19,795	\$ 68,571
3	3,572	1,887	2,793	19,518	30,199	11,459	2,793	19,518	33,770
4	4,893	16,337	3,937	18,515	38,989	21,430	3,937	18,515	43,882
5	4,297	16,149	2,367	14,640	33,156	20,406	2,367	14,640	37,413
6	4,310	23,510	3,829	18,620	45,958	27,820	3,829	18,620	50,269
7	3,023	10,039	2,019	6,174	18,233	13,062	2,019	6,174	21,256
8	5,486	25,354	3,071	16,265	44,690	30,839	3,071	16,265	50,176
9	3,902	11,794	1,109	12,679	25,581	15,695	1,109	12,679	29,483
10	3,279	9,782	1,487	7,637	18,906	13,061	1,487	7,637	22,185
11	3,293	14,670	1,584	7,781	24,035	17,963	1,584	7,781	27,328
12	2,710	9,026	1,047	4,385	14,458	11,736	1,047	4,385	17,168
13	1,714	5,740	113	1,152	7,005	7,454	113	1,152	8,719
14	5,741	22,405	3,212	13,748	39,365	28,147	3,212	13,748	45,107
15	2,639	4,285	690	3,211	8,187	6,924	690	3,211	10,826
16	2,992	13,911	1,715	14,118	29,745	16,903	1,715	14,118	28,737
17	2,992	13,911	1,715	14,118	29,745	16,903	1,715	14,118	28,737
18	2,992	13,911	1,715	14,118	29,745	16,903	1,715	14,118	28,737
19	3,147	9,167	1,401	9,401	19,969	12,313	1,401	9,401	23,115
20	3,231	11,769	1,455	6,138	19,362	14,999	1,455	6,138	22,592
21	3,687	11,733	3,193	7,284	22,502	15,560	3,193	7,284	26,035
22	4,490	12,015	2,703	1,784	22,502	16,504	2,703	1,784	26,991
Total	\$ 74,939	\$ 269,925	\$ 43,917	\$ 208,842	\$ 522,683	\$ 344,863	\$ 43,917	\$ 208,842	\$ 597,622

Office of the Secretary of the Treasury, Division of Research and Statistics.
 February 24, 1942.

All figures are deposits with the Treasurer of the United States on account of proceeds of sales of United States savings bonds.
 Notes: Figures have been rounded to nearest thousand and will not necessarily add to totals.

February 24, 1942.

Dear Mr. Stone:

I appreciated your writing me as you did under date of February 10th, but was sorry to hear that you felt you could not join us in Washington.

I know that you gave the matter a great deal of thought, and that your decision was a well considered one. I can only express my disappointment, therefore, and my thanks for your offer of service or assistance if at any time I may call upon you.

With cordial regards,

Sincerely,

(Signed) H. Wergenthau, JR.

File N.M.C.

Mr. Lauson H. Stone,
150 Broadway,
New York, New York.

GEF/dbs

120
150 BROADWAY
NEW YORK

February 10, 1942

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

My dear Mr. Secretary -

I had very much hoped to find an opportunity to talk over with you further the possibility of my coming down to Washington to do work along the lines of our recent discussion. My plans to be in Washington this past weekend went awry, and affairs

here will prevent my coming down for at least another week. Not wishing to delay my decision any further, I have been giving the matter considerable thought, and, after some hesitation, have come to feel that the best course is to remain here.

I shall not attempt to list the many considerations which have led me to this conclusion; suffice it to say that

that is my decision, at least for the present. Although the urge to participate more directly in the war effort may yield a different result in the long run.

I hope that my delay in so advising you has not been the source of any inconvenience.

Please allow me to express my appreciation of your having taken the time

to talk things over with me,
and also to thank you for your
most generous consideration.
If ever I can in any way
be of service or assistance
to you, I trust you will
call upon me.

With sincere regards,

Am

Respectfully yours

9:35

1942 FEB 12 AM 8 35

Laurel Stone

OFFICE
SECRETARY OF TREASURY

February 24, 1942.

Dear Frank:

Thank you for your letter of February 18th.

I am sending you a copy of my reply to Frank Freeman, and I too would like to discuss this with you when you are available. I shall look forward to seeing you at a time that is mutually convenient.

Sincerely,

(Signed) Henry

Honorable Frank C. Walker,
The Postmaster General,
Post Office Department,
Washington, D. C.

Enclosure. ✓

File N.M.C.

GEF/dbs

THE POSTMASTER GENERAL

February 18, 1942.

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

Dear Henry:

Your note of February 12, with the copy of Frank Freeman's letter, has been forwarded to me here in Chicago. Copy of your reply was not enclosed, but I was very much interested in Freeman's concern and I would like to talk to you about it when I return.

Best wishes to you. I will see you soon.

Sincerely yours,



FCW/cc

P.S. Mrs. Walker and I received word of your thoughtful invitation to your Dinner last week. We are both so sorry we could not be present and we appreciate your thoughtfulness and that of Mrs. Morgenthau, very much.

February 24, 1942

Mr. Swope

Secretary Morgenthau

Over the week-end I had several contacts with Clif Mack about our placing all of the orders for Russia under Lend-Lease, and getting them delivered before the first of April. There still remains a lot to be done, and I would appreciate it if you would more or less concentrate your efforts on this subject until we feel that we will be able to deliver this goods before April 1st. I would like you to keep me informed at frequent intervals.



TREASURY DEPARTMENT

PROCUREMENT DIVISION

WASHINGTON

OFFICE OF THE DIRECTOR

FEBRUARY 24, 1942

MEMORANDUM TO THE SECRETARY:

Reference is made to my scheduled report dated February 18th relative to the status of the Russian Purchasing Program, which report listed fifteen indicated deficiencies which could not be made up by April 1st unless further allocations were made by W. P. E. or higher priority granted.

I can now report that, due to further allocations by W. P. E., seven of the indicated deficiencies, specifically, Aluminum, Ferro Silicon, Ferro Chromium, Nichrome Wire, Cold Rolled Steel Sheets, Steel Rails and Steel Plates, will be current by April 1st. The Steel Rails and Plates are Non-Protocol items and the deficiency as to Steel Rails was made up by W. P. E. taking 10,000 tons from British production for the Russian requirements.

The remaining eight deficiencies as listed below are under active consideration by W. P. E. and you will be promptly advised of any further developments.

Tool Steel - Requisition received W. P. E. February 16th, in process of allocation, subject to clarification of specifications by Russians.

Steel Wire - W. P. E. endeavoring obtain revision specifications to enable production account inability suppliers to meet delivery specified in allocation orders.

Shell Steel - Revision present allocation and further allocation on requisition received by W. P. E. on February 16th required.

Steel Alloy Tubes - Requisition received by W. P. E.

FOR DEFENSE



February 2nd. Now in process of allocation.

Cold Rolled Steel Strips. Requisition received by W. P. B. February 16th. Now in process of allocation.

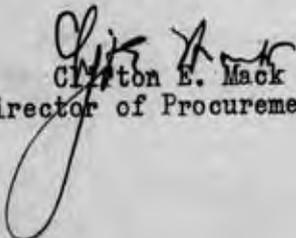
Stainless Steel Wire. Requisitions received January 28th and 31st for five tons each. Now in process of allocation; likewise, clarification of specifications required from Russians.

Hot Rolled Steel. Requisition received by W. P. B. February 11th. Now in process of allocation.

Marine Cable. Suppliers claim that AA priority is required to meet delivery schedules is now under consideration.

As specified in my status report of February 18th, the Russians have not submitted requisitions for the total Protocol requirements to April 1st in several instances, and it will be noted particularly that the existing deficiencies listed above are primarily due to the receipt of Russian requisitions only recently for requirements from October 1, 1941; likewise, the need for clarification of specifications by the Russians.

Every effort will be made, however, and I will advise you immediately of any further developments.


Clayton E. Mack
Director of Procurement

February 24, 1942

My dear Ed:

I am sending you herewith a further progress report from Clifton E. Mack, dated February 24.

It is unfortunate that so many of the requisitions for the Russian purchasing program have been so slow in reaching us. You will note that in the case of Tool Steel and Cold Rolled Steel Strips, requisitions were only received by W.P.B. on February 18th. This gives us very little time in which to turn around.

I would like to ask you to find out why these particular requisitions have been delayed so long.

We will continue to do everything we can, despite the difficulties outside of our control, to fulfill these requirements on or before April 1.

Yours sincerely,

(Signed) HENRY

Mr. E. R. Stettinius, Jr.,
Lend-Lease Administrator,
515 22nd Street,
Washington, D. C.

Copy to:

Mr. Swope
Mr. Mack



TREASURY DEPARTMENT

PROCUREMENT DIVISION

WASHINGTON

OFFICE OF THE DIRECTOR

FEBRUARY 24, 1942

MEMORANDUM TO THE SECRETARY:

Reference is made to my scheduled report dated February 18th relative to the status of the Russian Purchasing Program, which report listed fifteen indicated deficiencies which could not be made up by April 1st unless further allocations were made by W. P. B. or higher priority granted.

I can now report that, due to further allocations by W. P. B., seven of the indicated deficiencies, specifically, Aluminum, Ferro Silicon, Ferro Chromium, Nichrome Wire, Cold Rolled Steel Sheets, Steel Rails and Steel Plates, will be current by April 1st. The Steel Rails and Plates are Non-Protocol items and the deficiency as to Steel Rails was made up by W. P. B. taking 10,000 tons from British production for the Russian requirements.

The remaining eight deficiencies as listed below are under active consideration by W. P. B. and you will be promptly advised of any further developments.

Tool Steel - Requisition received W. P. B. February 16th, in process of allocation, subject to clarification of specifications by Russians.

Steel Wire - W. P. B. endeavoring obtain revision specifications to enable production account inability suppliers to meet delivery specified in allocation orders.

Shell Steel - Revision present allocation and further allocation on requisition received by W. P. B. on February 16th required.

Steel Alloy Tubes - Requisition received by W. P. B.

DEFENSE

BUY
UNITED
STATES
SAVINGS
BONDS
STAMPS

February 2nd. Now in process of allocation.

Cold Rolled Steel Strips. Requisition received by W. P. B. February 16th. Now in process of allocation.

Stainless Steel Wire. Requisitions received January 28th and 31st for five tons each. Now in process of allocation; likewise, clarification of specifications required from Russians.

Hot Rolled Steel. Requisition received by W. P. B. February 11th. Now in process of allocation.

Marine Cable. Suppliers claim that AA priority is required to meet delivery schedules is now under consideration.

As specified in my status report of February 18th, the Russians have not submitted requisitions for the total Protocol requirements to April 1st in several instances, and it will be noted particularly that the existing deficiencies listed above are primarily due to the receipt of Russian requisitions only recently for requirements from October 1, 1941; likewise, the need for clarification of specifications by the Russians.

Every effort will be made, however, and I will advise you immediately of any further developments.


Clayton E. Mack
Director of Procurement

OFFICE OF LEND-LEASE ADMINISTRATION
FIVE-FIFTEEN 22d STREET NW.
WASHINGTON, D. C.

copy to Mr. Roosevelt
Mr. Mack
2/24/42
264

E. R. Stettinius, Jr.
Administrator

February 24, 1942

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

Dear Henry,

Thank you for your letter of February 21 with enclosures. I appreciate your splendid cooperation in connection with our attempts to expedite the Russian program.

When Mr. Mack gives you the status report in connection with the work his people are doing with Mr. Bett's organization, I would greatly appreciate it if you would send me a copy.

With best wishes,

Sincerely yours,



E. R. Stettinius, Jr.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE FEB 24 1942

TO Secretary Morgenthau
FROM Messrs. Foley and White

1. We in the Treasury believe that effective administration of economic warfare in the Latin American countries, particularly as it relates to Foreign Funds Control and the Proclaimed List cannot be attained without a far greater degree of cooperation and "advice" from the United States than now exists.

2. To provide for that increased effectiveness, we believe a plan which is briefly outlined on page 2 of the appended memorandum, should receive careful consideration by the Board of Economic Warfare. A preliminary sounding-out at the State Department indicates an unsympathetic attitude to the proposal, apparently based on the fear that Treasury and the Board of Economic Warfare would be moving in on a field that the State Department wishes to keep exclusively under its own jurisdiction, even though it were to mean a much less efficient administration.

3. We should like your permission to submit the appended memorandum to Milo Perkins for possible consideration by the Board of Economic Warfare. We will, at the same time, send copies to the State Department.

APPROVED:


Secretary of the Treasury

H.W.
E.W.F.

February 23, 1942.

PROCEDURE FOR CARRYING OUT AN ACTIVE PROGRAM OF ECONOMIC
WARFARE IN LATIN AMERICA

Up until the outbreak of war our program of economic warfare in Latin America depended to considerable extent upon the effectiveness of our Proclaimed List program. Since the outbreak of war, however, the Latin American Republics have adopted local freezing controls of their own affecting the activities of the Axis countries and persons acting for the Axis countries. It is emphasized that it will only be through the wholehearted cooperation of the Latin American countries, in adopting and effectively administering real local controls, that we will be able to accomplish what we have been attempting so far as possible to accomplish through our Proclaimed List program.

The resolution adopted at the Rio Conference by the American Republics, with respect to the severance of commercial and financial relations between the American Republics and the Axis countries and persons acting for the Axis, sets forth the skeleton of a program which, if really put into effect by the Latin American Republics, will be one of the most important steps which these countries can take in connection with the economic war effort.

A number of these countries have adopted decrees which, on their face, purport to carry out, in part at least, the program outlined in such resolution. In most cases, however, the decrees which have been enacted do not, even on the surface, completely cover all of the points contained in such resolution. And, what is more important, in no case do we have sufficient information to enable us to ascertain how these decrees are really being administered.

In order to get the wholehearted cooperation of the Latin American countries, it is absolutely essential that we give these countries as much assistance as possible in setting up a real program of economic warfare. In this connection, it is noted that a number of these countries have already formally or informally requested our assistance. To date we have done little in giving real assistance to these countries in setting up such a program. This has been due, in large measure, to the fact that we do not have sufficient information concerning local conditions; the decrees that have been put into effect; how they are being administered; the ability of the local governments to administer them effectively; and the problems peculiar to the various countries which will arise in connection with such a program. Furthermore, even if we had such information in the form of memoranda from the missions, it is doubtful that we could effectively advise a Latin American government of the solution to its problems by sending memoranda back and forth. In this connection, it might be noted that recently the Peruvian Government has transmitted a memorandum of some six pages raising specific questions in connection with the freezing control; and while this memorandum has been carefully studied and answers prepared, it seems unlikely that the Peruvians, without the close and continued assistance of someone having a thorough knowledge of freezing control problems, will be able to work the information given into an effective freezing control.

What is needed immediately is to have men on the spot in these countries who will be able to obtain the information needed, to see what is going on, to render such technical and other assistance to these countries as may be needed, and, what is more important, to spur these countries on and affirmatively furnish them with real ideas as to what to do.

These men should not only have a knowledge of The Proclaimed List problems, but should also be thoroughly familiar with the problems of our own freezing control so that they will be able to pass on to these Latin American countries the benefit of our twenty-some months experience in this field.

It is suggested that a program be adopted, looking toward immediately sending such men to all the important Latin American countries, and possibly to each and every Latin American country, to be on the spot and, working through the State Department missions, to give such assistance to these countries as may be needed.

Accordingly, the following tentative proposal is suggested:

1. A Central Committee will be set up composed of one representative, respectively, of the State Department, the Treasury Department, and the Board of Economic Warfare. The Committee will have its offices in the State Department. It will be charged with the responsibility of working on

(a) All problems relating to The Proclaimed List.

(b) All problems arising in connection with the freezing control measures adopted or to be adopted by the various Latin American countries, including the furnishing of such assistance to these countries, through the American missions, as may be needed. This will also include the formulation of a program for integrating Latin American controls with our own freezing control.

(c) Other problems connected with the program of economic warfare, such as priorities, shipping, preclusive buying, etc.

These representatives will have authority from their respective departments to pass finally on questions falling within the scope of the Committee's functions, subject to the clearance of important policy decisions.

2. Each representative will have a number of assistants assigned to him from his department, starting out with approximately ten men from each department. These assistants will work on such problems as may be assigned to them by the Committee. Such of these assistants as do not have a thorough knowledge of Proclaimed List problems, freezing control problems as a whole, and other problems in connection with economic warfare, will be given a thorough training by the Committee and through "training schools" which may be conducted by the various departments. As soon as possible, many of these assistants will be assigned by the Committee to work in the field in the various Latin American Republics. A number of them could be stationed in the missions in these countries, while others could periodically make circuit trips through these countries, consulting with the missions and with the assistants who are stationed there, passing on the latest developments in Washington, and receiving a full report of the developments in the countries visited. These roving missions will serve as a liaison group between the Central Committee and the missions and the men stationed in the field.

Treasury Department 268
Division of Monetary Research

Date February 25 19 42

To: Miss Chauncey

The Secretary should see this.

H.D.W.

MR. WHITE
Branch 2058 - Room 214½

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE February 24, 1942

TO Secretary Morgenthau
FROM Mr. White
Subject: The Census of Foreign-Owned Property

A. The Treasury's census of foreign-owned property is now nearing completion. The total number of reports on TFR-300 received by the Treasury is 565,000 with a few thousand still in the Federal Reserve Banks. Approximately 35,000 reports were lost when Manila was captured. Additional reports are being collected currently on property held in this country for nationals of the Philippine Islands, and on the property of all Japanese nationals in the United States.

These reports are being carefully edited to eliminate double counting and errors, and to detect evasions. More than 450,000 reports have already been edited. The information on the reports is punched on cards to make the data available for mechanical tabulation. We have 160 people working on the census, only six of whom are professional economists.

The entire process of editing and recording the census will be completed in about three weeks. We shall then have a complete account of all foreign-owned property in the United States by name of owner, type of property, location of property, and other pertinent information. The fullness of our present knowledge of such property contrasts very favorably with our meager knowledge during the last war.

B. Preliminary compilations on the reports indicate the following interesting items:

1. The total of all foreign-owned assets in the United States exceeds \$11 billion.

2. British-owned assets in the United States, not counting securities sold before June 1941, will probably exceed \$2.5 billion. This is \$500 million more than previous estimates.

3. Total property of blocked nationals, other than corporations, residing in the United States amounts to \$600 million.

- 2 -

4. Many blocked nationals are hoarding large sums in currency. The largest currency hoard appears to be \$793,000 held by Samson Hanauer. Henry Bernstein--French playwright--holds \$126,000 in currency.

5. Many companies thought to be American have been revealed as foreign owned.

C. While the census is being compiled, we are making use of the reports steadily for various purposes:

1. A list of material and equipment exceeding \$700 million in value held for nationals was submitted by you to Vice President Wallace. Foreign Funds Control is co-operating with BEW and WPB to make these goods available for our war effort.

2. A list of nationals with patent-pooling or profit-sharing agreements in this country is being prepared for use by the Treasury and the Department of Justice.

3. A list of companies apparently evading freezing regulations is being prepared and the companies are being investigated by Foreign Funds Control. A similar list of individuals will also be prepared.

4. A list of individuals and companies whose assets have shown material change between June 1, 1940 and June 14, 1941 has been compiled, and they are actively being investigated by Foreign Funds Control to determine whether there is a cloaking of foreign-owned property.

5. A list of individuals and companies, citizens of the United Kingdom and located in the United Kingdom, together with their property holdings, has been prepared to aid the British Government in requisitioning the dollar assets of its nationals.

6. Studies of the census reports have been used by Foreign Funds Control as a basis for amending General License 42 applying to blocked nationals resident in this country.

D. The Treasury's census of foreign-owned property is the most thorough and comprehensive undertaken in this country, and it is not unreasonable to state that it will prove to be extremely useful to a number of agencies of the Government.

TREASURY DEPARTMENT

271

INTER OFFICE COMMUNICATION

DATE February 24, 1942

TO Secretary Morgenthau
FROM Mr. White *WDT*
Subject: The Recent Shift to Earmarked Gold

For the past six months there has been a pronounced shift from dollar deposits to gold by foreign governments and central banks. Earmarked gold has risen from \$1,965 million to \$2,345 million, while the deposits of foreign governments and central banks with the Federal Reserve Bank of New York have dropped from \$1,200 million to \$625 million.

The largest increase in earmarked gold is for the account of the Swiss National Bank, \$240 million during the last six months. Other increases in earmarking during this period, large for the countries concerned, are \$50 million for Sweden, \$35 million for Argentina, and \$25 million for Portugal. The appended table shows the movement in deposits, earmarked gold, and short-term investments held for foreign account by the Federal Reserve Bank of New York.

The usual explanation given by governments or central banks requesting earmarking of gold, that such gold is needed for reserves, certainly does not apply to the recent shift from dollars to gold. Two reasons for this shift may be adduced:

1. The fear that dollars will depreciate in terms of gold.
2. The feeling that earmarked gold historically has a preferred legal status compared to dollar deposits.

The second was probably the dominant reason for the increase in earmarking from the freezing of June 14, 1941 to our entry into the war. The first has probably been the dominant reason since December 7, 1941.

It is interesting to note that there has also been a large increase in holdings of Treasury bills. The Swedish State Bank has acquired \$125 million of Treasury bills since November 1941, and now holds \$103 million at the Federal. The Swiss National Bank has acquired \$60 million of Treasury bills since March 1941, and now holds \$40 million at the Federal.

Funds of Foreign Governments and Central Banks
with the Federal Reserve Bank of New York
(Million Dollars)

As of	All Countries			Swiss National Bank			Swedish State Bank		
	Deposits	Ear- marked Gold	Short- term Invest- ments	Deposits	Ear- marked Gold	Short- term Invest- ments	Deposits	Ear- marked Gold	Short- term Invest- ments
1941									
August 13	1,193	1,964	61	217	220	52	205	70	-
Sept. 17	1,126	2,005	44	213	240	37	206	70	-
October 15	1,188	2,019	37	199	261	29	201	70	-
November 12	1,129	2,064	34	175	301	15	191	70	10
December 17	852	2,192	141	80	360	50	81	95	82
1942									
January 14	752	2,215	175	44	400	60	54	95	105
February 18	624	2,345	153	26	460	40	19	120	103

Treasury Department

Division of Monetary Research

February 24, 1942.

Colonel William J. Donovan,
Coordinator of Information,
Washington, D.C.

Dear Colonel Donovan:

Reference is made to your letter of
February 12, enclosing a memorandum as follows:

"It is stated in dispatch
No. 1 that Secret German funds are
being disbursed by Gilbert Crawford,
446 Broadway. This is probably New
York."

We have made inquiry at this address in
New York and find no trace of a Gilbert Crawford.
J. S. Bache & Company, New York, maintain an
account for one Gilbert Crawford of Durango, Mexico,
which has shown little activity. Other Gilbert
Crawfords are being traced and if anything of inter-
est is learned you will be advised.

Sincerely yours,

(Signed) W. Morgenthau, Jr.
Secretary of the Treasury.

Photo file in M.C.
Orig. file in G-2
Orig. file in G-2

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

Wm. H. Gaston
~~Secretary Morgenthau~~

DATE FEB 24 1942

FROM E. H. Foley, Jr.

I refer to Colonel Donovan's letter to you of February 12th enclosing the following message received from abroad:

"It is stated in dispatch No. 1 that Secret German funds are being disbursed by Gilbert Crawford, 446 Broadway. This is probably New York."

On February 20th I received a memorandum from Mr. Gaston that you desired a report on this matter to be made to you today.

A representative of the Foreign Funds Control Investigative Unit in New York immediately conducted a direct investigation and checked with other Government enforcement agencies with the following results:

1. No Gilbert Crawford is known at 446 Broadway, New York. The superintendent and tenants of the building and a neighboring bank were queried.

2. Three other Gilbert Crawfords were found:

(a) Gilbert Crawford, Durango, Mexico. This individual maintains a small account with J. S. Bache & Company, New York. The account has shown little activity.

(b) a G. H. Crawford is reported as an officer of Dunlop Brothers Co. Ltd. Buffalo, New York. This name is in the F.B.I. files but they have nothing of significance on it.

(c) Gilbert H. Crawford, Nyack, New York. This individual is County Treasurer of Rockland County and is President of the Nyack Ice and Coal Company. He was a Major in the last war and is active in the American Legion. He is spoken of highly in his community.

- 2 -

We are continuing this investigation and will advise you of further significant developments.

S. 12 76

TREASURY DEPARTMENT

276

INTER OFFICE COMMUNICATION

DATE February 24, 1942

TO Mr. White

FROM Mr. Hoflich

Subject: Digest of London Press Reactions

Highlights from London press reviews, received from Colonel Donovan's office, for the period February 15-18, 1942:

1. Churchill's report to the House of Commons failed to convince or silence his journalistic critics. Several seized upon the Prime Minister's reference to heavy burdens as vindicating their contention that he should delegate some tasks to others. There was considerable editorial indignation at his reference to critical public opinion as "panic." Several editors feel that Churchill has become too impatient with criticism. The Prime Minister's account of the escape of the Scharnhorst and Gneisenau satisfied some commentators, but others found flaws in his interpretation.

The Prime Minister does not lack defenders who praise his courage, ability, and logic. Critics are rebuked for asking trouble at home when the empire is hardest pressed by the enemy. But even his stoutest champions leave the way open for cabinet changes, one remarking that immutable government in war is an impossibility.

2. Criticism continues of "the attitude of complacent superiority toward the colored peoples that has marked the British colonial administration in the East and for which we are now paying the price."

It is suggested that there still may be time to repair the grave consequences of that policy in India. The News Chronicle considers that Chiang Kai-shek's visit offers the last opportunity to set things right, and calls upon Downing Street to revise the policy which excluded India and other non-European nations from the Atlantic Charter. This paper is not alone in demanding a change in the official attitude toward India.

3. Prominent place is given to the Ministry of Economic Warfare report of vast U-boat fleets assembling in Germany, perhaps for the invasion of England.

4. Beaverbrook's Express urges immediate approval of the proposal of the Minister of Agriculture for higher guaranteed prices for farmers.

TREASURY DEPARTMENT

277

INTER-OFFICE COMMUNICATION

DATE February 24, 1942

TO Secretary Morgenthau
 FROM Mr. Dietrich

CONFIDENTIAL

Registered sterling transactions of the reporting banks were as follows:

Sold to commercial concerns	£127,000
Purchased from commercial concerns	£ 17,000

Open market sterling held at 4.03-3/4, with no reported transactions.

In a very dull market, the Canadian dollar discount widened to 11-1/2%, as compared with 11-5/16% on Saturday.

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

Argentine peso (free)	.2364
Brazilian milreis (free)	.0516
Colombian peso	.5775
Mexican peso	.2065
Uruguayan peso (free)	.5295
Venezuelan bolivar	.2770
Cuban peso	9/32% premium (nominal)

We purchased \$15,000,000 in gold from the earmarked account of the Bank of Java.

No new gold engagements were reported.

In London, a price of 23-1/2d was fixed for both spot and forward silver, equivalent to 42.67¢.

The Treasury's purchase price for foreign silver was unchanged at 35¢. Handy and Harman's settlement price for foreign silver was also unchanged at 35-1/8¢.

We made no purchases of silver today.

BRITISH EMBASSY
WASHINGTON, D.C.

February 24th, 1942.

Personal and Secret.

Dear Mr. Secretary,

I enclose herein for your
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.

BRITISH MOST SECRET

2713

(U.S. SECRET)

OPTEL No. 64

Information received up to 7 A.M., 23rd February, 1942.

2. NAVAL

Air reconnaissance yesterday showed GNEISENAU (in floating dock) and NURNBERG (6-inch Cruiser) at KIEL, SCHAUMWERST at WILHELMSHAVEN, one Pocket Battleship and one Hipper Class Cruiser at BERGEN, and the TERPITZ in her usual berth at TRONDHEIM. An enemy force of one VITTORIO class battleship, two cruisers, and four destroyers, with three merchant ships, was sighted at noon yesterday on a Southerly course about 180 miles north-north-west of BENGHAZI. Nothing further has been reported of this force, but a convoy was reported at 5.30 a.m. today about 170 miles east of TRIPOLI. A small Norwegian ship was sunk by submarine East of CAPE HATTERAS on the 11th. A British and Norwegian ship, both dispersed from outward United Kingdom convoy, have been sunk 500 miles east of NEWFOUNDLAND. A small United States cargo vessel is reported a total loss after having been bombed north of DARWIN on the 19th.

2. MILITARY

LIBYA. 30th. Some activity by patrols.

BURMA. 21st. Our forces withdrew to the SITTANG RIVER, the withdrawal was not heavily pressed.

3. AIR OPERATIONS

WESTERN FRONT. 21st/22nd. 32 tons of high explosive were dropped on objectives in the RUHR and 22 tons on aerodromes in NORWAY. Eighty R.A.A.F. bombers took part in the night's operations and lost one aircraft. 22nd. Reconnaissance were carried out of KIEL, WILHELMSHAVEN and Norwegian Harbours. 22nd/23rd. 66 bombers were sent out. WILHELMSHAVEN 50, EMDEN 7, OSTEND 5, Sea-mining 2, Leaflets PARIS 2. All returned safely. Cloud prevented observation.

LIBYA. 21st. Enemy aircraft showed increased activity with better weather. They attacked TOBRUK, GAZALA, GAMBUT and AGROMA, but caused only slight damage. One was destroyed.

MALTA. 21st/22nd and 22nd. A total of 109 aircraft attacked HAL FAR, where buildings were seriously damaged and numerous craters were made on the aerodrome, and also TAKALI and LUQA. Three of our aircraft were destroyed on the ground and others were damaged. Hurricanes destroyed one enemy aircraft, probably destroyed a second and nine others were hit. One of our aircraft is missing.

BURMA. During the 21st and 22nd our aircraft supporting our land forces, bombed and machine-gunned enemy troops in the BELIN, KAYAKTO and SITTANG areas. One of these attacks involved every available aircraft, which kept up a continuous attack for several hours on a column of over 500 vehicles. Two Blenheim were shot down during attack on enemy positions. Five of our fighters intercepted a force of 63 enemy aircraft, destroying three and probably destroying two more without loss.

TREASURY DEPARTMENT

280

INTER OFFICE COMMUNICATION

DATE February 24, 1942

to Secretary Morgenthau
from Mr. Kamarck
Subject: Summary of Intelligence Reports

Military Reports

German Navy

On February 21 at 11:15 A.M., a Hudson on reconnaissance reported a German naval force of two battleships (the Scharnhorst and Gneisenau or the two pocket battleships?), three cruisers, and destroyers steering north off the west coast of Denmark. Two striking forces of Beauforts (torpedo bombers) were sent out in the afternoon, but neither force reached its objective owing to extremely bad visibility.

The next day, February 22 at 7:28 A.M., a Beaufighter reported two battleships and three destroyers about 15 miles northwest of Stavanger steering northeast. (On the 19th, it was reported that the Tirpitz was under way at Trondheim. Evidently, a German naval concentration is in progress off Norway. The purpose might be to attack convoys going to Russia, protection against a prospective Allied invasion of Norway, or, perhaps, even for a descent on Iceland.)

(U.K., Operations Report, February 22, 1942)

Japanese Attack on Darwin

On February 19, the Japanese attacked Darwin, using 95 bombers and 12 fighters. A U.S. destroyer and six merchant ships were sunk. An Australian minesweeper and two merchant ships were seriously damaged. Six Lockheed Hudsons, two P-40's, and a B-24 were destroyed on the ground. Five Japanese planes were shot down and five others were probably destroyed. Ten P-40's were lost in the air fighting.

(U.K. Operations Report, February 21, 1942)

French Collaboration with the Axis

It is reported that in exchange for the use of the requisitioned Allied ships on the Libyan supply route, the Germans are allowing the French to keep for their own use until November, 1942, the entire production of military airplanes in the unoccupied zone. This is not likely to exceed 400 planes.

(U.K. Operations Report, February 21, 1942)

- 2 -

Free French Navy

The Free French submarine, Surcouf, is overdue at the Panama Canal. A U.S. transport reported that on the night of February 18, she accidentally rammmed and sank a craft believed to be a submarine in the Canal Zone. (The Surcouf was the largest submarine in the world, being over 2,000 tons in size.)

(U.K. Operations Report, February 21, 1942)

Of Possible InterestBritish Propaganda Directives

(The British are preparing the Empire for the possible loss of Java and Burma. The following are extracts from the weekly guidance bulletin of the Ministry of Information for its Empire news.)

- (a) An attack on Java can be expected soon, and the Japanese will have decisive superiority in men and material.
- (b) In Burma, the Japanese can also bring up superior forces by land and by sea, and the only route the British can use is the sea. The only land communications joining India and Burma are a few mule-tracks across swampy land and mountains.
- (c) The worst service to the Allied cause would be to deprecate the gravity of the situation.

(G.O.I., London Cable)

Vichy French Propaganda at Martinique

The following excerpts are taken from the official Propaganda Bulletin issued by the Information Service for the French West Indies, Fort de France, Martinique.

- (a) An article written by a French prisoner of war released from Germany, which attacks de Gaulle, praises Petain and Germany: "Have they understood the defeat, those who refuse to see with what a deep sense of European realities, Germany knows how to curb the triumph of her crushing victory by inviting France to participate in a new order?"
- (b) An address by Admiral Robert, High Commissioner for the French West Indies, attacking de Gaulle: "Not satisfied with having advocated separation from the Mother Country, this 'Gaulism' has shed the blood of Frenchmen, it is dyed in the deepest treachery, the treachery paid for with distinctions and money."

(G.O.I.)

Argentina

A counsellor of the Argentine Embassy in Switzerland made the following comment on the Argentine Ambassador to Germany: "As you already know 'El Viejo' (the old man) has left Berlin. We shall see whether he sinks or swims after rendering an account of his mission in Germany to the authorities. If there is still any justice, they will have to 'torpedo' him because, as everyone is saying 'Argentine had no Ambassador, but Germany had two, one in Buenos Aires and the other in Berlin.'"

(U.K. Censorship Intercept, February 18, 1942)

February 24, 1942

Dear Bill:

Thanks very much for sending me a copy of the weekly instructions by the Political Warfare Executive in England.

I have found them most interesting, and I wish that you could send them to me each week.

Sincerely,
(Signed) Henry

Colonel William J. Donovan,
Coordinator of Information,
Washington, D. C.

FK/cgk

*File to W.M.C.
cc - Thompson*



UNITED STATES GOVERNMENT
 COORDINATOR OF INFORMATION
 WASHINGTON, D. C.

7
Keller
 February 20, 1942

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

My dear Mr. Secretary:

We have just received the following from our London office:

"The information to follow comes from the PWE general weekly directive. [PWE = POLITICAL WARFARE EXECUTIVE, THE GROUP IN CHARGE OF FOREIGN PROPAGANDA - *CHK*]

"Strategy

"Russia. Maintaining pressure despite the fact that the very heavy snowfalls are making cross-country movements very difficult. They have been making progress at several points, including the Donets salient. Repeat that there is still no sign of where the Germans can stabilize.

"Libya. A German attack is expected soon. Repeat that Rommel's success is due to the fact that reinforcements have been diverted from the Eastern front.

"Far East. We have suffered a major disaster, and the full penalty for it has still to be paid. The out-look is ominous. Emphasize that Japan's hold on her gains hinges on her sea supremacy. This will inevitably pass to the Allies.

"Propaganda Policy

"a. Our propaganda must reflect the mood of the British nation faithfully. This is to remedy mistakes and to win through to victory by greater determination, vigor, and efficiency, and to face facts squarely.

- 2 -

"b. It is bad propaganda to speak of a long war and our final victory to the peoples of the occupied countries. They want a short war and a quick victory. They are at the moment both depressed and critical of us. Therefore, we must show them:

"1. That we are fully aware of the facts and are facing them.

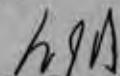
"2. That we are speeding up plans for intensified action against Germany.

"3. That, as winter draws to a close, the indomitable spirit of 1940 is surging back into our veins.

"c. All of Europe thinks that, in spite of Russia's achievements during the winter, in the spring Germany will launch a very formidable offensive. We need a note of urgency in our propaganda and a note of new vigor. We should put less emphasis on those who are collaborating with the enemy and should give more indications that collaborating with us is more worthwhile. We must give Europe a clear indication that we are speedily preparing ourselves for the greatest struggle of the war.

"d. Do not exaggerate the decline in German morale. According to recent reports it has improved. Make it clear that we are now going all out for victory and do not give the impression that we expect others to do the work for us."

Sincerely,


William J. Donovan

It has been learned from a most secret source that on February 24, 1942, A. DUBUS, the Attache at the French Legation in Caracas, Venezuela, made the following statement to his Government regarding the serious effect of submarine action in the Caribbean on Venezuela's economic position:-

"Now that German submarines have been sinking oil-tankers and cargo vessels in the Caribbean Sea along the shores of Venezuela, and bombing oil refineries in Aruba, Curacao and Trinidad, the people are alarmed. Headings in the papers read 'The War reaches us', 'The Blockade of Venezuela', 'One Venezuelan ship sunk', etc.....

Quite apart from anxiety caused by the fact that Venezuela runs the risk, for the time being at least, of being unable to export her main product - crude oil - and of no longer being able to receive goods which she needs, the State revenue is gravely affected, since it depends mainly on the dues from petrol, and on customs duties on imports.

.....About 100 tankers are said to be held up at Maracaibo, Aruba, and Curacao.....If no oil is exported the State revenue will lose about 350,000 bolivars per day.....The tankers which have been sunk represented a capacity of 60,000 barrels a day. Such are the statements made by 'competent' persons and published in the local press.....

"Threatened as the country is, by lack of storage facilities, the oil industry may have to reduce its production, or even face a complete stoppage. All shipping is at a standstill, including coastal shipping; the export of coffee and cacao has ceased, and there are no more imports by parcel post.

Of the 300 million bolivars worth of goods, representing about 500,000 tons, which Venezuela imported by sea every year, how much will she be able to receive now?

Fortunately for Venezuela, the United States and Great Britain are vitally interested (because of supplies for their naval and air Services) in seeing that the country's crude oil reaches the refineries, which are in close proximity to its shore and in the possession of England and Holland.

- 2 -

The Under-Secretary of State for U.S.A., Mr. Sumner Wells, has just announced that ships in the Caribbean would be convoyed.....

It is said in Venezuelan circles that, of a crude oil production of more than 30 million tons, scarcely four million is refined in the country.

The installations at Aruba, Curacao and Trinidad are open to naval attacks. The American-Anglo-Dutch Groups have, up to the present, always been opposed to the construction of large refineries on Venezuelan soil.

Perhaps they will now be disposed, in their own interests to satisfy the public opinion of this country by developing the refineries already there, or, by constructing new ones near where the oil is drilled, or at any rate, at a sufficient distance from the coast."

SECRET
COORDINATOR OF INFORMATION

RESTRICTED

MID 319.1 No. 640 M.I.D., W.D. 11:00 A.M., February 24, 1942.
Situation 8-11-41

SITUATION REPORTI. Pacific Theater.

Philippines: Nothing new to report. Burma: The British have been forced back to the Sittang River which parallels the railroad from Rangoon to Mandalay. Enemy ground superiority continues to be felt despite effective Allied air action. Java: The Japanese air force attacked an airport near Bandoeng and an air base near Malang. In the Timor Sea Japanese planes attacked shipping, and on New Guinea, Port Moresby was raided on the 23rd. Allied aircraft attacked the Japanese-occupied city of Rabaul on New Britain, and are reported to have destroyed six enemy bombers in a raid on Bali.

II. Western Theater.

No air activity of importance has been reported.

III. Eastern Theater.

Fighting continues along the general front. Russians claim to be pushing their advance on Smolensk. (A situation map will not be issued this date.)

IV. Middle Eastern Theater.

Press releases indicate patrol activity and minor combats in the area south and southwest of Tmimi. There is apparently an increase in Axis air activity both against ground troops in North Africa and the Isle of Malta. A Rome Communique states that the R.A.F. carried out attacks on Feb. 24 on the ports of Benghazi and Tripoli.

RESTRICTED