

May 28, 1942
3:00 p.m.

LEND-LEASE IN REVERSE

Present:

Mr. Wickard
Mr. Bell ✓
Mr. White ✓
Mr. Hicks ✓
Mr. Hendrickson
Mr. Wheeler
Mr. Acheson
Mr. Achilles
Mr. McCloy
Colonel Franks
Mr. Hansel
Captain Hendren
Mr. Cox
Mr. Ecker
Mr. Roston
Mr. Coe
Mr. Rosenthal

H.M. JR: I don't know whether it is weeks or months ago that we met to discuss Lend-Lease in Reverse and how we would handle payments of our armed forces abroad.

Mr. Acheson advises he is ready to report on the progress he has made, and you gentlemen might like to know, in the strictest confidence, what we estimate the British gold and dollar position is; and I think the figures we are going to show you we checked with them today or yesterday - very recently, anyway.

MR. WHITE: We checked with them. They wanted to get another look-see by themselves and would let us know. They said it looked all right at the first glance; they said they would let us know before this meeting, but they haven't.

H.M.JR: I think Mr. White might just tell us what our estimates are on the dollar position.

MR. WHITE: Possibly first I might summarize the position and then if there are any questions I can supply the details upon which the summarized estimates are based. The position as of May 15, 1942, a couple of weeks ago, which would supply us with the latest data that could be available, showed the following: The British Treasury had available gold, four hundred and ninety-nine million dollars. They had available dollar balances, ninety million.

The reason why I speak of it as available, and not merely dollar balances is because they have some additional balances in gold which they do not regard as available, and we do not count as available, for various reasons.

In addition to those two items, they have seventy-two million of what they call "scattered" gold, gold located in various parts of the world, which would take a little time for them to ship if they found it necessary to convert into dollars. We are inclined to include that in their funds which are available, if we don't regard it from the point of view of the immediate moment. That makes a total of six hundred sixty-one million dollars which we interpret as being available.

(Mr. Wickard entered the conference.)

H.M.JR: I was just asking Harry to give a report on the dollar position, very confidentially, of the British, and it totals six hundred sixty-one million dollars as of May 15.

MR. WICKARD: What is the trend? In other words--

MR. WHITE: Well, that I will take up next. That is what they had on May 15.

H.M.JR: I said we considered these very confidential.

MR. WHITE: We estimated, using mostly their figures, the gold and dollar expenditures which they anticipate

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during the remainder of this calendar year for various items, which we can recount if you are interested. They total seven hundred and thirty million dollars. They have dollar receipts coming to them for various types of transactions over the same period of three hundred and ten million dollars. Now, that leaves them a deficit during the remainder of this year on current operations of four hundred and ten million dollars. That is, their outgo will exceed their income by four hundred and ten million on current account.

They will receive during the coming year, during the remainder of this year, a total of approximately four hundred and ninety-seven million dollars, minus a change which I will speak of in a moment, of which Mr. McCloy's office notified me a few minutes ago, which will reduce that somewhat.

Now, if we take what they had on May 15, namely six hundred and sixty-one million dollars, and then deduct from that their deficit during the year of four hundred twenty million, and then add the anticipated receipts on nonrecurring items, so-called, of four hundred and ninety-seven million dollars, it would leave them with a balance at the end of the year of seven hundred and thirty-eight million dollars.

(Mr. Bell entered the conference.)

Now, some of the items going into those figures represent estimates. Estimates of trade would be the largest element of estimates and are susceptible, of course, to errors, plus or minus; but in our calculations, wherever there was a known doubt, we tried to err on the side of being conservative so as to give them the benefits of any doubts that may exist so that we would expect that the likely possibility is for them to have somewhat more than that, rather than less.

I want to qualify that by information which we have just received from Mr. McCloy that one of the items that had expected to yield sixty million dollars, plant facilities which they were going to get, some of it in the near future and some of it a little later, has, upon reexamination, been found to yield possibly fourteen million less. They are not certain but they think that is likely to be the case. There are some

buildings, some machine tools, which they feel they don't want to take over because they are too highly specialized and apparently not adapted for the use of the American needs. So one would have to reduce that, possibly, to seven hundred and twenty-five or, if you want to be a little more conservative, make it seven hundred million. That does not include any further take-outs.

In other words, if they were to be relieved of the payment due as of June 1, which would be two hundred and thirty-five million dollars, that would have to be added to that sum, which would bring it up to the neighborhood of nine hundred and fifty million dollars.

Now, that is a summary. The details, if you like, Mr. Secretary, can await any specific questions.

H.M.JR: That is fine. Now, if anybody wants to ask - we will go around.

MR. ACHESON: Could I ask about the nonrecurring items? I didn't get that figure.

MR. WHITE: Yes, the total was four hundred ninety-seven minus this fourteen million we have heard about, which would make it four hundred eighty-three. They consist of the ordnance and some planes and the facilities; and there are one or two other items, one of which they may be doubtful about. There is an item of twenty-five million which they can borrow, if they need it, on collateral which they already have left. They seem to think that the value of some of the collateral had diminished in the past months so low as to make it doubtful whether they could get another twenty-five million. But a conversation I had with the RFC official who is working on that, a couple of months back, seemed to indicate that if necessary they wouldn't have that difficulty, so we have included it.

MR. ACHESON: Does that finish them up on the non-recurring items?

MR. WHITE: That would finish them up on the non-recurring items, although actually to call all those

"nonrecurring" items is not accurate, because among those items are included the dollar expenditures of soldiers' pay in various sterling areas. That is an item which I presume will be recurring, but the facilities and the take-outs will not recur.

MR. BELL: They are paid in sterling.

MR. WHITE: Who is paid in sterling?

MR. BELL: The soldiers - our soldiers are paid in sterling.

MR. WHITE: Yes, but we buy the sterling. They get the dollars but - I think, Dan, what you are referring to, possibly the supplies, are the facilities which Dean Acheson is going to speak about, for which they are going to supply the sterling; but for the pay, though, the soldiers may get the sterling we now buy for them.

MR. BELL: I thought you had that included in another place.

MR. WHITE: No, that was in this place.

MR. McCLOY: That includes the eighty-four million or ordnance and the air facilities which you have got this re-estimate on.

MR. WHITE: That is right, and the other items - there are the Maritime shipyards, Todd Shipyards, twelve million; there is the balance of the RFC loan, twenty-five million; there are receipts from agreement purchases of Australian wool, fifteen million, of which they just received six million a couple of days ago. .

There is one other item that I think needs to be talked of, and that is the estimate of current gold production. The estimate that we have here is two hundred thirty-five million dollars, and that estimate excludes gold production of Australia, New Zealand, and British Oceania, which produced about eighty million

dollars in 1941, but the production is decreasing. How rapidly we couldn't find out, but they are not giving the new equipment and so there is every expectation that it will diminish, but we haven't counted that at all.

The British Treasury position has been that none of this two hundred thirty-five million of gold should be included because they regard that as a desirable source of dollar exchange which will be needed after the War, because of the mounting sterling bloc balances in England. So they would be inclined to leave that out. That is the major item about which I think there is any difference of opinion.

One other item might interest you, and that is the estimate of the dollar receipts from U. S. troops in the sterling area, the thing we were just talking about. We estimated sixty-five million. The Army estimate is much higher than that. If the Army estimate is nearer correct they will end the year with that much more money. The Army estimate is more than double that.

MR. BOSTON: This two hundred thirty-five million for gold is for the next six months?

MR. WHITE: It is for the remainder of this year and is to be compared with a figure much greater than that for an equivalent period which was produced last year during the same months.

MR. WICKARD: Did I understand you to say that was not included in any way in the figures you gave first?

MR. WHITE: They are included, but they are figures which the British would wish excluded.

MR. WICKARD: They should be excluded?

MR. WHITE: That is right.

MR. COX: How much for Lend-Lease purposes by the U.K. and the Dominion?

MR. WHITE: They estimate that, I think, at eighty-five million dollars for the rest of this - seventy-five million. That is just for U.K. For the others, they are lumped with merchandise figures. That is seventy-five for the remaining months.

H.M.JR: But the figure is seven hundred million before the decision is made whether or not we will take over the balance of unpaid contracts as of June 1, which is two hundred and ten odd million dollars?

MR. WHITE: That is correct.

H.M.JR: Does anybody else want to ask some questions?

MR. ECKER: On this gold, the two hundred thirty-five million, as I understand that, the balance as of the end of the year includes an estimated increase in current gold production of two hundred thirty-five, or is that exclusive of the current production of gold?

MR. WHITE: No, this two hundred thirty-five million is an estimate of the gold production in the British Empire exclusive of Canada and exclusive of Australia and Oceania, during the remainder of this year. It is a figure which is very much lower than the production for similar months of last year, and the year previous.

MR. ECKER: Additional production of gold is included in the balance as of December 31 of seven hundred thirty-eight million?

MR. WHITE: That is right. If you want to not count that, you would have to deduct from that figure this gold production, which would make it about five hundred million.

H.M.JR: If there are no other questions, will Mr. Acheson tell us the progress he has made.

MR. ACHESON: Mr. Secretary, I think the last meeting we had here with you was the one in which Mr. McCloy was going to take over some of the contracts.

The one before that was devoted to this subject of Lease-Lend in Reverse. At that meeting we had a memorandum which outlined some suggestions which were made, which met with general approval, and the result of the meeting was that I was asked to get in touch with the British and the Australians and see what could be done about it. I did get in touch with them, and we had considerable delay while the British and the Australians talked between themselves as to how they wanted to proceed.

The first question was whether they wanted to talk together or in two separate groups. They finally decided that they would talk together. Then we had another period when they discussed between themselves whether Australia would make a separate agreement or whether it would adhere to the British agreement. That situation has not been altogether worked out. They said they wanted to go ahead and talk about the Lease-Lend in Reverse first and then they would iron out between themselves whether they would make a separate Lease-Lend agreement with us or adhere to the British agreement.

After we got by those two points, the British and the Australians both presented to us a memorandum in which each of them outlined their ideas on Lease-Lend in Reverse. They were not very different from the memorandum that we had gone over in the meeting in the Secretary's office here, except that both of them showed a great deal of nervousness about their dollar position, and they had a great many minor reservations.

For instance, they agreed to supply our troops with everything which was available locally, wherever the troops were, or could be readily brought to those places, except that everything for which they paid dollars they wanted to be repaid in dollars. That got into such items as oil, which came from any place where they pay dollars for it, or any munitions which were under present Lend-Lease contracts.

We got a lot of minor exceptions, which we felt were undesirable to take away from any broad agreement and

which seemed petty and undesirable from a political point of view. So we went to work on those memoranda without going into it with the British or Australians any further, and produced an alternative proposal which we had put in the form of exchange of notes with the British and with the Australians. Those papers have been circulated to the Treasury Department and the Army and the Navy, the Board of Economic Warfare, and Lease-Lend Administration. We have suggestions from all of them which have been put into a revised draft, and that is what we have before us now. That is the document that you called this meeting about, if, that is, all the other agencies - they accepted the suggestions they made and they are in accord with presenting those documents to the British and the Australians and seeing how far we get with it.

H.M.JR: Do you mind, just so I will be sure I understand, giving a sort of a thumbnail sketch of what that agreement is.

I don't know whether Agriculture saw it or not.

MR. WICKARD: No.

H.M.JR: They did not see it.

MR. ACHESON: No, I don't think that went to you because it doesn't deal with any of the import problems you are dealing with.

These notes both start off with a recitation of the fact that in the United Nations' declaration of January 1 each one of the countries has stated that it has pledged itself to employ its full resources wherever they can be most effectively employed against the common enemy. Then it refers to the Lend-Lease agreement of February 23, 1941, in which we agreed to grant reciprocal aid to one another. Then it says that the general principle which is to be followed in Lend-Lease in Reverse and Lend-Lease direct, is to use the war production and war resources of each country where they can be most effectively used, taking into consideration available man power, production, and particularly shipping space.

The idea of that is to lay the principle that what-

ever there is in the United Kingdom or near the United Kingdom, or in Australia or near Australia, shall be provided by those countries for our troops instead of transporting that material all the way from the United States.

We then say that wherever possible we will undertake to make decisions about the utilization of our common resources together, and that another principle which we have in mind is to reduce so far as possible the need of each country for the currency of the other; in other words, to employ Lend-Lease and reciprocal aid wherever that can be effectively employed. When we state that the United Kingdom will provide as reciprocal aid under the same terms that we provide Lend-Lease aid the following list of items.

The first one is all military equipment, munitions, military and naval stores, whether provided in the United Kingdom or in the field, or sent to this country. Every military item that they give us, and they will give us all the military items which can be most effectively transported from Great Britain, will be as Lease-Lend aid.

Then here occurs the item which is introduced into this. It says that this is on the assumption that the United States will assume the remaining unpaid installments under the present Lend-Lease contracts, which Dr. White has set at two hundred and thirty-five million dollars. The reason for putting that in--

H.M.JR: Excuse me. Has that been in right along?

MR. ACHESON: No, sir, that has not been.

H.M.JR: I didn't understand that that was in right along.

MR. ACHESON: No, I was bringing out that that has now been put in. At the last meeting that we had Dr. White had a list of seven or eight methods by which the British

could get dollars. This was one of them. Another one was a hundred and fifty million dollars from the pay of our troops. Another one was to pay for some of the work which was done in Australia or the United Kingdom, and there were various methods which we could adopt to take care of the British dollar position.

We have put in here, for your consideration and discussion, this method as being a way of getting out of this agreement all these reservations about protecting the British on their dollar position by reimbursing them for every item for which they pay dollars and various minor things which they had through here all the time which seemed to us to take away from the breadth of this as a real reciprocal aid agreement.

H.M.JR: May I interrupt you again? To refresh my memory, when we talked about this the last time, you and I in this room - just to refresh my memory - wasn't it that we were talking about it costing us four hundred million dollars to maintain our troops in U.K., and that the thought was we would go fifty-fifty. Wasn't that the first proposal? Lend-Lease would remember that.

MR. ACHESON: I think at the last--

MR. WHITE: I think it is about three hundred odd million dollars.

H.M.JR: Wasn't it four hundred dollars?

MR. WHITE: And fifty-fifty.

H.M.JR: Would you remember? We were talking about waiting, recommending letting Lend-Lease wait?

MR. ACHESON: I think it was four hundred.

MR. McCLOY: It sounds about right. The fifty-fifty business - I remember some such suggestion.

MR. WHITE: Three hundred for civilian pay and a hundred for various troop supplies; so it would be four hundred together.

H.M.JR: And to be fifty-fifty.

MR. ACHESON: Yes, that was the suggestion that Lend-Lease brought in.

H.M.JR: The time we met in this room before - no catch to it, I am just trying to build up my memory - and then what we really are saying now is instead of going fifty-fifty we will take over two hundred thirty-five million.

MR. ACHESON: That is it.

H.M.JR: And then you pay - if the figure is still four hundred million, you pay the whole four hundred million.

MR. ACHESON: That is the proposal.

H.M.JR: Is that what it boils down to?

MR. ACHESON: That is exactly it.

H.M.JR: That is what it boils down to?

MR. ACHESON: Yes, sir.

MR. ACHILLES: To the extent that the United Kingdom is the most effective source of supply, they supply; we would supply those things which can be most effectively supplied from this country.

H.M.JR: You mean, is that the loophole - I am very loophole conscious. I am going before the Joint Tax Committee tonight.

MR. ACHESON: Secretary Morgenthau is correct in what he said. We figured out at the last meeting that the items which the Australians and the British themselves would supply would amount somewhere in the neighborhood of four hundred million. That was three hundred million for the works which would be carried on within their territories and about a hundred million for items of food and other things of that sort.

MR. WHITE: That estimate of the works which they would carry on I think is much in excess of what subsequent figures supplied by the Army seemed to indicate. Mr. Hicks, do you remember the exact figure?

MR. HICKS: It was cut a little more than in half. I understand one of the reasons is that they are using troop labor in some of the bases instead of civilian labor.

MR. WHITE: So instead of three hundred million, apparently less than a hundred and fifty.

H.M.JR: But to get back, the point that I get that you are making is, so that I won't be fooled on this thing - let's take the Middle East; the situation might be where even the Middle East - we might be nearer to them on the oil. If the English lost their oil, in that case we would furnish the oil.

MR. ACHILLES: It would be determined on purely practical grounds of where the stuff was available and which was the most efficient source of supply from the point of view of shipping. Leaving out financial considerations, that is, other than the general principle that they should supply what they could from the sterling area and we supply it from the dollar area - but that the decision would be basically, on practical grounds, where it was most efficient to get it.

H.M.JR: Then it is very uncertain how much they will put up. I mean, we know that we have got to take, over and above everything that we have done so far, and I want to say for the War Department that they have been fine on it - but we are facing a decision here today, should we take over two hundred thirty-five million, more or less, on the first of June. What the English would do on Lend-Lease in Reverse is the big question now.

MR. COE: It is certainly subject to specific negotiations, isn't it, before the two Army groups?

MR. ACHESON: I think the point that Mr. Achilles has brought up is really in a different field. Under this arrangement here there are, generally speaking, three types of articles that we are talking about. One is purely military items, anti-aircraft guns, and all that kind of thing. The British have supplied a certain amount of that material, and what it says here is that everything which is supplied of that nature is Reverse Lend-Lease.

Then you get into two different categories. One is the material which they supply to the troops in the field where the troops are. In Australia I think they have supplied seventy-eight million dollars' worth of stuff already, of which sixty has been Lend-Lease in Reverse, and eighteen has been paid for, probably a good part of that in the early days. Here obviously the local supply is the most efficient supply, and they just go ahead and do that.

Then you come to works which are being carried on in the Middle East. For instance, we are building works in the Persian Gulf, and there the document says that wherever the British are the most efficient suppliers of anything they agree to supply it to us. If it is a question of getting oil in the Persian Gulf and they can get oil right there, they supply it to us. Obviously, they are the closest person.

If it is a question of steel pipe and they haven't got any steel pipe, then we are the most efficient source. As Mr. Coe says, in that area the thing has to be a negotiation each time to see which is the best place to get it.

H.M.JR: I am not through yet on this thing. I don't know how far it went, this so-called pooling of all military supplies. Where does that cut across this picture?

MR. ACHESON: That has been done quite apart from

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this to whatever extent it has been done, and this merely refers to the fact that whatever decisions can be made in common will be made under whatever arrangements the President and Prime Minister send up to the Joint Munitions Assignment Board; or whatever else it may be. This doesn't add anything to that, Mr. Secretary.

H.M.JR: No, but I mean the pooling arrangements might be such that we might find ourselves in the position that we might have to be giving, well, a great deal more to our own troops than we figured that we might get if there was no pooling arrangement, and just this technical agreement was signed. I mean, it brings in another thing, another problem. I mean, we might be assigned the manufacturing of all anti-aircraft guns, for example - I don't know as it is a good example, but I will use it - under the pooling agreement, or all tanks, so that everything that went to Australia would have to be ours. They would say, "Under the pooling agreement you were told to make all tanks, so it isn't up to us to furnish any tanks to your troops in Australia," irrespective of how long - how many miles they are shipped, or whether the closest place - I just wondered if this pooling agreement might cut across this agreement.

MR. COX: It may to a certain extent, but I don't think it does in its major implications. The other kind of pooling that you are talking about is made primarily on strategic and production grounds.

H.M.JR: Yes, but--

MR. COX: And, for example, it might work in reverse - suppose the decision were made that Britain make all the fighters and we concentrate on bombers, and that our troops in Britain be equipped with British fighters, so you cut back on this again, and you get much larger supplies of military equipment than the other way. It works both ways.

MR. McCLOY: Shouldn't it be articulated - the Secretary made a good point, that that should be articulated

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with the pooling arrangement of the Munitions Assignment Board. Shouldn't it be referred to as fitting into that?

MR. WHITE: Let me give an illustration of how it might be necessary to do that, a little different than the one you made. I don't know that it is contemplated - I don't think it is, but there is merely a possibility, unless it is made clear.

Supposing that England decides to transfer an increasing number of its contracts, which it has hitherto placed in Canada, to the United States, which leaves Canada with increasing facilities. The United States, taking advantage of those facilities, orders the material in Canada, which means that the United States pays Canada in dollars; whereas prior to that arrangement the settlement was made between England and the U.K. in terms either of bloc sterling or something else. I say I don't know whether that is contemplated, but that is possible, and to what extent I don't know.

MR. COX: I think the combined chiefs and the Munitions Assignment Board make their decisions without regard to the financial aspects of the problem. There would be nothing to force the United States to pick up Canadian manufacturing facilities on pre-existing British contracts.

MR. WHITE: I don't think I made myself clear. I mean, we find that Canadian facilities are not being utilized to the fullest extent by virtue of the fact that they are dependent on British orders, which are declining. I gather that the Board, under those circumstances, would deem it desirable, as it definitely would be desirable, to utilize those facilities to the maximum amount and, therefore, give orders to the Canadian factories which prior to that decision had come from England. So what you would have would be a gradual reduction in England's orders to Canada, the difference being that in the one case England made the settlement with Canada, and in the latter case the United States pays Canada in dollars. I don't say that that is either contemplated or a part of this, but it is that type of operation that the Secretary has in mind.

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MR. COX: It is happening now.

H.M.JR: The only thing I am raising is this. We Secretaries, Ministries of Treasuries, the Secretary of the Treasury - the only time we ever get a chance to say anything is just before the check is drawn, and once I go along and say - approve whatever it is, two hundred thirty-five million, why then that is most likely the last I will ever see of this thing.

I am just raising the point now, because we have gone very far with the British on what we have done with existing contracts. I just wondered if we are really getting anything out of the Lend-Lease in Reverse. I am just raising whether we are really getting anything.

MR. ROSTON: Insofar as we have large troops stationed in Britain, I should suppose we would be getting a good deal from England on Lend-Lease in their equipment. I should suppose that would be over a period of several years a very considerable balance on this two hundred thirty-five.

H.M.JR: Under the pooling agreement, wouldn't we necessarily get a lot?

MR. McCLOY: You wouldn't necessarily get much, but you might. There are certain items that are being supplied now to our forces in Ireland, finished munitions, and it is small, but it might increase, might increase substantially.

H.M.JR: Do you think so, just as a guess?

MR. McCLOY: As a guess, I would say a pretty small percentage.

H.M.JR: Let me put it - that isn't what I mean. As a guess, do you think it would be growing in amount in dollars or equivalent of a dollar that they are going to have to--

MR. McCLOY: Yes, going from here out, but not to a very substantial extent, I should say.

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H.M.JR: I am sorry to have delayed you so long in reading, but I was doing my homework as you went along.

MR. COX: May I raise another question, Dean, on the proviso about balances due on June 1? Why wouldn't it as a political and practical matter be desirable to leave that clause out, and if you think it ought to be done, do it the way these prior take-outs were handled, instead of referring it to any agreement, because if the notes are made public, I should think one of the things Congress would want to know is why on commitments already existing you put in that kind of a provision. Then you have got to get in this whole complicated foreign exchange pool and everything else; and whether you can explain it to Congress or not, I don't know. It is a very difficult thing to draw a picture of.

MR. ACHESON: I don't think I quite get your suggestion. You mean leave the date out?

MR. COX: No, leave out the proviso clause on the munitions goods, finished munitions on order by the British in this country, because if they need additional dollar exchange help, then you can do what has already been done without the notes, in the Army take-over. If you put it in the agreement, then it seems to me you are going to raise a great deal of discussion on one of the most complex problems that Congress has ever had before it.

MR. ACHESON: Well, I think you are faced with an entirely practical problem here.

MR. COX: But up to now we have been willing to supply the British with not only Lend-Lease aid but dollar exchange aid without any formal agreement on their part. Now, it seems to me when you come to Lend-Lease in Reverse, they ought not necessarily to want a formal agreement from us; that as to contracts up to two hundred thirty-five million we would agree to take them out, if it is going to complicate either public relations or political relations.

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MR. ACHESON: But the difficulty in getting an agreement with the British and the Australians about Lend-Lease in Reverse is that they are giving up, by agreeing to Lend-Lease in Reverse, a source of dollars.

MR. COX: No question about it.

MR. WHITE: I question that. It is a question of the magnitudes. What I gather that the Lend-Lease arrangement is, as I read it, as it is drawn, is that whenever they have to make dollar expenditures, with the exception of some very small items, it comes from the dollar group.

Using the illustration that I think Mr. Achilles used, that if oil were necessary to be obtained on practical grounds for any troops in the Near East, if it had to be obtained in areas for which foreign exchange were necessary to pay, it is the United States that would buy it. The only time that England would pay is where it came from the sterling area. And I think it is important to distinguish between two things, because it is fundamental; that is, the problem involved in the take-outs is exclusively a foreign-exchange problem. It is not a question of measuring the amount which is being contributed by the United States as against the amount which is being contributed by England.

The reason for these take-outs lies in the fact that they fear that they will not have adequate dollar exchange. It is not an attempt to measure, to increase our contribution as against theirs. Therefore, the thing must be regarded exclusively from a foreign-exchange point of view, else confusion results, and what you merge with is nothing that relates to the problem in hand. As a foreign-exchange problem, I think what you have to concentrate on is how much they have got and how much they are likely to have as a result of the arrangement which you are negotiating for.

If you feel there are adequate amounts without the two hundred thirty-five, then Oscar's point comes to the fore. Do you want to take this measure for adding to

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their foreign exchange, if this measure involves the whole complication of arguments that have been built around the question of taking them out of past commitments?

MR. COX: I would go even beyond that. I would say if the other methods or means were not sufficient to give them the dollar exchange you think they ought to have, as an actual fact as against a prediction, then you ought to be willing to go ahead on this basis, too.

The only point I am making is that it seems to me it ought not to be in the formal note, because what you have done to date in the last three months is actually to give them that dollar exchange relief with no agreement. You have never had agreements in terms of helping the British, either in terms of supplies or dollar exchange because, after all, they are an ally.

MR. WHITE: There is something more than that involved in that, it appears to me. I think we all feel that we don't want to do something administratively which Congress had no intention of doing, and this question of the two hundred thirty-five involves a matter that Congress already understands with respect to past commitments.

Now, if the trend of events should be such that for one reason or another the British find themselves short of dollars six months from now, or a year from now, it seems to me that there is a clear basis to go to Congress and say they need dollar exchange; and if there aren't any of these take-outs available, and they are declining, you see, then Congress will make possible ways and means of supplying them, or Lend-Lease would, or some way would be found.

But for us to attempt to anticipate a need by doing what I think is contradictory to the Congressional intent - we have gone pretty far in that direction already - I mean, now is a good time to stop, look, and listen.

H.M. JR: I would like to ask a question, to see if I understood Mr. Acheson correctly. This two hundred thirty-five is really the meat of the coconut, is it?

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MR. ACHESON: That is right.

H.M.JR: I mean, the whole thing - you mean you have got to change their position by offering them this?

MR. ACHESON: Yes, if we take the other attack, then we have something which is really not a Lend-Lease in Reverse agreement at all, because what you have to say is that they will supply things up to a point where they begin to run short of foreign exchange, and then we will pay for it.

MR. WHITE: I don't see that from your account, but possibly you make that clear. I gather from your proposal they are going to supply things which are produced in the sterling area and we are going to supply things that are produced in the American area; if there is a need for things in the sterling area which can be more effectively, more quickly obtained outside the sterling area, then dollars will be paid.

If, on the other hand, America should need things which can be more easily supplied in the sterling area, Britain will pay them, but let us remember that that is the basis of the proposal, as I understand it; nowhere in that proposal is there any significant source of a demand for dollar exchange on the part of the British. There is a source for sterling, yes, that is true, but that is not involved in the question of foreign exchange.

MR. ROSTON: One phrase of that is not quite accurate, because the agreement would contemplate that British arms production in this country are being made subject to assignment.

MR. WHITE: But that involves two hundred thirty-five million. Let's keep away from that, because the assumption is they have money to pay for that, and that is past commitments; but aside from that, and that is the thing about which I take it you are discussing - aside from that, I don't quite see where they will be called upon to provide gold or dollars.

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MR. ACHESON: They won't, Harry. I meant to say - that isn't the point I was trying to make. They have an opportunity - if there were no Lend-Lease in Reverse at all, and we paid for the food and the works and everything which was being done or being used by our troops in Australia, they would have a source of dollars--

MR. WHITE: That is true.

MR. ACHESON: ... with which they could liquidate these pre-Lend-Lease contracts.

MR. WHITE: They could liquidate that without that, and still have some seven hundred million dollars at the end of the year; and, incidentally, you might be interested in the evaluation as to what will happen after the end of the year. I think that is important because we have only anticipated up to six months here. During the calendar year 1943, their current account will be reduced by a certain amount by virtue of the cessation of British payment.

Now, they will have a deficit in '43 of about two hundred million dollars on current account, assuming no major trends in trade and being conservative in estimates. To meet that two hundred million dollar deficit, this is what they will have: a current gold production - that was six hundred million dollars in '40, and we are estimating it at two hundred thirty-five for the rest of this year, or four hundred million this year. You can still further reduce it, as it might well be, owing to the lack of supplies for '43, but whatever it is, they would have that to contribute toward the two hundred million.

They would have also an increasing source of dollar exchange arising from the increased expenditures on soldiers' pay, which I presume is more apt to increase than decrease in total. So there is reason to believe that after the first of the year their dollar-exchange balances will increase, since, if I understand you correctly, your proposal does not call for any use of dollars on their part, and since the question of the two hundred thirty-five million dollars is exclusively a

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dollar exchange problem. I don't see how they have anything to concern themselves with unless some unforeseen thing develops.

To put the quid pro quo on a basis such as you would seem to put it, to include this two hundred thirty-five million dollars, is a surprising thing, because what in effect that becomes is the British will say, "We will be glad to supply sterling for your troops and your supplies, but you have got to give us two hundred thirty-five million more dollars." Then you ask, "Why?" What is the answer? Why?

MR. ACHESON: Well, I think you pointed out when you were going over the British dollar position that their attitude on the current gold production is that they should not be asked to turn that over.

MR. WHITE: Well, yes, if you want to examine that position. If you agree with it, then I think they need more money, but before we take that position, I think we would like to examine it. I see no particular reason--

H.M.JR: When Mr. Keynes was over here, as I remember, representing the British Treasury, the figure that they had in mind was if they could have a minimum of around five, six hundred million dollars, they would consider that was all right.

I would just like to interrupt this for a minute. I think this is something that Lend-Lease can answer, and nobody else. When I went up to testify on the first Lend-Lease, I made the statement before Congress that the British would pay for all outstanding contracts in the United States.

MR. COX: You did both on the Lend-Lease Act itself and on the appropriations.

H.M.JR: About a billion three or a billion four, wasn't it? It is over a year; I can't remember those things. Is that about right?

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MR. COX: That is right.

H.M.JR: I won't go and testify again, because I won't have to. I am not handling it any more, but you gentlemen do, and you people are responsible to Congress. I mean, the chances are they won't call me. But you have my testimony there, and I think - I don't see how anybody else can answer it except Lend-Lease, in view of the testimony that I gave. I don't know that there is a change subsequently. Are you people prepared to go up and explain why on June 1?

MR. COX: I think there is something more. I think that is one factor. I think Harold Smith's factor that the first Lend-Lease appropriation would not be used to take out pre-existing contracts, and the implication afterwards is another factor; but I think much more fundamental than that, if the appraisal dollar exchange position is correct, even from the British standpoint, I certainly wouldn't want to see a public document in which the issue was stripped the way Harry has stripped it, and which may be stripped that way by somebody in Congress saying, "After all, we have supplied up to X billion in Lend-Lease. When they come to supply stuff out of sterling sources, why should we have to give them the additional consideration."

Now, the only answer you have got to that is the dollar exchange position.

I don't know where, quantitatively, the dollar position ought to be, six hundred million or eight hundred million. Ultimately you get back to your value judgment of what dollar exchange position is a safe buffer for the British.

MR. WHITE: That is right.

MR. ACHESON: Well, of course what you say is true. Several things have happened since some of these events that we are talking about. One is that we are now in the war. The whole basis of this document is that each one of these two or three countries supplies under Lend-Lease that part of its war production which it makes

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available to the other one. It makes no difference under this document whether they are pre-existing contracts or later contracts, or what they are. If they are articles which come out of this country, we do it under Lend-Lease. If they are articles which come out of Great Britain or the British Colonial Empire or Australia, they pay for them and give them to us under Lend-Lease.

MR. COX: Except you have one qualification and that is the underlying assumption, in terms of the contribution of the war effort, that it is what is reasonably under the control of the other country in the sense that they can procure it. Now the British may be able to buy oil in a place because it is a sterling area or sterling would do it. They may also have contracts in this country which, unless this Government takes additional steps, they have got to control, which immediately throws you back again into dollar exchange position. But, it is no different in principle whether it is produced in Great Britain or this country if the financial mechanism pre-existing happens to be that the British have got to suffer under the contract, and you assume that they have got the means to pay for it, which is the gray case, sort of in between, and it seems to me--

MR. ACHESON: It depends on what principle you are adopting. You could adopt another one. The one that is put forward here is that dollar costs are paid for in this country and supplied under Lend-Lease, and that sterling costs are paid for in Great Britain or Australia and supplied under Reverse Lend-Lease.

It seemed to us that that was the best way to proceed and that is the way which is most easily understandable by the country and makes the best presentation of it.

MR. WHITE: And who pays for the expenditures in neutral countries which involve dollars? The United States does. And why has the United States taken the position? The Lend-Lease have taken that position, for

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the reason that they have rightly said that the foreign exchange assets of the British Empire are such that we want to relieve them as much as possible of those. So again there is behind all these decisions involving foreign exchange the notion that we want to see, and the Secretary has made that definite promise to them, that they have adequate amount of dollars in gold to see them through. They have given the figure of six hundred million themselves. So it again comes back, I think, to the question of an estimate of their foreign-exchange position.

MR. ACHILLES: One situation we want to avoid, and which, as I understand, has already arisen to a certain extent in Australia, is that an estimate, for instance, where the commanding general wants so much meat for the troops, the Australians say, "Here it is, no shipping problem; we have got it here, but we need dollars. We have got to sell it to you for cash rather than under Reverse Lend-Lease." That is the sort of thing we ought to head off completely if we can.

MR. WHITE: I understand they withhold meat because of not being paid dollars instead of sterling? Is that your suggestion?

MR. ACHESON: We want to prevent that.

MR. WHITE: Is there any suspicion in your mind that that might be the case?

H.M. JR: I would like to know when that thing comes, because I sat here until hell froze over and said, "Yes, yes, yes," to the English on buying millions and millions of dollars and never - always said the English were good for it. I never raised the question. I knew damn well they weren't good for it, and if the time comes they refuse us anything, I would like to handle that situation personally. I mean, I would like to be given the opportunity, for Mr. Roosevelt, to handle that situation personally, because I went through hell for them, financially. Mr. Churchill recognized it, because he personally thanked me for it. When that time comes that

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they say no to us on anything on a financial basis, you do me the favor of letting me handle that for Mr. Roosevelt.

MR. WHITE: Beyond that, even if that were so, and let's be skeptical, how does your suggestion correct that?

MR. ACHILLES: By putting the thing on the purely practical basis that as much as can effectively be supplied locally would be supplied locally.

MR. COE: You can have it on that basis and still leave open the other question, can't you? I mean, you can say that from now on what is to come out of the U.S. we make available through Lend-Lease, and what is to be paid to the troops in those areas in sterling, they furnish. You don't have to cross the bridge on this other unless you want to.

H.M.JR: I would like to ask Mr. Acheson - I realize he has put a lot of work into this thing, and all these things are difficult - does he think it would be impossible to include an agreement with the U.K. postponing any decision on existing contracts, having everything just the way it is, but leaving that out.

MR. ACHESON: No, I don't think it would be impossible, but I think you would probably have in it some reservations about the fact that if they got into foreign exchange difficulties, we would have to assume some kind of an obligation or that this agreement would be off in that situation.

H.M.JR: Well, we will have to anyway, and I mean - I don't want to plead the case for Lend-Lease, but we are all part of the same family. I think - I don't know whether this document has to be made public or not. It doesn't make much difference. But I think that at this stage where their foreign-exchange and dollar position looks pretty good, as far as we can see it, for the rest of this year, and certainly the first six months of next

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year, and in view of all the testimony, that at this time we take up two hundred thirty-five million dollars of their contracts, I think it is next to impossible to explain why. Somebody will have to go up and give them the information that the Treasury has as to their dollar position, I mean, if we are on call, and why on the first of June did we do this. I wouldn't want the job of explaining it. I am coupling that with a remark that I have told the British, and I said it publicly, that in my powers as Secretary of the Treasury, and as long as I sat here, within the powers that I have, I would see that they always had enough dollars to prosecute the war.

MR. ACHESON: I think you are going to have that question up in some form or other.

MR. ECKER: May I ask this question, Mr. Acheson? If that question were raised, is it necessary to go further and to agree to pay dollars for such of the equipment that came off of these contracts as are assigned to our forces, the U. S. forces? That is, assuming, of course, that the view is that the British dollar position does not need this additional strengthening by taking out two hundred thirty-five million of contracts.

MR. ACHESON: Well, I don't believe that would really help very much, because I don't think any of this is going to be assigned to American forces. These are all special items.

MR. McCLOY: Go back to the British.

MR. ECKER: Then you come back to the position which is fundamental as to whether the British dollar position now appears to be all right or needs an additional strengthening of two hundred thirty-five.

MR. ROSTON: After that it depends on whether or not you include current gold production.

MR. WHITE: Yes, now that - I mean, on those matters there is room for discussion. I think it should be made

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clear at this point that unforeseen developments, by their very term, are possible, and that there has been some discussion recently which has come to me second hand - possibly you know more about it, Dean - that India is beginning to balk at accepting sterling or is likely to balk. The English have said nothing of it, and they may insist on getting paid in foreign exchange or gold.

That is one of the contingencies which would throw our estimate out of gear, but it appears to me that if any such major development takes place which involves additional aid to England - it seems to me that the appropriate place to decide whether or not to give that aid is either on the bills which already exist, the Lend-Lease, or coming to Congress for further powers, rather than attempt to foresee every contingency, what seems to me to be a diversion of Congressional intent.

MR. ACHESON: May I clear up one situation, Mr. Secretary?

H.M.JR: Please.

MR. ACHESON: At the last meeting which we had here with you, you recall that you wrote the Army about these pre-lend-Lease contracts

H.M.JR: That is right.

MR. ACHESON: And we had the letter from Mr. Stimson written by Mr. McCloy that Mr. Stimson put the note on.

H.M.JR: Yes, a famous note.

MR. ACHESON: At that time, in view of the proposal which you made, which the Army was to take over, on these contracts, Mr. McCloy had various suggestions. At that time you said that you should go off and made a payment for the airplanes which had been taken over prior to January 10.

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H.M.JR: Which he has done.

MR. ACHESON: And something about the ordnance.

MR. McCLOY: Which is done, too. We will have the money in ten days. The contract has been signed.

MR. ACHESON: And that then you would consider again this matter of the pre-Lend-Lease contracts.

H.M.JR: What?

MR. ACHESON: That you had originally written Mr. Stimson about.

H.M.JR: Did we mention these contracts?

MR. ACHESON: That was what produced the meeting.

H.M.JR: I thought what produced the meeting was my following up the War Department on the airplane and the ordnance, but I didn't think anything other than that, not two hundred thirty-five or whatever the amount was at that time.

MR. ACHESON: That is what I wanted to clear up.

H.M.JR: Are you confident? If you are, I will take your word for it.

MR. ACHESON: No, but I thought that long letter you had from Mr. Stimson, which was not too easy to read, bore on the question of taking over these contracts.

H.M.JR: Well, if I am a little hazy about it, I am no different than Mr. Stimson was when he signed it.
(Laughter.)

MR. ACHESON: There was a paragraph at the end in which they said they would be willing to take them over, but wanted to go up to Congress and explain it to the committees.

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H.M.JR: Yes, but - you wrote the letter.

MR. McCLOY: I wrote the letter, but the reason that letter was confused was because we were trying to describe factually what had occurred and the various treatments we had given, applied in connection with taking over these munitions from the British. Up to one period of time, we did it one way; then in another period we did it a different way. There were three different methods that we followed. We tried to explain that, and then we didn't make any commitments as to what we were doing, just explained what the situation was. We said in the last paragraph, as I recall it - of course the letter is here somewhere - we would try to do everything we could to help out, but we pointed out that there was some difficulty politically.

MR. ACHESON: The fundamental question that you had raised by Mr. Morgenthau, who said, "Why don't you take over the rest of these contracts?"

MR. McCLOY: That is right.

MR. ACHESON: You said you didn't want to take them over.

MR. McCLOY: I didn't want to do it because of the political difficulty; that is the thing we are talking about now.

H.M.JR: Did I talk about taking over the outstanding contracts?

MR. McCLOY: We talked about it at that meeting.

H.M.JR: That I wrote that?

MR. McCLOY: You didn't write that - no, the only thing that was written was in that letter - the letter - the explanation of the methods we had applied in connection with the taking over of the munitions, mainly airplane contracts - airplanes, rather, at the time.

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MR. WHITE: At that time, Mr. Secretary--

H.M.JR: As I gather, Mr. Acheson raised the point that he thinks in my letter to Mr. Stimson I asked for the contracts made prior to March 15, 1941.

MR. ACHESON: That is what I was getting at. I thought the question we were now discussing was postponed from that earlier meeting. I never saw it, either.

MR. McCLOY: I think what happened was that you said here at the meeting, "Go back and see what you can do in the way of taking take-outs." I pointed out that we had had some difficulties with the Air Corps. I pointed out that we might be able to take over facilities, we might be able to take over some of the ordnance contracts, and certainly I thought we would be able to pay cash for certain of the airplanes that had been delivered during a certain period. I came back then and reported that I was able to give your Board a check offer for seventy-five million dollars for the airplanes we had taken out after January 1. I forget what that was. Then I reported that we would also go ahead with the ordnance, and then I reported that we might go ahead with the air facilities. Those are the three things that Mr. White talked about.

As I understood it, it was then, after I had made the report on the War Department, you would then take up again with the Lend-Lease as to what extent they might perhaps liberalize their policies that they had already had in effect to increase the dollar exchange of the British.

There were a number of items, for example, that the Lend-Lease had heretofore been refusing to buy for the British. Perhaps you might alleviate that, liberalize that policy and find additional amounts to build up this four hundred million. That was the figure we were then talking about.

H.M.JR: That is right. But the thing I think Acheson is talking about, and we will know that in a

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minute - I sent for the letter - did I, or didn't I in that thing say that we would take up the outstanding contracts?

MR. ACHESON: That is the question I was asking.

H.M.JR: Now, if I did, then why am I raising the question now? Is that right?

MR. ACHESON: No, I thought - this is my understanding of the procedure. I thought Mr. Morgenthau wrote to the War Department and said, "Why don't you take these things over and relieve this pressure?" The War Department wrote back and said, "We don't want to take these over, because we have told Congress we are not going to use the appropriation for this purpose," and came back with a counterproposal, which was, "You take over some of them, that Lend-Lease would liberalize to the extent of a hundred million and that we go fifty-fifty on the payments," and that Mr. Morgenthau said, "Well, we will consider at the meeting only the take-overs that you propose, and that when we see what you can do on that, we will reconvene the meeting and see where we stand on the other contracts."

MR. COX: I think the difference--

MR. ACHESON: That was my understanding of where we were.

H.M.JR: We will know in a minute or two. I have sent for the letter.

MR. ACHESON: My proposal is a compromise between what I thought--

MR. COX: As I recollect the conversation, both were talking about different things, one is the take-over of contracts, which involves both pre-March 11 and post-March 11 contracts; as to the post-March 11 contracts the Army had a political problem as to whether funds appropriated for the War Department procurement can be

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used to take over stuff under these contracts and then turned over to the British.

The other political question on the pre-March 11 contract is the one the Secretary raised. Naturally, I don't think there is any basic fundamental difference between the two, except the testimony on the first batch of them.

H.M.JR: I have given him (McCloy) the correspondence. We will let him report.

MR. McCLOY: There is no question. Your letter simply says that for the past four months you have been hearing about taking these British planes from the British at the time of the Pearl Harbor episode. You give your understanding of what it is, but I say that I don't know that this is the case. "Can you please advise me what the situation really is and what reimbursement has been made, if any, and what is intended?"

H.M.JR: On British planes?

MR. McCLOY: "I should appreciate it if you would tell me how much is involved in each of the types of transfer, and what the Army's decision about payment has been on each." Then, the famous letter came back, which tried to explain in words of one syllable, carrying through three pages, what we had done. We talked about four types of--

H.M.JR: Excuse me--

MR. McCLOY: Then we described the four types of diversions that we had made. We said what we thought we could do and we stated some objections to taking them all out.

"It is realized, however, that you must concern yourself with the financial results of such a transaction, in order that United Kingdom dollar exchange may be maintained at an appropriate level. To assist this undertaking, the War Department is willing to reimburse the British Government for the airplanes diverted to the United States up to the date of the effectiveness of the terms

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of the Arnold-Portal Agreement (January 1, 1942). This proposal has the approval of the Office of Lend-Lease Administration.

After our meeting we then went through with the seventy-five million dollar transaction, and, as I understand it, at that meeting I was asked to look into the possibility of taking over the ordnance contracts and such others that we thought we could do and get away with it. After that was done, the report was to be made to you and then you were going to explore the further possibilities and particularly I have in mind was their liberalization of Lend-Lease policy. There may have been some other steps that could be taken.

H.M.JR: I don't trust my memory these days for anything.

MR. McCLOY: There was no mention about the early take-overs in your letter; it was simply how have we dealt with these plane transactions.

H.M.JR: Doesn't this pretty much, the final word - doesn't it get down to Lend-Lease, I mean, as to these two hundred thirty-five million dollars worth of contracts, whether you people do or don't want this included in this agreement. Now that you have got this financial picture for the next twelve to eighteen months--

MR. COX: I think it is much broader than that. I think you get down to the question of the take-overs on the financial end. You have got a question of whether Lend-Lease or the War Department has got the money and the willingness to take over, but I would gather that decision, given the available funds, would be based in part on a consensus of opinion here. It is part of the policy - I don't think any particular agency ought to make a decision one way or the other which would in the judgment of everyone else interfere with the execution of the major policy.

H.M.JR: I don't mind saying how I feel after listening to this thing. I mean, I just wondered - just talking

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for myself - whether Mr. Acheson wouldn't approach these people one more and leave out the two hundred thirty-five million dollars. That is the way I feel, but I would like to hear from somebody else.

MR. COX: Can I throw out one alternative suggestion? I don't know whether it makes any sense. That is, putting these exchange of notes and other reciprocity provisions - that is, each will do what is reasonably within its power to take care of the foreign exchange position of the other. I think it might be some help.

MR. ACHILLES: I don't know whether that would be desirable.

MR. COX: That, it would seem to me - I would rather see it out altogether - more politically desirable than a firm commitment on something you will have a lot of difficulty explaining.

MR. ACHESON: I think you ought to consider, if we do what the Secretary has suggested, which can be done perfectly well - we can get an agreement on that basis - I think you will immediately have the question in another form, so that somebody will have to deal with it. And really, it becomes a balance of the two considerations that Harry White mentioned a moment ago, is it better to take over the two hundred thirty-five million dollars here or to try and get the current gold production. It is a balance, one or the other.

MR. WHITE: That problem has been up for some time, and they can always feel free to raise that again here; and that, in other words, puts the problem where it has been for the past two years on the question of the adequacy of their foreign exchange holdings, and the Secretary has been conversing with them almost once a week.

H.M.JR: I would like to answer that myself. I have never agreed to this position that the gold would just be put away in a separate pot. I have steadily

maintained the position that gold must be considered a part of their dollar asset, and I have never changed my position on it. They have regularly protested. I have just brushed it aside. My position has been perfectly consistent on that, that their gold was part of the dollars.

MR. WICKARD: It seems to me that that question has to be settled. If that question is settled and, as you say, it is, and that is accepted, or isn't accepted, for that matter, then you can maintain without question the six hundred million dollar balance which they have said they had to have. Is that right?

MR. WHITE: Yes, that would be about seven hundred million, probably, without that.

MR. WICKARD: Yes, well then, it doesn't seem to me--

MR. WHITE: No, I beg your pardon. I mean, without the two hundred and thirty-five; you would have to deduct that from the seven hundred thirty-five which would leave their position about five hundred million. That two hundred and thirty-five is rather crucial in the matter.

H.M.JR: No, but I don't think you understood, Harry. With the gold, how much is their position?

MR. WHITE: Well, it would be seven hundred and thirty-eight minus the two hundred and thirty-five, about five hundred million.

H.M.JR: No, no.

MR. BELL: That is right, if you deduct the contracts.

MR. WHITE: If they have to pay for the contracts and don't get the gold--

MR. COE: That isn't it.

MR. WICKARD: I am getting confused now.

MR. WHITE: Gentlemen, what we said was as follows, that if this two hundred and thirty-five million dollars which has been discussed were to be given to them they would have almost a billion dollars.

H.M.JR: Supposing they have to pay - let's say they have to pay for the two hundred and thirty-five.

MR. WHITE: Then they will have seven hundred and twenty-one million and we include an item which I said was controversial, namely, the gold.

MR. WICKARD: The gold - I say if that is included, then the six hundred million dollar balance is well taken care of.

MR. WHITE: No, they would only have about five hundred then.

MR. COX: If it is included.

MR. WHITE: If it is included it is well taken care of.

MR. WICKARD: That is my point. It seems to me if you settle the gold question, I don't think there is much necessity worrying about the other one.

H.M.JR: Well, Claude, I have always taken the position, and to show that the English agreed to it very much in the room here at one time when they were hard pressed, they went through a process of mentally earmarking the gold in South Africa and using it in that way. They couldn't lay their hands on it so they mentally earmarked it in South Africa, whatever that meant, but they used it and used some gold up in Canada. I mean, we have got all this precedent behind us, then they got the gold out of South Africa, replaced the gold in Canada and scared themselves off that way. They went to that extreme. Isn't that about right, *lan?* *squared?*

MR. BELL: Yes, that is right.

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H.M.JR: So I mean, when they get up against it they have used their gold, and I have maintained steadily that they have to use their gold just the way we would use ours if we got hard pressed.

MR. WHITE: One additional bit of information. This position with respect to their including their gold among their assets represents a change in their position, a change which occurred some time ago. I think it was almost a year ago, not quite; but before that there was never any question but what the gold was part of their assets.

MR. COE: Are they having any trouble getting the gold from South Africa?

MR. WHITE: They may have.

MR. ACHESON: I think their worry comes from the worry you mentioned, the sterling obligations.

MR. WHITE: There are these possibilities which may develop. I think it would be a mistake for anyone to think they may never be faced with a shortage of dollar exchange. They may be. India may not accept any sterling; South Africa may not accept any sterling, and they will be in a position where we will have to come to their assistance.

MR. BELL: Dean, is this agreement flexible enough so that the United States can use discretion in paying dollars for these items that you enumerate?

MR. ACHESON: I assume it.

MR. BELL: Then why aren't we in a position to give them dollars whenever we want to, to maintain this fixed balance regardless of the two hundred and thirty-five?

MR. COX: That is one of the reasons I suggested the alternative clause, to make that clear on the basis

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of the agreement, I should think, that one method of relieving the dollar-exchange position in unforeseen situations would be to pay dollars instead of getting it by reciprocal aid.

MR. WHITE: Isn't that something that had better be left orally rather than in the record? It raises all kinds of problems if you say it in such general terms, and that is the procedure upon which you have been operating up to now very successfully.

H.M.JR: Well, McCloy, do you want to express an opinion?

MR. McCLOY: I would like to see the two hundred and thirty-five million proviso left out, definitely.

H.M.JR: You would?

MR. McCLOY: Yes, I would.

MR. BELL: The record is pretty clear on the Hill all the way along, and every meeting has made it tighter, I think, hasn't it, Oscar? At every hearing the question has come up.

MR. COX: No. It came up first on the appropriation testimony.

MR. McCLOY: Whenever it came up it was damn clear.

H.M.JR: Can I just go on. Mr. Wickard?

MR. WICKARD: I was just repeating what I said a while ago. It seems to me that if their gold is counted in on the dollar credit they have there is no difficulty from their standpoint, unless there are some unforeseen circumstances which would have to be taken care of anyway. I don't see why you don't leave that out.

H.M.JR: You gentlemen representing Mr. Wallace, do you want to express an opinion?

MR. ROSENTHAL: I would be inclined to take the same position, Mr. Secretary.

H.M.JR: How about the Navy Department?

CAPTAIN HENDREN: I don't know very much about it, Mr. Secretary, except it seems to me it would be better to leave it out if the same purpose can be accomplished by leaving it out.

H.M.JR: Somebody for Lend-Lease?

MR. COX: We used up our time. I think we have pretty well expressed the--

H.M.JR: Well, you have got the expression - have I overlooked anybody?

In view of the way they feel, would you mind taking it up again with them?

MR. ACHESON: No, I will be glad to.

H.M.JR: Would you do that?

MR. ACHESON: Of course I will be glad to. I think it is - I think I have expressed that I think it is a mistake, but the - we have got to face the position sooner or later that the British are very worried about their gold and dollar position and that they have a good deal of justification, you can see that.

MR. WHITE: I think so.

H.M.JR: Yes, but they have got much less reason to be worried now than they have had any time since they have been at war.

MR. WHITE: They have worried from the first moment they got in the war.

MR. ACHESON: Their debts are increasing at a very great rate.

MR. WHITE: Sterling debts.

MR. ACHESON: And current gold is one of the few assets they have against that.

MR. WHITE: That raises the whole complexity of post-war questions, monetary questions, which I for one would be very happy to go into but certainly it can't be disposed of in that fashion. There are a great many things to be disposed of in that, and I think a meeting might be devoted to that, if you like. I certainly wouldn't wish to come to any quick decision on that because they are piling up their sterling bloc balances and we have to supply them with the gold with which to meet those bloc balances if they are drawn upon after the war.

H.M.JR: Well, you have gotten an expression and if it is agreeable to you - you weigh everybody's views. The way I feel, I would like to ask you to have another try at it.

MR. ACHESON: All right.

H.M.JR: And as soon as you are ready, we will meet again. I realize it is very different today.

Thank you very much.

March 20, 1942

Dear Henry:

For the past four months I have been receiving letters from the War Department, the Lend-Lease Administration, and the British Purchasing Missions, referring to the fact that various planes and other military supplies originally intended for Britain are being taken over by the United States Army for its uses or for shipment to Russia. Most of the letters refer to the method that will be used to reimburse the British Government, but since there are several types of diversions involved, the letters disagree with each other, and consequently, I find that I do not know either the amounts involved in the diversions, or the type of reimbursement that the British will receive in any of the transactions.

As I understand it, the types of diversion are as follows:

1. Diversions of materials from British dollar contracts (a) for the use of the United States Army, and (b) for shipment to Russia in fulfillment of United States obligations to Russia under the Moscow Protocol;
2. Diversions from British Lend-Lease allocations (a) for the use of the United States Army, and (b) for shipment to Russia in fulfillment of United States obligations to Russia under the Moscow Protocol.

Some of the information that I have received, leads me to believe that the British will receive payment in dollars for the planes and materials diverted from their own dollar contracts, but I know that my information is not complete.

I should appreciate it if you would tell me how much is involved in each of the types of transfer, and what the Army's decision about payment has been on each.

Very sincerely yours,

(Signed) H. Morgenthau, Jr.

Secretary of the Treasury

The Honorable Henry L. Stimson,
Secretary of War,
Washington, D. C.

WAR DEPARTMENT
WASHINGTON

April 3, 1942

Dear Henry:

I have at hand your letter of March 20 which brings up the question of diversions of equipment from various sources of financing for the use of the United States Army, or in certain cases for the use of the Russian Government. This question arose mainly through the action of the United States Army Air Corps during the period subsequent to December 7 in taking delivery from British financed contracts with United States manufacturers various aircraft which were utilized by the United States Army itself, or in certain cases transferred to the U.S.S.R. under Lend-Lease. I can understand your confusion as to the method that the Army plans to use in repayment for this equipment. I believe that the following outline will clarify the matter.

The four types of diversions outlined in your letter are substantially correct. However, there remains some question as to the exact dollar value which should be placed upon the airplanes diverted by the War Department. A satisfactory conclusion must be arrived at between the War Department and the British Air Commission before any values can be quoted. Particular difficulty is being experienced in determining what amount, if any, will be included to allow for amortization of British capital invested in United States plants and what appropriate charges should be allowed for accelerated service tests performed upon the airplanes in question.

Three alternate methods present themselves for establishing appropriate credits to the British Government.

1. Reimbursement in dollars to the British for material diverted to other uses by the United States.
2. Repayment in kind to the British for equipment diverted.
3. The entering of a credit on the Lend-Lease books of account for the value of the material diverted to the United States, thereby reducing the total Lend-Lease bill by that amount.

These three methods apply, of course, only to material diverted from British dollar contracts. In the opinion of the War Department, no problem exists on diversions to the War Department from foreign government Lend-Lease allocations, as the funds which financed this procurement were never definitely committed to any foreign government and were never within the control of any foreign government.

With the establishment of the Munitions Assignments Board as a functioning agency, all production within the United States of items common to the United States and to foreign governments, regardless of the source of financing, immediately became one large "pool". The equipment in this "pool" will be distributed on the basis of strategic determinations to the Theaters of War throughout the world in which the equipment is most urgently needed. Thus, the over-all production of the United States becomes the determinant as to the availability of equipment. A transfer of equipment to any foreign government automatically becomes a Lend-Lease transfer regardless of the source of financing or the agency making the original procurement. Those items diverted by the United States to governments other than the one originally making the procurement will be taken up on the accountability records of the War Department, placed in normal stock, and immediately lose their identity. It will be the responsibility of the foreign governments from whose contracts equipment has been taken to see that appropriate documents are forwarded to the War Department upon which a credit can be made to their Lend-Lease account. The entering of this credit should complete the transaction. This will be balanced by the transfer of goods by the United States Army to foreign governments which will, in effect, be repayment in kind.

A further complication exists in that it is contemplated that in the near future shipments of equipment manufactured in the United States will be consigned to a representative of the United States Army in the theater of operations in which the equipment is to be utilized. His disposition of the material will be determined by strategic needs and will bear little or no relation to any statement of Lend-Lease requirements previously submitted to the War Department, nor will it have any reference to the source of procurement and financing of the material in question. Such procedure will considerably expedite the war effort, which is the end that we all have in mind.

It is realized, however, that you must concern yourself with the financial results of such a transaction, in order that United Kingdom dollar exchange may be maintained at an appropriate level. To assist this undertaking, the War Department is willing to reimburse the British Government for the airplanes diverted

to the United States up to the date of the effectiveness of the terms of the Arnold-Portal Agreement (January 1, 1942). This proposal has the approval of the Office of Lend-Lease Administration.

Of the three alternative methods presented for handling the problem of diversion from foreign dollar financed contracts to the United States Army the most feasible from the War Department's point of view is that of entering a credit to the account of the foreign government concerned upon the Lend-Lease books.

Yours faithfully,

(signed)
Henry L Stimson

Secretary of War.

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

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE May 28, 1942

TO Secretary Morgenthau
 FROM Mr. White
 Subject: The British Gold and Dollar Position,
 May 15 through December 31, 1942

- I. The British gold and dollar position has materially improved in recent months:

	<u>January</u> 31	<u>March</u> 6	<u>March</u> 31	<u>April</u> 30	<u>May</u> 15
	(in millions)				
"Available" gold	\$403	\$440	\$452	\$449	\$499
Official dollar balances	55	32	71	52	90
"Scattered" gold	52	68	82	112	72
(The British state that this gold is scattered in various parts of the world, and hence unavailable. It has now become so large and so variable from month to month that we believe it should be added to the "available" gold and dollars to obtain a correct picture.)					
<u>Sub-total: "available" and "scattered" gold and dollars</u>	<u>\$510</u>	<u>\$540</u>	<u>\$605</u>	<u>\$613</u>	<u>\$661</u>
Belgian gold	105	105	105	105	105
(This represents gold borrowed from Belgium and said to be unavailable because of the equal liability to the Belgian Government.)					
Gold held against immediate liabilities.	10	10	10	10	10
(The British state that this is a reserve set up in accordance with the terms of clearing agreements)					
<u>Total gold and dollars</u>	<u>\$625</u>	<u>\$655</u>	<u>\$720</u>	<u>\$728</u>	<u>\$776</u>

II. The prospect for the remainder of the year is that Britain's gold and dollar balances will continue to increase, reaching \$700 million to \$750 million by December 31. This forecast is based on a conservative estimate--largely from British figures--of Britain's probable deficit on "current" account, and upon a conservative evaluation of special receipts from the sale of some of Britain's dollar contracts, from the expenditures of American troops in the Sterling Area, from the current gold production of the Sterling Area, and so forth. The details of this estimate are as follows:

III. Estimated British expenditures on "current" account, May 15 through December 31, 1942

A. Payments to U.S. by U.K.			
(a) On BPM commitments	\$295		
(b) Other merchandise outside lend-lease	75		
(c) Services outside lend-lease	65		
(d) Other	50	\$485	
B. Payments to U.S. by other Sterling Area			
(a) Merchandise imports	\$110		
(b) Services	50	160	
C. Payments by Sterling Area outside U.S. requiring gold or dollars			
(a) Oil	\$ 40		
(b) All other, including \$22 million for payments to Iran	45	85	

When negotiations for a British-Iranian exchange settlement first arose, it was estimated that \$5 million a month would be required to meet the sterling deficit of Britain in Iran. The terms of the final settlement, however, call for British payment of Iranian dollar obligations and only 40% of the remaining British deficit. We do not know how much of a change this will make in the original estimate supplied by the British, but it may reduce Britain's expenses on this account from \$40 million for the 8-month period to \$25 million.

Total gold and dollar expenditures on "current" account

\$730

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IV. Estimated Sterling Area gold and dollar receipts on "current" account May 15 through December 31, 1942

A. U.K. receipts from U.S.

(a) Merchandise	\$ 60	
(b) Services	45	
(c) All other	<u>50</u>	\$155

B. Rest of Sterling Area

(a) Merchandise	<u>\$130</u>	
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This estimate is about \$35 million higher than that made in our former study. The figure used in that study excluded exports from Australia and New Zealand. Since it now appears that these areas will be held and will continue to export, they have been included. Exports from Ceylon and British India, however, are still excluded. If these areas should be held our estimate would be \$200 million instead of \$130 million.

(b) Services	<u>25</u>	155
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<u>Total Sterling Area gold and dollar receipts on "current" account</u>		\$310
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V. Estimated Sterling Area gold and dollar deficit on "current" account May 15 through December 31, 1942

420

VI. To offset this deficit the British will probably obtain the following special receipts:

A. Purchase by army of ordnance contracts	85	
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We understand that half of this amount is to be paid very soon.

B. Army purchase of British plant facilities	60	
--	----	--

This includes only those plants for which a presidential directive for purchase has been given. In addition to this, the British might succeed in selling \$30 million of other plants.

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- C. Maritime Commission purchase of
Todd Shipyards \$ 12
- The sale contract of the
Todd California Yard,
calling for a payment of
\$5.5 million, was signed
on May 18. The sale contract
of the Todd Bath Yard, a
somewhat larger contract,
is expected to be signed
within 2 weeks.
- D. Dollar receipts from U.S. troops
in the Sterling Area 65
- The Army's estimate for
this figure is more than
twice as large, and
neither this estimate nor
the Army's estimate takes
account of the pay raise
now being discussed in
Congress.
- E. Balance of R.F.C. loan 25
- \$35 million of the \$425 million
loan has not been dispersed, but
we understand that the R.F.C.
will retain \$10 million as a
sinking fund.
- F. Receipts from Agreement purchases of
Australian wool 15
- \$6 million was received on May 25.
In addition to this, the British
will receive about \$10 million from
the sale of wool already received
in this country, plus a further
amount for wool that will arrive
during the remainder of the year.
- G. Current gold production 235
- This excludes the gold produc-
tion of Australia, New Zealand,
and British Oceania, which
produced about \$80 million of

- 5 -

gold in 1941, although we understand that these countries are continuing to produce gold. The estimate of \$235 for the period May 15 to December 31 is equivalent to about 60 percent of the gold production of British African countries in the same number of months in 1941.

The British contend that current gold production should not be counted as a dollar receipt because of the necessity of accumulating a reserve against their rapidly increasing sterling debt overseas.

Total of anticipated special receipts \$497

VII. Summary:

- | | |
|---|------------|
| 1. "Available" and "scattered" gold and dollar balance, May 15, 1942 | \$661 |
| 2. Total gold and dollar expenditures on "current" account May 15 through December 31, 1942 | - \$730 |
| 3. Total gold and dollar receipts on "current" account May 15 through December 31, 1942 | <u>310</u> |
| 4. Gold and dollar deficit on "current" account May 15 through December 31, 1942 | - 420 |
| 5. Anticipated special gold and dollar receipts May 15 through December 31, 1942 | <u>497</u> |
| 6. Estimated "available" and "scattered" gold and dollar balances, December 31, 1942 | \$738 |

We believe that these estimates are conservative, and that Britain's gold and dollar balances at the end of the year may well be as large as \$800 million. If in addition to this amount, Britain were to receive payment for the \$235 million due on her aircraft contracts, her gold and dollar balances would be over \$1 billion.

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VIII. The Prospect for 1943

During calendar 1943 Britain's deficit on "current" account should be reduced to about \$200 million per year because of the cessation of payments on BPM contracts.

There will be available to meet this deficit (1) current gold production, which, though probably smaller than the \$600 million produced in 1941 and than the \$400 million forecast for 1942, will nevertheless be substantial, and (2) a large volume of American troop expenditures in the Sterling Area. We may expect, therefore, that Britain's dollar balance will increase further after the end of the year, even if other unexpected expenditures, such as that occasioned by the Iranian incident, should occur. Should some major development arise, this forecast would, of course, be upset.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE May 28, 1942

TO Secretary Morgenthau
FROM Mr. Kamarck

Subject: Shipment of Planes to British Forces

1. In the week ending May 26, 1942, a total of 103 planes of all types (65 combat planes) were shipped to British forces.

2. The Northrop Vengeance, listed in the last report as a pursuit plane is really a dive-bomber. The description of this plane as a pursuit ship was based on "Aerosphere, 1941" which is mistaken in this respect.

The Northrop Vengeance is a single-motor dive-bomber, and is the same as the U.S. Army's A-31 attack bomber. It is powered with a 1600 or 1700 h.p. Wright motor.

Table A - Shipments by Area

	Week Ending <u>May 26, 1942</u>	Total Shipped in 1942 to date	Total Shipped since <u>Jan. 1, 1941</u>
<u>To the United Kingdom</u>			
Light and medium bombers	15	264	1,425
Heavy bombers	8	58	162
Naval patrol bombers	0	8	110
Pursuit	21	707	1,018
Army Cooperation	0	71	102
Trainers	0	0	24
Total to the United Kingdom	44	1,108	2,841
<u>To the Middle East</u>			
Light and medium bombers	8	200	530
Heavy bombers	0	0	5
Pursuit	13	249	1,097
Army Cooperation	0	12	12
Trainers	0	8	150
Total to the Middle East	21	469	1,794
<u>To the Canadian Forces</u>			
Light and medium bombers	0	37	205
Heavy bombers	0	1	1
Naval patrol bombers	0	23	31
Pursuit	0	30	72
Trainers	38	368	1,609
Total to Canadian Forces	38	459	1,918
<u>To the British Pacific Forces</u>			
Light and medium bombers	0	133	233
Naval patrol bombers	0	0	27
Pursuit	0	186	349
Trainers	0	0	105
Total to Pacific Forces	0	319	714
<u>To the British Indian Forces</u>			
Pursuit	0	40	40
Total to Indian Forces	0	40	40
<u>Totals</u>			
Light and medium bombers	23	634	2,393
Heavy bombers	8	59	168
Naval patrol bombers	0	31	168
Pursuit	34	1,212	2,576
Army Cooperation	0	83	114
Trainers	38	376	1,888
Grand Total	103	2,395	7,307

Table B - Shipments by Types

	<u>Week Ending May 26, 1942</u>	<u>Total Shipped in 1942 to date</u>	<u>Total Shipped since Jan. 1, 1941</u>
Bell Airacobra	0	314	468
Boeing B-17	0	12	32
Boston III	0	10	34
Brewster Buffalo	0	0	168
Cessna Crane I-A (AT-17)	4	56	56
T-50	0	86	700
Consolidated Catalina	0	31	168
Liberator	8	47	136
Curtiss Kittyhawk	15	466	848
Tomahawk	0	0	544
Douglas Boston I, II, and III	0	0	492
Fairchild 24 R-9	0	73	95
Glenn Martin Baltimore	8	203	271
Maryland	0	0	150
Grumman Martlet II	0	46	87
Lockheed Hudson	15	309	1,279
Lightning	0	3	3
Ventura I	0	12	12
Ventura Bomber	0	94	94
North American B-25B	0	6	6
Harvard II	0	52	949
Mustang	19	378	458
Northrop Vengeance	0	5	5
Pitcairn Autogiro	0	0	5
Stearman PT-27	34	182	183
Vought-Sikorsky Chesapeake	0	0	50
Vultee-Stinson O-49	<u>0</u>	<u>10</u>	<u>14</u>
Grand Total-All Types	103	2,395	7,307

Table C - Plane Shipments to the British by Weeks

<u>Week Ended</u>	<u>Light and medium bombers</u>	<u>Heavy bombers</u>	<u>Naval patrol bombers</u>	<u>Pursuit</u>	<u>Army Cooperation</u>	<u>Trainers</u>	<u>Totals</u>
Weekly average of shipments in 1941	36	2	3	28	1	30	100
January 6, 1942	24	0	5	30	4	9	72
January 13, 1942	3	0	2	58	0	42	105
January 20, 1942	4	0	0	14	0	60	78
January 27, 1942	24	0	1	100	5	13	143
February 3, 1942	9	0	3	10	4	4	30
February 10, 1942	20	0	3	59	0	4	86
February 17, 1942	9	0	2	41	7	0	59
February 24, 1942	24	0	2	86	7	1	120
March 3, 1942	26	0	1	80	6	0	113
March 10, 1942	25	2	0	78	1	0	106
March 17, 1942	34	1	0	94	8	0	137
March 24, 1942	94	9	12	79	0	84	278
March 31, 1942	49	1	0	58	4	10	122
April 7, 1942	69	2	0	8	4	5	88
April 14, 1942	55	7	0	86	6	29	183
April 21, 1942	55	11	0	43	15	34	158
April 28, 1942	35	10	0	39	0	26	110
May 5, 1942	14	2	0	98	0	4	118
May 12, 1942	10	3	0	75	12	6	118
May 19, 1942	22	0	0	37	0	7	66
May 26, 1942	<u>23</u>	<u>8</u>	<u>0</u>	<u>34</u>	<u>0</u>	<u>38</u>	<u>103</u>
Total shipments since January 1, 1941 to date *	2,393	168	168	2,576	114	1,888	7,307

* Total includes planes shipped in 1942 prior to March 17 which are not included in the weekly totals up to that date.

READING COPY OF SECRETARY'S STATEMENT
BEFORE JOINT COMMITTEE ON TAXATION, THURSDAY, MAY 28, 1942
8 pm
ON PROFITS LIMITATIONS

The very helpful interest in tax collection problems shown by the members of the Joint Committee on Internal Revenue Taxation, under the able leadership of your Chairman, Mr. Doughton, encourages me to appear before you to discuss an administrative matter.

I know that this Committee and the Congress are determined that no man and no corporation shall be permitted to make exorbitant profits out of the war effort. It is the responsibility of the Congress to draft legislation to achieve that purpose. It is our responsibility at the Treasury to use all the powers the Congress has given us to see that all taxes are fully, honestly, and justly collected.

It is our responsibility to see that by no form of trick or chicanery is any one taxpayer permitted to escape his just share and thus to throw unjust burdens on others.

I have come before this Committee tonight to tell you of some instances of what seem to me to be particularly unpardonable attempts to escape wartime taxation, and I should like to report what the Treasury is doing and intends to do to stop these practices. In every instance the method used by the taxpayer was to inflate expenses with the evident purpose of avoiding normal and excess profits taxes on corporation earnings.

The devices used included the payment of excessive salaries, the distribution of unearned bonuses and the payment of unreasonable sums for purported services to persons closely connected with the management of the companies involved.

It will be obvious to members of this Committee that these practices, if successful, would reduce the revenue of the Government, the revenue we need so urgently for fighting and winning the war.

We do not intend that this shall happen. We do not intend that any of these practices shall succeed. The Congress has already given power to the Treasury to deal with cases of this kind, and that power is being exercised.

The instances I shall mention to you were discovered as a result of speeding up our investigation of 1941 returns of corporations holding war contracts. Reports of the examination of thirty-one returns for 1941 are now available. Let me mention briefly seven cases illustrating the practices with which we have to deal.

Company A makes an important airplane part. This corporation is owned by one man who hired himself as its sales representative. His compensation in 1941 was one million six hundred and fifty-six thousand dollars. By consolidating these earnings with those of the corporation, we have blocked this obvious attempt to divert profits and we have increased the corporation's income tax by one million, one hundred and seventeen thousand dollars.

Company B makes steel. All stock in this corporation is held by three families. Excessive salaries were paid to officers who were also stockholders. The Revenue Agent has recommended disallowance of eighty-two thousand dollars in salaries, and the company has already agreed to ~~disallowance of fifty-eight thousand dollars.~~ ^{to}

Company C makes vital equipment for airplane pilots. This corporation paid thirty-one thousand, one hundred and four dollars in rent in one year to the wife of the president for using property which had cost her forty-five thousand, four hundred and twelve dollars.

A brother of the principal stockholder, without special training or ability, drew a salary of fifteen thousand dollars a year and a son and daughter, just out of school, got seven thousand five hundred dollars a year each.

Company D makes tools and dies. This company is owned by two brothers and their wives. It paid dividends of forty thousand dollars in 1940 and one hundred thousand dollars in 1941, while salaries totaling one hundred twenty-eight thousand dollars were paid in 1941 to the president, his wife and his brother.

Company E makes forgings. The stock is owned by three families.

From 1938 to 1941 the salaries of employees who were stockholders and relatives of stockholders increased five hundred and twenty-three percent. Excessive salaries for 1941 have been disallowed to the amount of five hundred sixty-eight thousand dollars.

Company F makes equipment for airplanes.

Three principal officers of this corporation took salaries of one hundred thousand dollars each and the corporation claimed it had set aside over five hundred seventy-five thousand dollars in bonuses. Salary and bonus payments totaling five hundred sixteen thousand dollars were found to be excessive.

Other disallowed deductions included sixteen thousand dollars paid for watches given to employees, fourteen thousand dollars for banquets and picnics, four thousand dollars for photographs taken at banquets and picnics, and one thousand nine hundred dollars for tickets to football games. Other important deficiencies were found in the tax return.

Company G makes a device important to aviation. This corporation is owned almost entirely by one man, his wife and his brother. The two men increased their salaries from twelve thousand dollars and fifteen thousand dollars in 1939 to seventy-two thousand dollars and ninety thousand dollars in 1941.

The royalty rate on the patent jointly held by them was increased, with the result that with expanded sales for war purposes, the royalties paid to them increase from eighty-seven thousand dollars in 1939 to one million, one hundred and seventy-nine thousand dollars in 1941.

You will note that I have not named any of the corporations or the individuals concerned. I leave it to this Committee to decide whether that should be done. Personally I am inclined to believe it would have a very wholesome effect.

Assistant Secretary Sullivan and Commissioner Helvering are here tonight to give you further details of the results of some of these investigations.

They stand ready to come before you from time to time and to report the results of further investigations now in progress.

It should be noted that these cases all deal with returns for 1941. It is of course true that all of the contracts for war work covered by these 1941 returns were signed before the United States entered the war and that nearly all the earnings represented in the tax-dodging devices attempted were pre-war earnings. But I think that changes the situation very little. An attempt to escape lawful taxes while we were actually at war would be only a slight degree blacker than an attempt to escape taxes which would pay for arming and equipping our Army and Navy when we stood in imminent danger of attack.

It may be that these instances are an isolated few and that not many more of the same kind will be found. I sincerely hope that will be the case. I am wholly confident that the great and overwhelming proportion of American corporations are too patriotic even to consider such practices.

We are taking two steps to detect and deal with the evils I have mentioned. In the first place, we are expediting examination of the tax returns and records of all corporations, beginning with those who have war contracts, to determine whether excessive expenses are being claimed. Ordinarily our investigation of returns filed for the year 1941 would not begin until July 1, 1942, and this work would continue through the fiscal year ending June 30, 1943.

Under present circumstances we can not afford to wait so long before acting. By speeding up our investigations we expect to check unlawful practices of this sort at an earlier stage.

In the second place, we are disallowing excessive expenditures which have the effect of reducing corporate tax liabilities. We are compelling the corporations to include such amounts in earnings, and at the same time we are requiring the recipient to pay full personal income taxes on the amounts received.

The disallowance of excessive expenditures does not represent a new procedure. The law and regulations permit the deduction only of ordinary and necessary business expenses for the purpose of determining profits.

In applying the law and regulations, the Bureau of Internal Revenue has often disallowed expenditures which seemed to lack sound business justification and which were, in effect, distributions of profits. Today, however, the problem has assumed major importance in view of the huge increases in income of a great number of corporations resulting from the war effort.

In presenting this problem to you, I am anxious to be as constructive as possible. It seems to me that the businessmen of this country are entitled to know not only the extent of our legal powers but also the standards that we have adopted in applying them.

Accordingly, it may be helpful if I outline the following general considerations that will guide us in examining expenses claimed in tax returns.

1. Salaries and Bonuses Paid to Officers and Employees.

Deductions claimed for greatly increased salaries and extraordinary bonuses paid to officers or employees will be disallowed unless the taxpayer proves that the payments are, in fact, for services actually rendered and are reasonable.

In determining whether the payments are reasonable, it will be assumed that reasonable compensation is only as much as would ordinarily be paid for like services by like enterprises under like circumstances.

The factors that will be considered in determining the reasonableness of such payments are the duties performed by the recipient, the character and amount of responsibility, the time devoted to the enterprise, and the peculiar ability or special talent of the particular officer or employee. Where the payments are to relatives or to shareholders, the taxpayer must show that family considerations have not influenced the amount paid and that the payments are not distributions of profits in disguise. Large profits attributable to causes entirely unrelated to the activities of the officers or employees, which are not unusual in these abnormal times, do not of themselves justify or warrant large salary payments.

2. Rents, Royalties and Other Payments to Shareholders.

Deductibility of rents, royalties or other payments to shareholders depends upon whether such charges are in fact fair and reasonable payments for the use of property and are not merely a device for distribution of profits. Any shareholder should be entitled only to a fair return on his investment in the property which he permits the corporation to use.

3. Payments to Profit Sharing or Pension Trusts.

The deductibility of payments to pension trusts is governed by section 23(p) of the Internal Revenue Code. If payments to such trusts are reasonable, their deduction will be allowed.

If the payments are unreasonable in amount, or if the trust is not created for the exclusive benefit of employees, or if it is a device to distribute profits to shareholders, the deductions will be disallowed. It is also our purpose to set up a barrier to deductions of large salaries, bonuses, or insurance premiums for officers under the guise of payments to a pension trust.

4. Payments for Repairs.

The deductibility for income tax purposes of costs of repairs depends upon whether the expenditure is actually for repairs, or is in fact a capital expenditure which should be added to capital investment or charged against reserve for depreciation, since the costs of repairs are deductible while capital expenditures are not.

We must guard against the tendency during high profit years to make extensive improvements and to charge the cost of such improvements against profits under the caption of repairs.

It will be our policy to scrutinize carefully the items claimed as deductions for expenditures for repairs. We shall disallow such deductions where it is not shown that the expenditures are in fact for repairs instead of for improvements or betterments which should be capitalized.

5. Expenses or Allowances Paid to Obtain Government Business, Including Fees Paid to Washington Representatives or for Other Professional Services.

Whether deductions for items of this class will be allowed depends upon whether they meet the test laid down in the Internal Revenue Code, that is, whether they are necessary and ordinary and reasonable. If such items are considered exorbitant or unreasonable, they will be disallowed as deductions. Many of the factors that apply in determining the deductibility of salaries and bonuses will apply also in determining the deductibility of items of this class. Particular attention will be given to deductions for payments which are against public policy, and all such deductions will be disallowed.

6. Amounts Paid For Advertising.

The test of whether expenditures for advertising are deductible is whether they are ordinary and necessary and bear a reasonable relation to the business activities in which the enterprise is engaged. This is not intended to exclude institutional advertising in reasonable amounts or good will advertising calculated to influence the buying habits of the public. If such expenditures are extravagant and out of proportion to the size of the company or to the amount of its advertising budget in the past, or if they are not directed to public patronage which might reasonably be expected in the future, such payments will be disallowed as deductions.

With these standards as our guideposts, we are progressing as fast as practicable with our investigation of the 1941 returns. Those who are engaged in this work must, of course, think not only of the best interests of the Government but also of the need of being completely fair to the taxpayers. The Committee, the Congress and the country are entitled to know that the unscrupulous and selfish few are not being allowed to distort their tax returns so as to escape their fair share of the costs of the war. I can assure the Committee of this: that nothing is being left undone which will expedite our work.

If we find that our existing powers are not adequate to deal with the evil I have been discussing, I shall not hesitate to come before the appropriate committee to ask for any additional authority that may be needed.

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FOR RELEASE ON DELIVERY

Statement of Secretary Morgenthau
before the
Joint Committee on Internal Revenue Taxation
Thursday, May 28, 1942.

The very helpful interest in tax collection problems shown by the members of the Joint Committee on Internal Revenue Taxation, under the able leadership of your Chairman, Mr. Doughton, encourages me to appear before you to discuss an administrative matter.

I know that this Committee and the Congress are determined that no man and no corporation shall be permitted to make exorbitant profits out of the war effort. It is the responsibility of the Congress to draft legislation to achieve that purpose. It is our responsibility at the Treasury to use all the powers the Congress has given us to see that all taxes are fully, honestly and justly collected. It is our responsibility to see that by no form of trick or chicanery is any one taxpayer permitted to escape his just share and thus to throw unjust burdens on others.

I have come before this Committee tonight to tell you of some instances of what seem to me to be particularly unpardonable attempts to escape wartime taxation, and I should like to report what the Treasury is doing and intends to do to stop these practices. In every instance the method used by the taxpayer was to inflate expenses with the evident purpose of avoiding normal and excess profits taxes on corporation earnings. The devices used included the payment of excessive salaries, the distribution of unearned bonuses and the payment of unreasonable sums for purported services to persons closely connected with the management of the companies involved.

It will be obvious to members of this Committee that these practices, if successful, would reduce the revenue of the Government, the revenue we need so urgently for fighting and winning the war.

We do not intend that this shall happen. We do not intend that any of these practices shall succeed. The Congress has already given power to the Treasury to deal with cases of this kind, and that power is being exercised.

The instances I shall mention to you were discovered as a result of speeding up our investigation of 1941 returns of corporations holding war contracts. Reports of the examination

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of 31 returns for 1941 are now available. Let me mention briefly seven cases illustrating the practices with which we have to deal.

Company A makes an important airplane part. This corporation is owned by one man who hired himself as its sales representative. His compensation in 1941 was \$1,656,000. By consolidating these earnings with those of the corporation, we have blocked this obvious attempt to divert profits and we have increased the corporation's income tax by \$1,117,000.

Company B makes steel. All stock in this corporation is held by three families. Excessive salaries were paid to officers who were also stockholders. The Revenue Agent has recommended disallowance of \$82,000 in salaries, and the company has already agreed to a disallowance of \$58,000.

Company C makes vital equipment for airplane pilots. This corporation paid \$31,104 in rent in one year to the wife of the president for using property which had cost her \$45,412. A brother of the principal stockholder, without special training or ability, drew a salary of \$15,000 a year and a son and daughter, just out of school, got \$7,500 a year each.

Company D makes tools and dies. This company is owned by two brothers and their wives. It paid dividends of \$40,000 in 1940 and \$100,000 in 1941, while salaries totaling \$128,000 were paid in 1941 to the president, his wife and his brother.

Company E makes forgings. The stock is owned by three families. From 1938 to 1941 the salaries of employees who were stockholders and relatives of stockholders increased 523 percent. Excessive salaries for 1941 have been disallowed to the amount of \$568,000.

Company F makes equipment for airplanes. Three principal officers of this corporation took salaries of \$100,000 each and the corporation claimed it had set aside over \$575,000 in bonuses. Salary and bonus payments totalling \$516,000 were found to be excessive. Other disallowed deductions included \$16,000 paid for watches given to employees, \$14,000 for banquets and picnics, \$4,000 for photographs taken at banquets and picnics, and \$1,900 for tickets to football games. Other important deficiencies were found in the tax return.

Company G makes a device important to aviation. This corporation is owned almost entirely by one man, his wife and his brother. The two men increased their salaries from \$12,000 and \$15,000 in 1939 to \$72,000 and \$90,000 in 1941. The royalty rate on the patent jointly held by them was increased, with the result that with expanded sales for war purposes, the royalties paid to them increased from \$87,000 in 1939 to \$1,179,000 in 1941.

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You will note that I have not named any of the corporations or the individuals concerned. I leave it to this Committee to decide whether that should be done. Personally I am inclined to believe it would have a very wholesome effect.

Assistant Secretary Sullivan and Commissioner Helvering are here tonight to give you further details of the results of some of these investigations. They stand ready to come before you from time to time and to report the results of further investigations now in progress.

It should be noted that these cases all deal with returns for 1941. It is of course true that all of the contracts for war work covered by these 1941 returns were signed before the United States entered the war and that nearly all the earnings represented in the tax-dodging devices attempted were pre-war earnings. But I think that changes the situation very little. An attempt to escape lawful taxes while we were actually at war would be only a slight degree blacker than an attempt to escape taxes which would pay for arming and equipping our Army and Navy when we stood in imminent danger of attack.

It may be that these instances are an isolated few and that not many more of the same kind will be found. I sincerely hope that will be the case. I am wholly confident that the great and overwhelming proportion of American corporations are too patriotic even to consider such practices.

We are taking two steps to detect and deal with the evils I have mentioned. In the first place, we are expediting examination of the tax returns and records of all corporations, beginning with those who have war contracts, to determine whether excessive expenses are being claimed. Ordinarily our investigation of returns filed for the year 1941 would not begin until July 1, 1942, and this work would continue through the fiscal year ending June 30, 1943. Under present circumstances we cannot afford to wait so long before acting. By speeding up our investigations we expect to check unlawful practices of this sort at an earlier stage.

In the second place, we are disallowing excessive expenditures which have the effect of reducing corporate tax liabilities. We are compelling the corporations to include such amounts in earnings, and at the same time we are requiring the recipient to pay full personal income taxes on the amounts received.

The disallowance of excessive expenditures does not represent a new procedure. The law and regulations permit the deduction only of ordinary and necessary business expenses for the purpose of determining profits. In applying the law and

regulations, the Bureau of Internal Revenue has often disallowed expenditures which seemed to lack sound business justification and which were, in effect, distributions of profits. Today, however, the problem has assumed major importance in view of the huge increases in income of a great number of corporations resulting from the war effort.

In presenting this problem to you, I am anxious to be as constructive as possible. It seems to me that the businessmen of this country are entitled to know not only the extent of our legal powers but also the standards that we have adopted in applying them. Accordingly, it may be helpful if I outline the following general considerations that will guide us in examining expenses claimed in tax returns.

1. Salaries and Bonuses Paid to Officers and Employees.

Deductions claimed for greatly increased salaries and extraordinary bonuses paid to officers or employees will be disallowed unless the taxpayer proves that the payments are, in fact, for services actually rendered and are reasonable.

In determining whether the payments are reasonable, it will be assumed that reasonable compensation is only as much as would ordinarily be paid for like services by like enterprises under like circumstances. The factors that will be considered in determining the reasonableness of such payments are the duties performed by the recipient, the character and amount of responsibility, the time devoted to the enterprise, and the peculiar ability or special talent of the particular officer or employee. Where the payments are to relatives or to shareholders, the taxpayer must show that family considerations have not influenced the amount paid and that the payments are not distributions of profits in disguise. Large profits attributable to causes entirely unrelated to the activities of the officers or employees, which are not unusual in these abnormal times, do not of themselves justify or warrant large salary payments.

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- 6 -

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JUN 11 1942
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10 EAST 40th STREET, NEW YORK

May 28th, 1942.

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

Dear Mr. Morgenthau:

I was extremely happy to have done the program and I think that the "Battle Hymn" is both beautiful and significant.

I was sorry to have missed seeing you at the broadcast and I hope it can be made up very soon. I was happy to have seen and appeared with Mrs. Morgenthau who has encouraged me so many times during my career.

Thanks to you and Mrs. Morgenthau for your kind expressions.

Cordially,

Paul Robeson

PR:B

May 28, 1942.

Dear Miss Thompson:

I have been very glad to receive your letter of May 19, sent at Mrs. Roosevelt's suggestion, which contained a letter from Meyer Davis, the well-known orchestra leader, regarding the use of more music in connection with the War Program.

The Office of Motion Pictures and Special Events of the War Savings Staff of the Treasury has been much interested in this suggestion from Mr. Davis, and is writing him to discuss further developments of his suggestion.

Sincerely,

(Signed) H. Morgenthau, Jr.

Miss Malvina C. Thompson,
The White House,
Washington, D. C.

NMC:dma

File M.M.C.

May 28, 1942

Meyer Davis, Esq.
225 West Fifty-Seventh Street
New York, New York

My dear Mr. Davis:

Mrs. Roosevelt duly received your letter of May 13 about a greater use of music in the present War Program, and sent it to the Secretary of the Treasury for consideration. Secretary Morgenthau has referred it to me.

The War Savings Staff is deeply interested in this fine suggestion. We have an Office of Motion Pictures and Special Events, under the able direction of Carleton Duffus. Mr. Duffus is deeply interested in your suggestions, and knowing you to be a seasoned leader in the musical field, wishes that you would write him in detail your suggestions as to how this idea could be put into effect.

I can assure you that any suggestion you make will be most gratefully received.

Yours sincerely,

James L. Houghteling
Director
National Organizations Division

JLH/hb

Handwritten: 166

THE WHITE HOUSE
WASHINGTON

May 19, 1942

Dear Mr. Secretary:

Mrs. Roosevelt asks if you could use the suggestion made by Mr. Meyer Davis in his letter of May 13th enclosed.

Very sincerely yours,

Malvina C. Thompson
Secretary to
Mrs. Roosevelt

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

*Office of Motion Pictures and
Special Writings
Carlton Duffus*

C O P Y

MEYER DAVIS' MUSIC
Orchestras Extraordinary

May 13, 1942

Mrs. Franklin D. Roosevelt
The White House
Washington, D. C.

Dear Mrs. Roosevelt,

I should like to offer an idea for your consideration and support. It is to utilize the talents of thousands of professional musicians to play patriotic and other inspiring music on the streets of the cities in the United States.

I cannot think of a greater stimulus to patriotic giving than that of bands playing the "Stars and Stripes Forever" ... "Anchors Aweigh" ... "Marines' Hymn" ... and "Caissons Go Rolling Along" unexpectedly marching by. Many a hand would reach in a pocket to split a pay check with Uncle Sam.

Through the agencies of the Musicians' Union and the many other patriotic bodies, I believe a plan could be evolved whereby unemployed musicians could be compensated for this work.

Music has always been a potent factor in war. The martial memories of our victorious past, together with the tender sentiment regarding our boys now in active service, make music an integral part of our home front. Musicians want to help and so do I; and I'd like to lead the first street march should this plan go through.

I hope that you may be able to give this idea your support.

Most respectfully,

Meyer Davis

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE May 28, 1942

TO Secretary Morgenthau

FROM Mr. Haas

Subject: Number of days it takes to receive a war savings bond issued by a Federal Reserve Bank or by a corporation issuing agent.

On Friday, May 22, the Federal Reserve Banks again made a sample survey to determine the number of days it takes a person to receive a war savings bond (1) issued by the Federal Reserve Bank, or (2) issued by a corporation which is qualified as an issuing agent. The results of the first part of this survey and a comparison with the survey made last week are shown in Table 1 attached to this memorandum. The results of the second part of this survey are shown in Table 2 attached. The major items noted are similar to those noted last week. They are the following:

- (1) A person buying a war savings bond by sending a check to the Federal Reserve Bank through the mails normally waits a week before he receives his bond. Two of these days are consumed by the movement of the mails; three more of these days are required by the Federal Reserve Bank to collect the check; and one of these days is a Sunday on which no business is transacted.
- (2) At peak periods -- particularly those when a large volume of applications are on hand for companies whose employees are purchasing under the payroll savings plan -- it takes a person 10 to 15 days to obtain his bond. The three Federal Reserve Banks standing at the top of Table 1 attached were apparently in the midst of such peak periods on Friday, May 15, but these peak periods had passed by Friday, May 22.
- (3) A few corporation issuing agents are taking 20 to 30 days to deliver bonds purchased by employees participating in the payroll savings plan (Table 2). Most corporations are able to deliver bonds purchased by such employees within 2 weeks after payment has been completed, however, and a few corporations are able to deliver the bonds the very same day the payments are completed.

Table 1

Approximate number of days it takes a person
to receive a war savings bond issued by a
Federal Reserve Bank 1/

Federal Reserve Bank	: Survey made : May 15, 1942	: Survey made : May 22, 1942
Richmond	15	7
Philadelphia	10	8
San Francisco	10	7
Chicago	8	9
Dallas	8	3
Boston	8	7
New York	7	6
Kansas City	6	6
Cleveland	5	5
Minneapolis	4	4
Atlanta	4	4
St. Louis	4	5

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

May 28, 1942.

1/ Allows 2 days for period in the mails.

Table 2

Longest period of time it takes an employee of a selected group of corporations to receive his war savings bond purchased under the payroll savings plan and issued by his employer

(On the basis of the survey made by the Federal Reserve Banks on May 22, 1942)

Name of company and location	: Maximum num-: : ber of days : : to receive : : bond :	Explanation submitted by the Federal Reserve Banks
1. A corporation selected by Federal Reserve Bank of San Francisco	30	Usual time from 20 to 30 days.
2. Armour & Co., Chicago, Ill.	28	Bonds in group selected covered orders from the Spokane, Washington, office of this company. Part of the delay was due to mail movements.
3. Standard Oil Co. of Indiana, Chicago, Ill.	27	Bonds in group selected covered Missouri offices of this company. Part of the delay was due to mail movements.
4. Western Union Telegraph Co., Richmond, Va.	22	
5. American Brass Co., Boston, Mass.	21	Company is getting its issuing procedure better organized and is speeding up the issuance of the bonds.
6. Southwestern Bell Telephone Co., St. Louis, Mo.	21	
7. A corporation selected by the Federal Reserve Bank of Atlanta.	20	A complete audit of the payroll is necessary before bonds may be issued.
8. Stewart-Warner Corp., Chicago, Ill.	13	
9. Atlantic Steel Castings Co., Chester, Pa.	9	Company expects to organize its procedure so that it will be able to deliver bonds with the pay from which the last deduction is made.
10. St. Louis Independent Packing Co., St. Louis, Mo.	9	
11. Theo. Hamm Brewing Co., St. Paul, Minn.	9	
12. Brown & Bigelow, St. Paul, Minn.	8	

(Continued)

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

May 26, 1942.

Table 2

Longest period of time it takes an employee of a selected group of corporations to receive his war savings bond purchased under the payroll savings plan and issued by his employer

(On the basis of the survey made by the Federal Reserve Banks on May 22, 1942)

(Continued - 2)

Name of company and location	: Maximum num-: : ber of days : : to receive : : bond :	Explanation submitted by the Federal Reserve Banks
13. United-Carr Fastener Corp., Cambridge, Mass.	7	Bonds paid for on one pay day are delivered next pay day.
14. Century Electric Co., St. Louis, Mo.	5	
15. Radio Condenser Co., Camden, N. J.	4	
16. John Wanamaker, Philadelphia, Pa.	4	
17. A corporation selected by the Federal Reserve Bank of New York.	3	
18. A corporation selected by the Federal Reserve Bank of Atlanta.	3	
19. Potter and Johnston Machine Co., Pawtucket, R.I.	1	
20. A corporation selected by the Federal Reserve Bank of Atlanta.	1	
21. Sears Roebuck & Co., Minneapolis, Minn.	1	
22. A corporation selected by the Federal Reserve Bank of New York.	0	Bonds delivered day payment is completed
23. Ditto.	0	Ditto.

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

May 26, 1942.

Sales of United States Savings Bonds
From May 1 through May 27, 1942
Compared with Sales Quota for Same Period
(At issue price in millions of dollars)

CONFIDENTIAL

Date	Series E				Series F and G				Total			
	Actual Sales		Quota,	Sales	Actual Sales		Quota,	Sales	Actual Sales		Quota,	Sales
	May 1	May 1	to Date	to Date	May 1	May 1	to Date	to Date	May 1	May 1	to Date	to Date
Daily	to	to	as % of	Daily	to	to	as % of	Daily	to	to	as % of	
	Date	Date	Quota		Date	Date*	Quota		Date	Date	Quota	
1	\$ 12.7	\$ 12.7	\$ 14.0	90.7%	\$ 7.5	\$ 7.5	\$ 12.0	60.8%	\$ 20.0	\$ 20.0	\$ 26.0	76.9%
2	11.6	24.3	25.7	94.6	7.9	15.2	21.4	71.0	19.4	39.4	47.1	83.7
4	22.3	46.5	47.8	97.3	10.3	25.5	39.4	64.7	32.6	72.0	87.2	82.6
5	8.9	55.5	57.8	96.0	7.6	33.1	49.3	67.1	16.6	88.6	107.1	82.7
6	18.4	73.8	70.5	104.7	15.6	48.8	64.9	75.2	34.0	122.6	135.4	90.5
7	23.2	97.0	84.0	115.5	12.1	60.8	76.9	79.1	35.3	157.9	160.9	98.1
8	17.2	114.2	98.0	116.5	6.4	67.2	86.1	78.0	23.6	181.4	184.1	98.5
9	14.5	128.7	109.7	117.3	5.6	72.8	92.6	78.6	20.0	201.5	202.3	99.6
11	23.3	152.0	131.8	115.3	8.1	80.8	104.2	77.5	31.3	232.8	236.0	98.6
12	9.4	161.3	141.8	113.8	4.6	85.4	110.6	77.2	14.0	246.8	252.4	97.8
13	15.8	177.1	154.5	114.6	9.0	94.4	120.8	78.1	24.8	271.5	275.3	98.6
14	16.9	194.0	168.0	115.5	7.7	102.1	129.3	79.0	24.6	296.2	297.3	99.6
15	14.9	208.9	182.0	114.8	6.8	108.9	136.5	79.8	21.7	317.9	318.5	99.8
16	14.3	223.2	193.7	115.2	5.2	114.1	142.1	80.3	19.5	337.4	335.8	100.5
18	24.3	247.5	215.8	114.7	9.4	123.5	153.0	80.7	33.7	371.1	368.8	100.6
19	9.8	257.4	225.8	114.0	4.2	127.7	159.2	80.2	14.0	385.1	385.0	100.0
20	13.7	271.1	238.5	113.7	11.2	138.9	169.6	81.9	24.9	410.0	408.1	100.5
21	19.4	290.5	252.0	115.3	10.6	149.5	178.4	83.8	30.0	440.0	430.4	102.2
22	19.1	309.6	266.0	116.4	7.1	156.6	186.1	84.1	26.2	466.2	452.1	103.1
23	14.1	323.7	277.7	116.6	4.8	161.4	192.3	83.9	18.9	485.1	470.0	103.2
25	23.8	347.5	299.8	115.9	9.9	171.3	204.9	83.6	33.7	518.8	504.7	102.8
26	13.1	360.6	309.8	116.4	7.9	179.2	212.5	84.3	20.9	539.8	522.3	103.4
27	15.1	375.7	322.5	116.5	10.1	189.3	226.2	83.7	25.2	565.0	548.7	103.0
28			336.0				238.7				574.7	
29			350.0				250.0				600.0	

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

May 28, 1942.

Source: Actual sales figures are deposits with the Treasurer of the United States on account of proceeds of sales of United States savings bonds. Figures have been rounded and will not necessarily add to totals.

* Takes into account both the daily trend during the week and the monthly trend during the month.

Sales of United States Savings Bonds
From May 1 through May 27, 1942
Compared with Sales Quota for Same Period
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CONFIDENTIAL

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2	11.6	24.3	25.7	94.6	7.9	15.2	16.0	95.0	19.4	39.4	41.7	94.5
4	22.3	46.5	47.8	97.3	10.3	25.5	29.5	86.4	32.6	72.0	77.3	93.1
5	8.9	55.5	57.8	96.0	7.6	33.1	37.1	89.2	16.6	88.6	94.9	93.4
6	18.4	73.8	70.5	104.7	15.6	48.8	49.8	98.0	34.0	122.6	120.3	101.9
7	23.2	97.0	84.0	115.5	12.1	60.8	60.3	100.8	35.3	157.9	144.3	109.4
8	17.2	114.2	98.0	116.5	6.4	67.2	69.3	97.0	23.6	181.4	167.3	108.4
9	14.5	128.7	109.7	117.3	5.6	72.8	76.3	95.4	20.0	201.5	186.0	108.3
11	23.3	152.0	131.8	115.3	8.1	80.8	89.8	90.0	31.3	232.8	221.6	105.1
12	9.4	161.3	141.8	113.8	4.6	85.4	97.4	87.7	14.0	246.8	239.2	103.2
13	15.8	177.1	154.5	114.6	9.0	94.4	110.1	85.7	24.8	271.5	264.6	102.6
14	16.9	194.0	168.0	115.5	7.7	102.1	120.6	84.7	24.6	296.2	288.6	102.6
15	14.9	208.9	182.0	114.8	6.8	108.9	129.6	84.0	21.7	317.9	311.6	102.0
16	14.3	223.2	193.7	115.2	5.2	114.1	136.6	83.5	19.5	337.4	330.3	102.1
18	24.3	247.5	215.8	114.7	9.4	123.5	150.1	82.3	33.7	371.1	365.9	101.4
19	9.8	257.4	225.8	114.0	4.2	127.7	157.7	81.0	14.0	385.1	383.5	100.4
20	13.7	271.1	238.5	113.7	11.2	138.9	170.3	81.6	24.9	410.0	408.8	100.3
21	19.4	290.5	252.0	115.3	10.6	149.5	180.8	82.7	30.0	440.0	432.8	101.7
22	19.1	309.6	266.0	116.4	7.1	156.6	189.8	82.5	26.2	466.2	455.8	102.3
23	14.1	323.7	277.7	116.6	4.8	161.4	196.8	82.0	18.9	485.1	474.5	102.2
25	23.8	347.5	299.8	115.9	9.9	171.3	210.3	81.5	33.7	518.8	510.1	101.7
26	13.1	360.6	309.8	116.4	7.9	179.2	217.9	82.2	20.9	539.8	527.7	102.3
27	15.1	375.7	322.5	116.5	10.1	189.3	230.5	82.1	25.2	565.0	553.0	102.2
28			336.0				241.0				577.0	
29			350.0				250.0				600.0	

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

May 28, 1942.

Source: Actual sales figures are deposits with the Treasurer of the United States on account of proceeds of sales of United States savings bonds. Figures have been rounded and will not necessarily add to totals.

* Takes into account daily trend within the week, but does not take into account the trend by weeks during the month.

being taken to Farm
by Wye

5-28-42

Secretary Morgenthau

(Signed) D. W. BELL, Bell and Mr. Haas

Subject: The proposed increase in the Treasury bill program.

In response to your request, we have prepared this memorandum on the pros and cons for increasing the bill program together with a review of the recent situation with respect to excess reserves.

It is generally agreed among members of the Treasury staff that it would be desirable to take steps to increase excess reserves of member banks. As of May 20, excess reserves aggregated \$524 millions in New York City and \$2,041 millions outside New York City, or a total of \$2,565 millions. The New York figure was at the lowest level it has ever reached in recent years, according to the Wednesday series on excess reserves, and compares with a figure of \$1,345 millions on October 29, just before the increase in reserve requirements went into effect last fall, and with a figure of \$935 millions on March 18, the day before the date picked for the benchmark establishing a pattern of yields for the Government market.

For banks outside New York City, the current figure on excess reserves is not very much different from the level of recent months, but it is reduced about \$1,200 millions from the level on October 29 and about \$600 millions from the level just after the increase in reserve requirements last fall. Total excess reserves for the country have declined about \$850 millions since the week after reserve requirements were increased, a figure which, incidentally, is approximately 75 percent of the increase since that time in money in circulation -- an important factor in drawing down excess reserves.

The Federal Reserve System desires that no change be made with respect to reserve requirements at this time, and prefers to wait until legislation may be enacted to make it possible to change the reserve requirements of member banks

Secretary Morgenthau - 2

in central reserve cities without necessarily making a change in the requirements for member banks in reserve cities. Chairman Keeles expects to seek such legislation in the near future, and the Treasury has indicated its approval of the idea.

Meanwhile, it is desirable that some means be taken to provide for easing the reserve situation at this time, and the best approach would seem to be through open-market purchases by the Federal Open Market Account. A program involving purchases of longer-term Treasury securities to increase excess reserves would not be desirable since it would tend to drive prices up from the March 19 level. At a meeting between representatives of the Treasury and of the Federal Reserve System last week, it was agreed that it would be desirable to tackle the problem by further enlarging the Treasury bill program at once. It was suggested that weekly offerings of bills be increased by \$100 millions from the present level of \$250 millions. This proposal has several advantages:

1. With the bill rate posted at $\frac{3}{8}$ of 1 percent, an increase in bill offerings would probably result in some increases in bill purchases by the Federal Open Market Account, thereby providing increases in excess reserves. The amount involved might be large or small, depending on the demand for bills from the commercial banks. In order to assure that it would be significant, however, Dr. Stewart made the excellent suggestion that the Federal Reserve might buy a minimum amount of \$50 millions of the increase each week. This amount would approximately offset decreases in excess reserves which have been occurring as a result of increases in money in circulation.
2. An increase in bills would provide greater fluidity to the money market and would make for more effective utilization of present excess reserves. The Federal Reserve System is planning to conduct a selling campaign to induce commercial banks with large excess reserves to convert them in part into investments in Treasury bills. With the posted bill rate, any individual bank would be well advised to take bills and thus earn something like $\frac{3}{8}$ of 1 percent on its funds, since

Secretary Morgenthau - 3

the bills may be turned over at any time to the Federal Open Market Account whenever the bank deems it desirable. Meanwhile, there would be some tendency for excess reserves to flow to other banks whose reserve situation may be tight.

3. Even if the reserve situation should not be improved through the enlarged Treasury bill program, the Treasury would still have gained in that it would have sold securities at a low interest rate, and the issues would be of the type which bankers are anxious to get. Some diminution of excess reserves might actually occur in this case, but this would not be serious, since any weakness which might follow in Treasury notes and bonds as a result could be offset by Federal Reserve purchases of such issues, and thus provide increases in excess reserves in that manner without driving up market prices.

The only apparent disadvantage in increasing the bill program is that this area has been envisaged to some extent as something which should be held open to take care of a rainy day. This disadvantage is not important, however, since the rainy day situation can easily be taken care of by operations to increase excess reserves at critical times, so that banks could again absorb greater amounts of Treasury bills.

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APR 21 1950

Division of the Federal Reserve
Treasury Department

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Treasury Department
Division of Monetary Research

Date..... May 28, 1942.....19

To: secretary Morgenthau

From: Mr. White

The Stabilization Fund today purchased 1,000,000 Swiss francs from the Central Bank of Turkey at a rate of 23.26 cents. These francs were acquired at this very attractive rate in accordance with the authorization you granted a few weeks ago when it appeared that the Fund might be able to buy some francs from the Bank of Portugal. We were unsuccessful in that attempt.

The Swiss francs will be used (a) to supply the needs of our Government; (b) to supply the needs of friendly governments in this hemisphere and among the United Nations; (c) possibly to make occasional sales in the market if it is felt that a lower market rate for Swiss francs is in the public interest.

In view of the low rate at which we acquired the francs there will be no difficulty in disposing of them without loss. For example, last Friday, the Federal Reserve Bank had to pay 27.50 cents to obtain 500,000 Swiss francs for the Royal Norwegian Government.

MR. WHITE
Branch 2058 - Room 214½

TREASURY DEPARTMENT
INTER OFFICE COMMUNICATION

DATE MAY 28 1942

TO Secretary Morgenthau
FROM Mr. Foley

For your information

Relative to your work as a member of the Joint Committee on
Reduction of Nonessential Federal Expenditures.

The Senate Committee on Finance on Thursday, May 28, 1942, will consider H.R. 4 and H.R. 4845, and other veterans pension measures. H.R. 4 and H.R. 4845 were considered by a subcommittee and reported in January without recommendation to the full committee. First year costs are estimated to involve more than \$33,000,000.

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TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE MAY 28 1942

TO Secretary Morgenthau
FROM Mr. Foley

Attached is the fifth report on pending legislation prepared in Mr. Bernard's office to assist you in your work as a member of the Joint Senate and House Committee on economy.

SMFH

Report as of May 25, 1942 on Pending Legislation
Wherein There is Possibility of Non-Defense Economies

Since the last report, as of March 31, 1942, there has been no major change of interest within the scope of these reports.

The Senate Committee on Finance on Thursday, May 28, will consider H.R. 4 and H.R. 4845, and other veterans pension measures. H.R. 4 and H.R. 4845 were considered by a subcommittee and reported in January without recommendation to the full committee. First year costs are estimated to involve more than \$33,000,000. Other pension bills in the committees of both Houses are not receiving any particular action.

The situation as regards H.R. 5993, the Omnibus Rivers and Harbors bill, and H.R. 6724, Representative Dondero's substitute Rivers and Harbors bill including only thirty-eight projects, has not changed. However, H.R. 6999, authorizing a \$144,000,000 appropriation for construction of pipe line and navigable barge canal across Florida, and improvement of the Intracoastal Waterway between Florida and Mexico, was introduced April 27, 1942 by Representative Mansfield, and on May 25, 1942 was reported by the House Committee on Rivers and Harbors and is now pending before the House.

- 2 -

On May 19, 1942 Representative Peterson, for the Committee on Merchant Marine and Fisheries, reported on S. 1481, pension for workers on the Panama Canal. The report indicates that previous estimates of costs may be too high. The Committee estimates that first year cost will be between \$500,000 and \$750,000.

Farm Financing Legislation

Two bills designed to extend for two years the reduced rates of interest on Federal land bank and Land Bank Commissioner loans have been reported by the Committees. H.R. 6315 was reported by the House Committee on Agriculture on May 18, 1942; S. 2544 was reported by the Senate Committee on Banking and Currency on May 20, 1942. The Senate bill also provides for the reduced rate of interest in sales contracts. As noted in our previous reports, the Treasury, under present law, is obligated to make up the difference to the Federal land banks between the contract rate and the statutory rate on loans.

Other bills on this same problem, including S. 2290, S. 2025, S. 2529, H.R. 7072, and H.R. 7080, are inactively pending in their respective committees. The House Committee on Agriculture has as yet taken no action on H.R. 7050, "Perpetual Farm Parity Act of 1942" introduced May 11, 1942 by

- 3 -

Representative Coffee of Nebraska. In addition to establishing a parity formula this bill, under section 8, would allocate to the Commodity Credit Corporation all customs duties and excise taxes collected on the entry of farm products (present law in U.S.C., 1940 ed., title 7, section 612c allocates 30% of all duties for similar purposes).

H.R. 7091 "Farm Credit Act of 1942" which involves a comprehensive attack upon the farm financing situation, was introduced May 14, 1942 by Chairman Fulmer of the House Committee on Agriculture and has been ordered reported by that Committee. The report is now being prepared. This bill includes provision in section 7(d) for Treasury reimbursement of interest lost by reason of change in interest rates according to the formula of the bill. Section 8(a) provides for United States guaranty of principal and interest of Federal farm loan bonds, and section 11(a) declares policy to be against securing deficiency judgments in case of good faith efforts to retire the debt.

Life Insurance for Military and Naval Personnel

Certain additional bills have been introduced providing for life insurance without cost, or at reduced cost, to persons in the active military or naval service. S. 2543 was introduced by Senator George May 19, 1942, and S. 2550 was introduced

- 4 -

by Senator Clark on May 21, 1942. Both bills were referred to the Committee on Finance. H.R. 7085, providing for National Service Life Insurance and waiver of premiums on certain insurance, was introduced May 12, 1942 by Representative Hartley and referred to the Committee on Ways and Means. No particular action has been taken on these bills nor on the other similar measures mentioned in previous reports. H.R. 7029, which was introduced by Representative Sparkman on April 30, 1942 and referred to the House Committee on Military Affairs, contains certain provisions relative to insurance as a part of amendments felt to be necessary to the Soldiers' and Sailors' Civil Relief Act of 1940.

Extension of Employees' Compensation Act

H.R. 6917 provides extension of employees' compensation to members of fire departments injured in the performance of duty on property controlled by the United States if the firemen are not covered by state or other compensation act. The bill was introduced April 13, 1942 by Representative Beiter and referred to the House Committee on the Judiciary. H.R. 7042, providing coverage of civilian defense workers, was introduced May 5, 1942 by Representative Celler and was referred to the House Committee on the Judiciary. No action has been taken on either bill.

- 5 -

It should be pointed out that a provision somewhat similar to those of the latter bill was deleted from the Second War Powers Bill.

Miscellaneous other bills.

Note: Except as otherwise indicated the Committees have taken no action (other than routine reference to a Department) and do not presently contemplate any on the bills following:

Number: S. 2450

Title: "To authorize the President to acquire a stockpile of motor vehicles and parts and equipment therefor for national defense purposes."

Features: This bill authorizes an appropriation not to exceed \$5,000,000,000 to enable the President to acquire motor vehicles, parts and equipment for national defense purposes.

Status: Introduced by Senator Downey April 16, 1942; referred to the Committee on Military Affairs.

Number: S. 2475

Title: "To provide reimbursement for the loss of taxes on certain real property acquired by the United States for military or naval purposes."

- 6 -

Features: Provides that payment shall be made to reimburse towns and villages in the United States for (1) loss of revenue from taxes, and (2) loss or impairment of value to municipal improvement, as a result of acquisition by or on behalf of the United States for general military or naval purposes since January 1, 1940.

Status: Introduced April 23, 1942 by Senator Aiken; referred to Committee on Military Affairs.

Number: S. 2511 and H.R. 7047

Title: "Conferring jurisdiction upon the Court of Claims to hear, determine, and render judgment upon claims of Indians of the Northern Indian Confederacy, and for other purposes."

Features: Confers jurisdiction upon the Court of Claims to hear and render judgment on claims of Indians whose tribes occupied areas in the Northwest Territory; claims based on alleged denial of Indian rights, misappropriations of Indian funds, etc. There is nothing to indicate the probable cost of this bill, but it could be enormous. Section 12, however, provides "That if the amount of any judgment so recovered for any of the Indians under this Act shall exceed \$5,000,000 the Secretary of the Treasury [is authorized to pay in installments]".

- 7 -

Status: S. 2511 was introduced May 6, 1942 by Senator Shipstead; referred to the Committee on Indian Affairs. Committee anticipates no action this session.

H.R. 7047 was introduced May 5, 1942 by Representative Knutson; referred to the Committee on Indian Affairs.

Number: S. 2540

Title: "Authorizing and directing the Reconstruction Finance Corporation to create a subsidiary corporation to be known as the War Distress Finance Corporation, to deal with cases of business distress and financial hardship attributable to the war and causes related thereto, and for other purposes."

Features: War Distress Finance Corporation to have \$500,000,000 capital to relieve financial distress attributable to the war "including the refinancing of obligations on homes, businesses, or other obligations which are in default * * * on account of conditions fairly attributable to the war".

Status: Introduced May 18, 1942 by Senator Pepper; referred to the Committee on Banking and Currency.

Number: S. 2550

Title: "To provide that monthly payments of yearly renewable term or automatic, or National Service Life Insurance shall not

- 8 -

serve to reduce amounts of compensation or pension payable under existing compensation or pension laws."

Features: Title is fully explanatory.

Status: Introduced May 21, 1942 by Senator Clark; referred to Committee on Finance.

Number: H.R. 6897

Title: "To provide for the dollar-for-dollar matching by the United States of savings by enlisted men in the armed forces through the sale of Soldiers, Sailors, and Marines Savings bonds, and for other purposes."

Features: Directs to the Secretary that the Secretary of the Treasury issue a special Soldiers, Sailors, and Marines Savings bond to be purchased by deduction from credit accounts for enlisted men which accounts are composed of pay deductions matched dollar for dollar by Federal contribution. Bonds are to bear no interest and shall be due and payable at the end of service or the conclusion of present wars, whichever is later.

Status: Introduced April 2, 1942 by Representative Voorhis; referred to the Committee on Ways and Means.

Number: H.R. 6903

Title: "Providing for taxation by the States and their political subdivisions of certain real property acquired for

- 9 -

military purposes."

Features: Providing all real property in continental United States hereafter acquired for general military purposes together with improvements thereon shall remain subject to taxation by the state and political subdivision in which it is located to the same extent as other real property is taxed, unless the power of taxation is waived.

Status: Introduced April 6, 1942 by Representative Mott; referred to the Committee on the Public Lands.

Number: H.R. 6960

Title: "For the compensation of property owners in territory to be taken for bombing and target ranges."

Features: Provides for reimbursement of private interests for the taking of property or property rights in territory taken for use as bombing or target ranges.

Status: Introduced April 20, 1942 by Representative Anderson; referred to the Committee on the Judiciary.

Number: H.R. 6962

Title: "To extend provisions of the Act of March 20, 1933, and veterans regulations applicable to World War veterans and dependents to veterans and dependents of the present war, and for other purposes."

- 10 -

Features: Title is explanatory.

Status: Introduced April 20, 1942 by Representative Lesinski; referred to the Committee on Invalid Pensions. Committee is awaiting reports and expects to hold hearings before the House recesses.

Number: H.R. 7057

Title: "To provide for the purchase of motor vehicles for war purposes, to remove restrictions on the sale of motor vehicles, and for other purposes."

Features: Directs the Reconstruction Finance Corporation to purchase all automobiles and trucks the manufacture of which was completed on or after January 16, 1942, and such additional vehicles as may be needed for war purposes; authorizes sale of vehicles to other agencies and departments at R.F.C. purchase price; removes restrictions on sale of other automobiles and trucks.

Status: Introduced May 7, 1942 by Representative Gehrman; referred to the Committee on Banking and Currency.

Number: H.R. 7055

Title: "To promote research on minerals in the United States, to establish mining and metallurgical stations in universities and colleges in the several States to aid prospectors and small opera-

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tors, and to promote utilization of the natural resources of the Nation."

Features: Authorizes annual appropriation of \$50,000 to each state for mining and metallurgical stations, support for research in mineral development.

Status: Introduced by Representative Scrugham May 6, 1942; referred to Committee on Mines and Mining.

MAY 28 1942

Secretary Morgenthau

Mr. Foley

Attached is the fifth report on pending legislation prepared in Mr. Bernard's office to assist you in your work as a member of the Joint Senate and House Committee on economy.

[Initialed] H. H. F., Jr.

EMC:ec 5/27/42

Report as of May 25, 1942 on Pending Legislation
Wherein There is Possibility of Non-Defense Economies

Since the last report, as of March 31, 1942, there has been no major change of interest within the scope of these reports.

The Senate Committee on Finance on Thursday, May 28, will consider H.R. 4 and H.R. 4845, and other veterans pension measures. H.R. 4 and H.R. 4845 were considered by a subcommittee and reported in January without recommendation to the full committee. First year costs are estimated to involve more than \$33,000,000. Other pension bills in the committees of both Houses are not receiving any particular action.

The situation as regards H.R. 5993, the Omnibus Rivers and Harbors bill, and H.R. 6724, Representative Dondero's substitute Rivers and Harbors bill including only thirty-eight projects, has not changed. However, H.R. 6999, authorizing a \$144,000,000 appropriation for construction of pipe line and navigable barge canal across Florida, and improvement of the Intracoastal Waterway between Florida and Mexico, was introduced April 27, 1942 by Representative Mansfield, and on May 25, 1942 was reported by the House Committee on Rivers and Harbors and is now pending before the House.

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Representative Coffey of Nebraska. In addition to establishing a parity formula this bill, under section 8, would allocate to the Commodity Credit Corporation all customs duties and excise taxes collected on the entry of farm products (present law in U.S.C., 1940 ed., title 7, section 612c allocates 30% of all duties for similar purposes).

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Features: This bill authorizes an appropriation not to exceed \$5,000,000,000 to enable the President to acquire motor vehicles, parts and equipment for national defense purposes.

Status: Introduced by Senator Downey April 16, 1942; referred to the Committee on Military Affairs.

Number: S. 2475

Title: "To provide reimbursement for the loss of taxes on certain real property acquired by the United States for military or naval purposes."

- 8 -

Features: Provides that payment shall be made to reimburse towns and villages in the United States for (1) loss of revenue from taxes, and (2) loss or impairment of value to municipal improvement, as a result of acquisition by or on behalf of the United States for general military or naval purposes since January 1, 1940.

Status: Introduced April 23, 1942 by Senator Aiken; referred to Committee on Military Affairs.

Number: S. 2511 and H.R. 7047

Title: "Conferring jurisdiction upon the Court of Claims to hear, determine, and render judgment upon claims of Indians of the Northern Indian Confederacy, and for other purposes."

Features: Confers jurisdiction upon the Court of Claims to hear and render judgment on claims of Indians whose tribes occupied areas in the Northwest Territory; claims based on alleged denial of Indian rights, misappropriations of Indian funds, etc. There is nothing to indicate the probable cost of this bill, but it could be enormous. Section 12, however, provides "That if the amount of any judgment so recovered for any of the Indians under this Act shall exceed \$5,000,000 the Secretary of the Treasury [is authorized to pay in installments]".

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Status: S. 2511 was introduced May 6, 1942 by Senator Shipstead; referred to the Committee on Indian Affairs. Committee anticipates no action this session.

H.R. 7047 was introduced May 5, 1942 by Representative Knutson; referred to the Committee on Indian Affairs.

Number: S. 2540

Title: "Authorizing and directing the Reconstruction Finance Corporation to create a subsidiary corporation to be known as the War Distress Finance Corporation, to deal with cases of business distress and financial hardship attributable to the war and causes related thereto, and for other purposes."

Features: War Distress Finance Corporation to have \$500,000,000 capital to relieve financial distress attributable to the war "including the refinancing of obligations on homes, businesses, or other obligations which are in default * * * on account of conditions fairly attributable to the War".

Status: Introduced May 18, 1942 by Senator Pepper; referred to the Committee on Banking and Currency.

Number: S. 2550

Title: "To provide that monthly payments of yearly renewable term or automatic, or National Service Life Insurance shall not

- 8 -

serve to reduce amounts of compensation or pension payable under existing compensation or pension laws."

Features: Title is fully explanatory.

Status: Introduced May 21, 1942 by Senator Clark; referred to Committee on Finance.

Number: H.R. 6897

Title: "To provide for the dollar-for-dollar matching by the United States of savings by enlisted men in the armed forces through the sale of Soldiers, Sailors, and Marines Savings Bonds, and for other purposes."

Features: Directs to the Secretary that the Secretary of the Treasury issue a special Soldiers, Sailors, and Marines Savings bond to be purchased by deduction from credit accounts for enlisted men which accounts are composed of pay deductions matched dollar for dollar by Federal contribution. Bonds are to bear no interest and shall be due and payable at the end of service or the conclusion of present wars, whichever is later.

Status: Introduced April 2, 1942 by Representative Voorhis; referred to the Committee on Ways and Means.

Number: H.R. 6903

Title: "Providing for taxation by the States and their political subdivisions of certain real property acquired for

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military purposes."

Features: Providing all real property in continental United States hereafter acquired for general military purposes together with improvements thereon shall remain subject to taxation by the state and political subdivision in which it is located to the same extent as other real property is taxed, unless the power of taxation is waived.

Status: Introduced April 6, 1942 by Representative Mott; referred to the Committee on the Public Lands.

Number: H.R. 6960

Title: "For the compensation of property owners in territory to be taken for bombing and target ranges."

Features: Provides for reimbursement of private interests for the taking of property or property rights in territory taken for use as bombing or target ranges.

Status: Introduced April 20, 1942 by Representative Anderson; referred to the Committee on the Judiciary.

Number: H.R. 6962

Title: "To extend provisions of the Act of March 20, 1938, and veterans regulations applicable to World War veterans and dependents to veterans and dependents of the present war, and for other purposes."

- 10 -

Features: Title is explanatory.

Status: Introduced April 20, 1942 by Representative Lesinski; referred to the Committee on Invalid Pensions. Committee is awaiting reports and expects to hold hearings before the House recesses.

Number: H.R. 7057

Title: "To provide for the purchase of motor vehicles for war purposes, to remove restrictions on the sale of motor vehicles, and for other purposes."

Features: Directs the Reconstruction Finance Corporation to purchase all automobiles and trucks the manufacture of which was completed on or after January 16, 1942, and such additional vehicles as may be needed for war purposes; authorizes sale of vehicles to other agencies and departments at R.F.C. purchase price; removes restrictions on sale of other automobiles and trucks.

Status: Introduced May 7, 1942 by Representative Gehrman; referred to the Committee on Banking and Currency.

Number: H.R. 7055

Title: "To promote research on minerals in the United States, to establish mining and metallurgical stations in universities and colleges in the several States to aid prospectors and small opera-

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tors, and to promote utilization of the natural resources of the Nation."

Features: Authorizes annual appropriation of \$50,000 to each state for mining and metallurgical stations, support for research in mineral development.

Status: Introduced by Representative Scrugham May 6, 1942; referred to Committee on Mines and Mining.

HMC:ec 5/27/42

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TREASURY DEPARTMENT
INTER OFFICE COMMUNICATION

DATE MAY 28 1942

TO Secretary Morgenthau
FROM Mr. Foley

In accordance with the existing instructions, there is submitted herewith a summary report of activities and accomplishments carried on by the Legal Staff for the month of March 1942.

Sr 7L.

TREASURY DEPARTMENT

MAY 30 AM 11 30

W. A. RICHARDSON
OFFICE

SUMMARY REPORT ON ACTIVITIES AND ACCOMPLISHMENTS
IN THE OFFICE OF THE GENERAL COUNSEL
MARCH, 1942.

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

1. Tax Convention between the United States and Canada:

The proposed Tax Convention between the United States and Canada which was negotiated at Washington some months ago and which was signed on March 4, 1942, has been transmitted by the President to the Senate and has been made public by that body, the text of the convention appearing in the Congressional Record of March 10, 1942, beginning at page 2222. A representative of the Chief Counsel's Office sat in at the conferences and assisted with the drafting of the convention. This matter was handled under the supervision of Mr. G. E. Adams, Head of the Legislation and Regulations Division.

2. Interesting Case arising under Tax Convention with

Canada: An interesting case involving the proposed tax convention with Canada has just reached the attention of this office. Mrs. A, a citizen and resident of Canada, derived in 1935 income from the sale of stocks or securities in the United States. Due to lack of jurisdiction over her person and property the tax, while assessed, remained uncollected until 1941. In that year Mrs. A, while traveling in a

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taxicab in New York City, mislaid property of considerable value upon the surrender of which by the taxi driver Mrs. A paid him an award of \$100. A few hours after such incident, representatives of the revenue service called upon Mrs. A at her hotel and informed her that she could not leave the United States until she settled her tax liability, with the result that in June 1941 the sum of \$12,000 was paid the United States in settlement of the tax liability, but not the penalty for failure to file a return (case now pending in the Income Tax Unit). Counsel for Mrs. A inquired whether, if the proposed convention is ratified, refund of the tax thus paid will be made. He was informally advised that the convention does not apply to such tax although it may, under certain circumstances, apply to the penalty yet unpaid.

3. Effect of High Tax Rates upon Expenditures for Advertising: It has been said that high tax rates encourage large expenditures for advertising in newspapers, magazines, etc. For instance, if the corporate tax rate averaged 60%, a dollar spent for advertising cost the taxpayer only 40 cents. Goodwill may, therefore, to some extent be developed largely at the expense of the Government. A small tax rate based on the amount spent for advertising might bring in

fifty or more millions of dollars of revenue annually. Representative Sauthoff of Wisconsin has suggested that a tax be applied to newspaper and radio advertising. The matter is being brought to the attention of the Tax Legislative Counsel.

4. Tydings' Report: The Chief Counsel for the Bureau of Internal Revenue received from the Tydings' Committee on Inquiry in re Transfer of Employees a questionnaire requesting information and data concerning the activities of the Legal Division under his supervision. The requested information and data were prepared by Mr. C. T. Ellis of the Chief Counsel's immediate office and sent forward to the Committee under date of March 26, 1942.

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

5. New York Foreign-Trade Zone (for description see February, 1942, report, Item 3): On March 28, 1942, Mr. Chambers attended a meeting of the Committee of Alternates of the Foreign-Trade Zones Board, which considered and recommended approval of a request of Mayor LaGuardia that certain piers and uplands adjacent thereto in New York City be included in the foreign-trade zone for the duration of the present emergency, to take the place of that part of the

zone which has been requisitioned by the War Department. A resolution to that effect has been drafted for the approval of the Board.

6. Overtime compensation for Customs' Employees: Messrs. Chambers and Ivey prepared for the signature of the Commissioner of Customs a circular letter advising the collectors that the Comptroller General has declined to render a final decision on the question of overtime compensation for services performed on January 1, 1942, until the customs overtime litigation in the Court of Claims is disposed of; that the Comptroller General expressed the view that in the meantime no extra compensation should be paid for January 1, 1942, or any subsequent national holiday on which work is similarly required pursuant to an administrative order; and that the collectors should be governed accordingly.

7. Transfer of functions of Bureau of Marine Inspection and Navigation: As a result of the transfer to the Bureau of Customs under Executive Order No. 9088 of February 28, 1942, of many of the functions of the Bureau of Marine Inspection and Navigation, the Chief Counsel's Office of the Bureau of Customs commenced during March legal research, review, and

other activities relating to the functions transferred. Mr. George Kramer, an attorney formerly of the Department of Commerce, was transferred to this office to carry on the additional legal work resulting from the transfer of functions.

8. Funds available for special tax research: An opinion addressed to Mr. Thompson, which was written by Mr. Feidler and signed on March 2, 1942, concludes that the appropriation for the "consolidated emergency fund" in the First Deficiency Appropriation Act, 1942, cannot be used beyond April 30, 1942, for financing the special tax research on Federal, state, and local fiscal relations (Mr. Gulick's group). The regular appropriation for the Bureau of Internal Revenue should not, as a matter of law, be used.

9. The employment of Canadian and British nationals by the Treasury Department: An opinion addressed to Mr. Harry White which was written by Mr. DuBois and Mr. Feidler and signed on March 10, 1942, considers two cases in which (1) there has been a declaration of intention to become a citizen and (2) there has been none, and concludes that if there is no declaration of intention, the alien can not be employed in the Department. If there is a declaration, it is possible to employ the alien in a non-Civil Service position paid from the Stabilization Fund.

10. Payment of Government check to attorney of payee:

An opinion addressed to the Administrative Assistant to the Secretary, which was prepared by Mr. Collins and Mr. Feidler and signed on March 16, 1942, concludes that (1) whether an attorney engaged to collect a claim from the United States may endorse his client's name depends on the law of the particular state; (2) the Treasurer should not pay checks so endorsed unless the attorney has implied authority to endorse under the law of the state where the check is signed; (3) there is no necessity to amend the Federal forgery statutes to meet the situation.

11. Certifying and disbursing functions under Public Law 389, Act of December 29, 1941: An opinion addressed to Mr. Bartelt, which was prepared by Mr. Wald and Mr. Feidler and signed on March 19, 1942, concludes that under Public Law 389: (1) certifying officers must be of the agency which is concerned with the obligation for which the vouchers are certified; (2) the mechanical act of signing a voucher may be delegated to a subordinate without subjecting that subordinate to a certifying officer's responsibility; (3) it is legally unwise to permit one person to be both certifying and disbursing officer; (4) disbursement of emergency relief funds for War and Navy Departments is within purview of Public Law 389.

12. Payments by the Secretary of the Treasury for industrial loans under section 13b(e) of Federal Reserve Act:

An opinion addressed to Under Secretary Bell, which was prepared by Mr. DuBois and Mr. Gilmore and signed on March 20, 1942, advises that payments may be made to the Federal Reserve Banks for industrial loans without requiring the Banks to complement the payments received from the Secretary with equal advances out of their own funds. However, amendment of the regulations of the Secretary, dated August 14, 1934, would be necessary, and amended regulations were submitted with the opinion.

13. Appointment of Inspector, White House Police: An opinion, addressed to Chief Wilson, which concludes that the new position of Inspector in the White House Police force, appropriated for by the First Deficiency Appropriation Act, 1942, must be filled from the Metropolitan Police force or the United States Park Police, was prepared by Mr. Meyer, and signed on March 24, 1942.

14. Use of Government silver stocks in industrial defense plants: This opinion, addressed to Secretary Morgenthau, concludes that under the authority conferred upon the President in the Joint Resolutions declaring war between the United

States and Japan, Germany, and Italy, he may direct stocks of "free silver" contained in the available stocks of the Government be transmitted to industrial plants for use in a manner which will permit substantially all of it to be returned at the termination of the war. The opinion was prepared by Messrs. Feidler, Brenner, Tobolosky, and Meyer and was signed on March 30, 1942.

15. Revision of Index Cards and Statutory Index for General Counsel's Opinions: The revision of index cards and statutory index for General Counsel's opinions was necessary to the completion of the Digest of General Counsel's Opinions Nos. 301 to 500, inclusive, and to the consolidation and completion of the Citation Index for General Counsel's Opinions Nos. 1 to 500, inclusive. The work required rewriting and reclassifying all the cards maintained in the card index file. An estimated 3000 cards were revised and the plan and style of the digest cards and paragraphs, which over a period of years had been varied, were made uniform. In order to facilitate use of the digest and citation index, explanatory statements of the plan of each was prepared, and a Table of Titles was prepared for the Digest. This work was done by the members of the Opinions Section.

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

16. Public Debt Act of 1942 (for description see January, 1942, Report, Item 29, and February, 1942, Report, Item 14):

The Public Debt Act of 1942, which was drafted by Messrs. Bernard and Ahroon, was approved by the President on March 28, 1942, and became Public Law No. 510. Mr. Bernard accompanied the Secretary and Under Secretary to the hearings before the Ways and Means and Finance Committees on this bill and assisted them in presenting the Treasury's testimony thereon. He also prepared the Committee reports on the bill.

17. New Five-Cent Coin and Conditional Gift Legislation (for description see January, 1942, Report, Item 31): The Second War Powers Bill, which contains two Treasury-sponsored titles, the conditional gift legislation as Title XII and the silver-nickel coin legislation as Title XIII, was approved by the President on March 27, 1942, and became Public Law No. 507.

18. Proposed Legislation to Regulate Production of Opium Poppy (for description see April, 1941, Report, Item 17):

This bill, to discharge more effectively the obligations of the United States under certain treaties relating to the manufacture and distribution of narcotic drugs by providing for

domestic control of the production and distribution of the opium poppy and its products, and for other purposes, was introduced by Senator George, on March 25, 1942, as S. 2405 and referred to the Committee on Finance. It was also referred to the Committee on Ways and Means.

19. Un-American Activities Committee (for description see August, 1941, Report, Item 16): In addition to his regular routine duties with the Un-American Activities Committee, Mr. Spingarn continued his work on the controversial William Wheeler Hinckley case. He interviewed a number of people in connection with this case, including (1) Miss Eleanor Nelson, Executive Secretary of the United Federal Workers of America, a CIO union for Federal workers, who expressed the opinion that the Treasury should retain Hinckley in his present position, and (2) Mr. James Carey, National Secretary of the CIO, who indicated that the Treasury was justified in dropping Hinckley. The report of the Committee, recommending that Hinckley be removed from his Treasury post was prepared by Mr. Spingarn. At the request of Mr. Graves, Mr. Spingarn also prepared a memorandum to Mr. Graves commenting on the points made in a memorandum by Mr. Gaston, who disagreed with the conclusion reached in the report. Mr. Gaston discussed the case with the Secretary, who expressed the desire that

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Hinckley be dropped.

20. Board of Legal Examiners (for description see July, 1941, Report, Item 15): Mr. Bernard as alternate for Mr. Foley is continuing his work on this Board.

21. Law Committee of Defense Communications Board (for description see November, 1940, Report, Item 23): Mr. Spingarn (who is the Treasury's representative on the Law Committee of this Board) attended joint meetings of the Law and Coordinating Committees on March 21 and 23, 1942.

21. Economy Committee Material (for description see November, 1941, Report, Item 29): There was prepared for the use of the Secretary of the Treasury in his work as a member of the Joint Committee of Reduction of Nonessential Federal Expenditures, established by Section 601 of the Revenue Act of 1941, a fourth report on legislation presented to Congress.

22. State Cooperation with Federal Agencies in Defense Efforts (for description see November, 1941, Report, Item 30): This office prepared a letter to Mr. Thomas B. Paton, Assistant General Counsel of the American Bankers Association, outlining the circumstances which led to the request by this Department for state legislation authorizing institutions to act as issuing agents for the sale of War Bonds. Subsequently,

Mr. Paton called attention to the Washington case of Decker vs. Fowler, in which it was determined that a decedent, by taking out in his lifetime certain Government bonds in which another person was made an additional beneficiary, had not made a valid gift of the proceeds of the bonds to said beneficiary. He was advised by Mr. Spingarn that the Treasury is anxious to settle the question raised in the Decker case by intervening in some other case. A copy of the statement of the Treasury's position with reference to this case is being prepared for him.

23. Executive Order Establishing Interdepartmental Committee for the Voluntary Payroll Savings Plan for the Purchase of War Savings Bonds: Mr. Bernard and Mr. Rupert drafted the proposed Executive Order and relevant papers. The Order contemplates the establishment in all departments and agencies of a voluntary payroll allotment plan similar to that now in operation by the Treasury.

24. Resolution Requiring Reports Pertaining to Government Contracts and Income on Contracts: This office prepared a letter on this resolution (S.J.Res. 134), in which the comments of the Procurement Division and the Bureau of Internal Revenue were combined, pointing out the difficulty and

expense in complying with the provisions requiring reports showing the names of persons to whom contracts have been awarded and income received and income tax paid by such persons, segregated to reveal Governmental sources separate from other sources. The letter which was addressed to the Chairman, Senate Committee on Appropriations, recommended against enactment of the joint resolution.

25. Abolition of Comptroller of Customs: Mr. Spingarn of this office furnished Mr. Gaston with a memorandum reviewing at length the history and background of a proposal to abolish the positions of the seven Comptrollers of Customs. It appears that there had been some recent discussion between Marvin McIntyre and Mr. Graves about this matter. Mr. Graves decided, however, that it would be inadvisable to attempt by any process to vacate or abolish these positions at this time in view of the resentment that would probably be aroused in Congress and the improbability of success.

26. Illustration of War Savings Bonds: Mr. Bernard and Mr. Ranta of this office prepared a regulation authorizing the illustration of War Savings Bonds in connection with the campaign for the sale of such bonds.

27. Bill to Determine Damages from Eradication of Mediterranean Fruit Fly: This office prepared a letter to the Chairman of the Senate Committee on Claims, which Committee had reported S. 2022 in January, 1942, objecting to burdening the Treasury Department with the functions of determining these claims, and suggesting the advisability of scrutinizing the legislation with a view to disapproval if found to be a nonessential expenditure. The bill involves an appropriation of \$10,000,000 and the investigation would entail extensive work and the probable creation of much ill will toward the arbitrating agency.

28. Tansey Relief Bill Hearing: At the request of the committee, Mr. Spingarn, and Mr. Forrest of the Alcohol Tax Unit appeared at a hearing of the House Claims Committee on this bill (H.R. 1540), to award Tansey \$81,000 plus interest for certain liquor in which he had an interest which was seized and destroyed by Federal prohibition agents in October, 1926, pursuant to a court order. Mr. Spingarn testified in opposition to the bill, which is an \$81,000 Treasury grab and without any merit. A representative from the Department of Justice also opposed the bill.

29. Proposed Silver Legislation: This office reviewed the proposed silver legislation, the original draft of which was prepared by Mr. Rupert of this office in conjunction with Miss Hodel and Mr. Brenner of Mr. Bernstein's office.

30. Retirement Law: This office prepared a summary of the provisions of the Retirement Law of particular interest to Treasury lawyers.

31. Priority Rating of the Various Agencies for War Personnel Transfer Purposes: This office prepared a memorandum describing in detail the injustice done the Legal Division by the recent Budget priority rating list which is to govern the transfer of personnel between agencies during the war. The General Counsel's office, along with most of the Treasury, was placed in Class 5, the lowest class on the list. This memorandum was sent to Mr. Schoeneman for enclosure in a letter which the Secretary directed to the Bureau of the Budget complaining about the priority rating list from the standpoint of the entire Treasury Department.

32. Testimony before Senate Finance Committee: Mr. Spingarn, and Mr. Forrest of the Alcohol Tax Unit Branch of the Legal Division, appeared and testified at a hearing of the Senate Finance Committee on March 5 on H.R. 6543 and H.R. 6273.

The first bill (which was sponsored by the War Production Board, but actually drafted in the Treasury Department) is designed to facilitate the production of industrial alcohol by beverage distilleries. The other bill (which is sponsored by the liquor industry, but has Treasury approval), would liberalize the provisions of existing law with respect to allowable liquor losses for tax purposes. Both bills were ordered reported at the conclusion of the hearing.

33. Budget Hearing on Foreign Fund Control Deficiency Item: Mr. Spingarn of this office represented the Legal Division at a Budget hearing on March 6 on the Foreign Funds Control Deficiency Item for inclusion in the Second Deficiency Bill.

34. Compromise cases: We prepared the final recommendations in seven compromise cases during the month. Approval was given to an amended offer in compromise of the indebtedness of the Sun Maid Raisin Growers of California and the Sun Maid Raisin Growers Association to the Farm Credit Administration. This concluded a matter which had been the subject of negotiation, conference, and study for many months. The indebtedness was \$3,049,728.69. The compromise resulted in cash payment to the Government of \$179,271.52; conveyance to the Government of a clear title to real and personal property appraised at \$360,073.06; conveyance to the Government (sub-

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ject to a five-year lease with repurchase option) of the operating plant valued at \$675,011.79; a new note (representing assets which are retained by the debtors and which are subject to superior liens) in the amount of \$595,849.61. The compromise writes off \$1,239,522.71 of the original indebtedness. The rate of interest on the new indebtedness is 2 1/2% as against 3 3/8% on the old indebtedness. The terms of compromise were much more advantageous than those originally proposed.

35. Dismissal of Indictments: Mr. Ranta of this office prepared a letter to Assistant Attorney General Berge advising that this department was reluctant to concur in the request for the dismissal of an indictment against Anthony Panchella for passing a counterfeit note, in view of the defendant's former criminal record. Also a letter was prepared advising that this Department would interpose no objection to the dismissal of count one of an indictment charging Antolino M. Garrillo with false personation as payee of a Government check, inasmuch as defendant had been sentenced on count two charging forgery of the check, and the judge at the time of the sentence was apprised of all the facts of the case.

36. Congressional Action on other Treasury-sponsored Legislation: (a) Huntsville National Bank. Our bill (S.2309) for the relief of the First National Bank of Huntsville, Texas, was passed by the Senate on March 30, 1942.

(b) Alcohol Production. H.R. 6543, to amend certain provisions of the Internal Revenue Code relating to the production of alcohol, was approved by the President on March 27 and became Public Law No. 508.

(c) Relief of Disbursing Officers. On March 17, 1942, Senator Brown introduced our bill for the relief of G.F.Allen, Chief Disbursing Officer of the Treasury Department, and for other purposes, as S. 2379. The bill was referred to the Senate Committee on Claims.

(d) Mailing of Small Firearms. This bill, H.R. 1793, to authorize the mailing of small firearms to officers and employees of the enforcement agencies of the United States, was approved by the President on March 7, 1942, and became Public No. 484.

(e) Captured or Missing Government Personnel. H.R. 6446, which authorizes the continuation of pay and allowance of captured or missing military or civilian employees of the Treasury Department and other agencies of the Government, during periods of absence from posts of duty, and for other

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purposes, was approved by the President on March 7, 1942, and became Public No. 490.

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

37. Hawaiian Currency and Securities: In response to many requests for aid relative to currency and securities held in Hawaii, arrangements were concluded early in March for the dispatch of Treasury representatives to Honolulu. The procedure which these representatives were to follow in the destruction of currency and securities and the giving of credit or the reissue of securities on the Mainland was approved, together with a brief digest of the probable assignment difficulties they might encounter. Subsequent reports from the Treasury representatives in Hawaii indicated that the procedure worked out has been functioning well, especially with reference to the surplus currency problem. Messrs. Cunningham, Reeves and Tietjens worked on this.

38. Reorganization of Government Agencies: In connection with the Executive Order establishing certain reorganizations of government agencies, we discussed with representatives from the General Counsel's Office of FHA,

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questions with regard to necessary changes in the form and execution of FHA Debentures. We also made suggestions for the revision of the orders for the issue of Debentures by the Federal Savings and Loan Insurance Corporation. We also discussed with representatives of the Home Loan Bank Administration, questions in connection with the proposed issue of Short-term Debentures of the Consolidated Home Loan Banks. These Debentures are not guaranteed by the United States, but do have to be approved prior to issue by the Secretary, and they are also marketed through the Public Debt Service.

Messrs. Cunningham and Tietjens handled this matter.

39. Bonding of Certifying Officers: We worked with representatives from Mr. Bartelt's office on regulations to be issued by the Treasury Department and the forms of bonds to be required of certifying officers pursuant to legislation effective April 1, 1942, which requires all certifying officers to give bond, and directs that the Treasury Department prescribe certain standards for such bonds. The Opinion Section, together with Messrs. Reeves and Tietjens, worked on this.

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40. Industrial Credit Corporation Bill: We worked with Mr. Heffelfinger in the preparation of a report to the Bureau of the Budget expressing the views of the Treasury Department with respect to proposed legislation sponsored by the Board of Governors of the Federal Reserve System to create a Federal Industrial Credit Corporation. The proposed corporation would extend financial assistance to smaller commercial and industrial businesses. Loans could be made directly to businesses or in cooperation with financing institutions, but not more than \$1,000,000 could be outstanding at any one time to any one business. The corporation's capital would be supplied through payment by the Secretary of the Treasury of approximately \$112,000,000 remaining from the \$139,000,000 originally appropriated for the purposes of making advances to the Federal Reserve Banks for industrial loans. Upon completion of these payments, the United States would become the owner of all stock in the Federal Deposit Insurance Corporation heretofore subscribed to by the Federal Reserve Banks. A report was prepared by Mr. Reeves on the legislation approving the purpose of the bill.

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41. Gift of Airplane by the Spartan Company, Tulsa, Oklahoma: At Under Secretary Bell's suggestion, we talked with Assistant Secretary of the Navy Bard and Captain Ramsey of the Bureau of Aeronautics about arrangements being made by the Navy Department to accept the gift of a Navy airplane from the management and employees of the Spartan Aircraft Company. We prepared the necessary letters from the Treasury Department and forwarded to Captain Ramsey a letter signed by the Acting Secretary accepting the gift on behalf of the United States by authority vested in the Secretary under the Second War Powers Act, 1942. Mr. J. Paul Getty, President of the Aircraft Company, advised that the plan was to work the staff on Sunday and make the presentation on Monday, March 30. Captain Ramsey later advised that the Under Secretary's letter had been used during the presentation and that the Navy had taken over the plane, as planned. Messrs. Reeves and Tietjens worked on this matter.

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

42. West Coast Evacuation Program: Messrs. Luxford, Lawler, Edelman, and Naiden of this office in cooperation

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with members of the Administrative Staff assisted Lieutenant General DeWitt, Commanding General, Western Defense Command and Fourth Army, in handling property problems created by the program of evacuation of Japanese, Germans and Italians from the west coast military areas. The work involved cooperation with the Federal Reserve Bank of San Francisco, Farm Security Administration, Department of Agriculture, Federal Security Agency and the Office of Price Administration.

Numerous interviews were held with Japanese industrial and community leaders, as well as with potential purchasers of Japanese property by Messrs. Lawler, Luxford and Edelman.

Documents delegating authority to the Federal Reserve Bank of San Francisco, as well as Special Regulation No. I, and the amendment of General License No. 68A, each of which was designed primarily to deal with problems on the West Coast, were issued in connection with this program, and in cooperation with the staff in Washington. Likewise, appropriate press releases were issued, and a cooperative Public Relations Program carried out under the direction of this office.

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Messrs. Luxford, Lawler, Naiden, DuBois and Murphy handled this matter.

43. Issuance of Documents: (a) General Ruling No. 11 (For description see January, 1942 report, Item 40; February, 1942 report, Item 31). General Ruling No. 11 issued by the Treasury Department, Communications Ruling No. 1 issued by the Office of Censorship, and a press release explanatory of these documents were released on March 18. The over-all course of action to be followed under the freezing control with respect to transactions involving trade and communication with enemy territory and enemy nationals was thus instituted. The purposes of these documents were in part to define and regulate trade and communication with enemy nationals, and to supplant the inflexible concepts of the old Trading with the enemy Act, thus giving to the commercial world a concrete test by which their relations with foreign countries, and particularly the neutrals, might be defined. These documents also had the effect of integrating the Censorship concept of enemy with that of Foreign Funds Control and thus placing all trade and communication upon a uniform footing. Messrs. Luxford, DuBois, and Murphy worked on this program.

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(b) General Ruling No. 6A. General Ruling No. 6A, controlling the importation of currency into the United States from blocked countries not within the generally licensed trade area, and from Proclaimed List nationals, was also issued. In conjunction with this general ruling it was necessary to issue instructions to collectors of customs, postmasters and other agencies concerned in the handling of currency. At the present time progress is being made on further instructions relating to the treatment of currency which has been held under General Ruling No. 6A. These instructions are being worked out in conjunction with representatives of the New York Federal Reserve Bank. Messrs. Luxford, Murphy and Rains, in conjunction with Mr. DuBois, are working on this matter.

(c) General License for Purchase of United States Securities. Steps are also being taken to draft a general license relating to the purchase of Government securities, particularly Defense Bonds, from blocked accounts. This license is being considered in conjunction with Public Debt and will, it is hoped, further Secretary Morgenthau's program for the sale of these bonds.

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Messrs. Murphy and Aarons are handling this matter. Likewise an amendment to the Internal Revenue Code which will exempt from the stamp tax transfers made pursuant to the Trading with the enemy Act and the First War Powers Act is being considered. Messrs. DuBois, Murphy and Golding, in conjunction with Mr. Flesch of the Chief Counsel's Office are working on this.

(d) Amendment to Executive Order No. 8389. Consideration is being given to an amendment to Executive Order No. 8389* in order more clearly to delineate between the functions of the Alien Property Custodian and the Secretary of the Treasury. The purpose of this amendment is to enable the Treasury Department more effectively to carry out the functions assigned to it in the wartime administration of freezing control. In this connection a memorandum for the Alien Property Custodian and the President are being prepared. Messrs. Luxford, Aarons, DuBois, Friedman, Murphy, and Golding are handling this matter.

(e) Voiding of Transfers. Active consideration is being given at the present time to the issuance of a general ruling which will have the effect of nullifying

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transfers and assignments made abroad which have not been licensed by the freezing control. This problem becomes particularly important in view of a number of pending suits in the State of New York which are testing the validity of these transfers. Messrs. Luxford, Daum, Cook, Zarky, and Golding are working on this matter. Also, they are giving consideration to a general ruling relating to proxies. Mr. Zarky is also working on the latter problem.

44. Extension of Freezing Control (For description see February, 1942 report, Item 29): Freezing control was extended to the Netherlands East Indies by the issuance of Public Circular No. 17. This document called attention to the automatic extension of the Executive Order to the areas under Japanese control, and amended certain general licenses which had authorized transactions by or on behalf of persons in the Netherlands East Indies. Messrs. Luxford and Murphy handled this matter.

45. Vesting of Axis Property: (a) Ships. A study was made by Messrs. Luxford and Zarky of the vesting of title to certain sabotaged vessels in order to avoid the necessity for lengthy hearings under the Ship Seizure Bill.

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(b) Transfer of General Aniline and Film Corporation Stock to Alien Property Custodian (For description see February, 1942 report, Item 26(a)). Documents are presently being prepared to transfer the stock of General Aniline and Film Corporation to the Alien Property Custodian. In this connection, research has been made into the legal implications of such a transfer in order that we may best protect the interests of the Secretary of the Treasury. Messrs. DuBois, Golding, and Duam are making this study.

46. "Scorched Earth" Program for Hawaii (For description see February, 1942 report, Item 30): This office participated in the formulation of, and is drafting the documents with respect to, a program to prevent Japan from gaining access to securities and currency in the case of an attack on Hawaii. Financial, Government, and military authorities in Hawaii have requested protection for securities and currency in Hawaii, and extensive plans are in the process of preparation. Miss Goode and Messrs. Luxford and Murphy are preparing these documents.

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47. China, the Philippines, and the Southwestern Pacific: (a) Moratorium (For description see February, 1942 report, Item 24). This office is studying the desirability of a moratorium on the funded obligations of certain Philippine corporations, such as the Manila Electric Company and the Manila Gas Company. Certain Philippine companies having substantial assets within the Philippines are finding it difficult to meet interest payments on their funded obligations. Failure to meet such payments may result in losses to the stockholders and bondholders out of all proportion to actual losses resulting from the invasion of the Philippines. Some of the companies involved have requested the Treasury Department to provide relief in the form of a moratorium in order that interest payments may be postponed until such time as it is possible to evaluate more accurately the financial condition of such companies. Messrs. Luxford, Cook, and Golding are handling this matter.

(b) Currency Rates. A study is being made by Mr. Luxford of the rate at which United States currency is selling in the Near and Middle East.

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(c) Proposed Philippine Decree (For description see February, 1942 report, Item 25). This office has given consideration to the possibility of having either the Philippine Government or the United States Government issue a decree voiding the transfer of Philippine assets to the Japanese invaders. The technique of such decree would be to interfere with the Japanese economic penetration along the lines being followed by Germany with respect to certain occupied portions of Europe. Messrs. Luxford and Golding are considering this matter.

48. Censorship (For description see January, 1942 report Item 40; February, 1942 report, Item 31): As a part of the General Ruling No. 11 program, this office cooperated with the Office of Censorship in the issuance of Communications Ruling No. 1 forbidding communications with enemy nationals. Likewise, the preparation of an explanatory press release has been worked out with representatives of Censorship. Since that time this office has had occasion to consider communications problems of interpretation which have arisen in connection with the administration of the Office of Censorship.

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During the month of March the Office of the Chief Postal Censor issued a general order to all of its stations in the United States and Panama defining the treatment to be given mail containing property in which Foreign Funds Control was interested. Representatives of this office worked with representatives of the Office of the Chief Postal Censor in drafting this order as well as explaining its ramifications before the Censorship School conducted by the Board of Economic Warfare. Messrs. Luxford, Murphy, and Rains handled the work and problems in connection with these matters.

At the present time consideration is being given to the extension of this technique to other matters in which Foreign Funds Control is interested, particularly communications which may contain information indicative of violations and evasions. We are also engaged in making the regulations relating to the importation of stamps more stringent. Messrs Murphy and Rains are handling this phase of the problem.

49. Census Reports (For description see January, 1942 report, Item 45; February, 1942 report, Item 39): The work done by this office with regard to foreign-owned

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property reports included: (a) Conferences by Mr. Reeves with the Department of Justice regarding the use of Form TFR-300 in anti-trust work, particularly in respect of patents ^{and} restrictive agreements;

(b) Advice to various governmental agencies concerning reports by them on Form TFR-300, given by Messrs. Reeves, Arnold, and Hannett;

(c) Conferences with the Administrative Staff of Foreign Funds Control and of the Division of Monetary Research regarding the use and editing of reports on Form TFR-300, participated in by Messrs. Reeves and Arnold;

(d) Conferences with state and city officials in Albany, New York City, and Trenton, New Jersey, concerning reports of Form TFR-300 by agencies of New York and New Jersey, handled by Mr. Arnold;

(e) Decisions on miscellaneous questions concerning the filing of Series J and K, Form TFR-300, prepared by Messrs. Reeves, Arnold, and Hannett.

50. Litigation: Certain problems arising in connection with attachments and pending cases are being studied by

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Messrs. Reeves, DuBois, Aarons, Luxford, Wolf, and Golding.

51. Public Relations (For description see January, 1942 report, Item 42; February, 1942 report, Item 30): As in the past, in connection with the issuance of each major document, explanatory press releases were issued. Such releases were intended to explain to the public in simple language what the purpose of each document was and its general provisions. Also, from time to time, press releases for the benefit of special groups, calling attention to particular situations of interest, have been issued. In this connection, a release to the Office of Facts and Figures of an explanation of General License No. 42, relating to resident aliens, was made, and a similar release, explanatory of General Ruling No. 11, is in preparation. Messrs. Luxford, Naiden, and Murphy handled this matter.

52. Directive Licenses: This Division cooperated with the Administrative Section in the issuance of licenses authorizing and directing several types of transactions. Most important among these were (1) the removal of files and papers of such organization as the German Library of

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Information to the newly established Federal Funds Control Record Library in the Federal Reserve Bank of New York, handled by Mr. Aarons, and (2) the sale of "stranded" strategic merchandise which had been destined for invaded countries and with which no one in this country would otherwise have had power to deal, which matter was handled by Messrs. Aarons, Luxford, and Golding.

53. Patents (For description see February, 1942 report, Item 26): A draft of documents was prepared by Mr. Kehl for the compulsory licensing of blocked patents under the First War Powers Act. The documents included regulations of the Secretary of the Treasury, memorandum to the President, press release, and forms for license applications and notice of claim.

54. Insurance Problems: Amendments to Proclaimed List insurance instructions were drafted by Mr. Kehl to cover assignments and surveys by agents with respect to Proclaimed List losses. In that connection an analysis of the British Statutory List insurance instructions was also made.

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55. Interpretations: Voluminous correspondence was handled which involved questions of interpretation of the Executive Order, Regulations, rulings, and licenses by Miss Hodel, Miss Klein, and Miss Goode.

Inter-office interpretations regarding (1) the effect of illegal entry on status under General License Nos. 42 or 68A, and (2) the necessity of reports by trustees under paragraph 2(a)(ii) of General License No. 42 were drafted. Miss Hodel and Miss Goode handled these matters.

After the issuance of General Ruling No. 11, prohibiting transactions involving trade and communication with enemy nationals, a number of problems of interpretation arose in connection with these documents. The most pressing of these problems was the status of attorneys in fact and attorneys at law who represented enemy nationals, and the position of banks who had prior to March 18, 1942, received instructions from enemy nationals with respect to the operation of accounts. At the present time a series of public and confidential interpretations is being worked out to meet these problems by Messrs. Luxford, Golding, Murphy, and DuBois.

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56. Compliance Problems - Investigations (For description see February, 1942 report, Item 44): (a) Procedure for presenting cases for prosecution. A plan was prepared providing for the coordination of the Investigative and Enforcement Units of Foreign Funds Control and the compliance Problems Section of this Office in preparing a criminal report upon certain violations of the Executive Order. The plan provides for the preparation and presentation of the criminal report to the Attorney General. Mr. Grills worked on this plan.

(b) Prosecution of Kenji Iki. This office cooperated with the Investigative Unit and Enforcement Unit of Foreign Funds Control in preparing a criminal report concerning violations of the Executive Order by Kenji Iki in Seattle, Washington. Iki is charged with dealing with more than a half million dollars worth of securities in violation of the Executive Order. The report has been sent to the Attorney General who has instructed the United States Attorney in Seattle to take appropriate action. Messrs. Grills and Hannett handled this case.

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(c) Investigation of certain alleged dealings with Fezandie & Sperrle. In cooperation with the Anti-Trust Division of the Department of Justice, a proposed outline for an investigation of Fezandie & Sperrle, Inc. was prepared by this office to be used by the United States Attorney in Trenton, New Jersey, in a Grand Jury investigation of General Dyestuffs, Inc. Mr. Grills handled this matter.

(d) Rueckwanderer Investigation. Members of this staff have examined the memoranda and exhibits submitted by the Department of Justice concerning its investigation of the Rueckwanderer business and possible criminal prosecutions in that connection. Mr. Quint handled this case.

(e) Investigation of Lieutenant Colonel Georges F. Doriot. A member of this staff, Mr. Quint, participated in a conference with members of the Administrative Staff and with Lieutenant Colonel Doriot of the Quartermaster Corps, United States Army, concerning Colonel Doriot's associations with Banque Worms and various holding companies organized by Banque Worms, and concerning Colonel Doriot's association with various members of the Vichy group.

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(f) Investigation of the Pennzoil Company. An investigation was made by Mr. Rains concerning the affairs of the Pennzoil Company with a view to determining whether the Company should be prosecuted for violations of the freezing control.

57. Liquidation Problems (For description see February, 1942 report, Item 28): A memorandum was prepared concerning questions relating to powers of attorney involved in the liquidation of the San Francisco branch of Mitsubishi Shoji Kaisha, Ltd. The problem of the possible creditor preference involved in paying employees of Mitsui Bussan Kaisha, Ltd., a severance pay and bonus was studied. These matters were handled by Mr. Marks.

58. Investigation of Blocked Law Firms: A memorandum was prepared with regard to the legal problems involved in seizure of the files and records of a blocked law firm by Miss Goode and Mr. Marks of this office.

59. Admiralty and Shipping Problems: In connection with a libel brought against certain Latvian steamships, conferences were held with the State Department and

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Maritime Commission and letters were prepared for the court and the attorneys stating the Treasury's position with regard to the questions raised. Messrs. Reeves and Aarons handled this matter.

60. Foreign Funds Control Pamphlet: This office cooperated with the Federal Reserve Bank of New York in compiling a pamphlet (to be distributed to the public) containing documents pertaining to Foreign Funds Control. Miss Hodel worked on the pamphlet.

61. Latin America (For description see January, 1942 report, Item 37; February, 1942 report, Item 55): (a) United States Concerns in Latin America. A public circular (No. 18) and press release were issued making it clear that United States concerns operating in Latin America may not deal with enemy territory or enemy nationals. Mr. DuBois handled this matter.

(b) Program of Economic Warfare in Latin America. A program for sending a number of men to Latin America to assist the missions and the local governments with respect to local freezing control matters (and other economic warfare measures) has been the subject of correspondence and discussion between State, Treasury

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and BEW. Although not finally agreed upon, plans are being made for Treasury and BEW to supply about fifteen men each (to start) and for these men to be put through about a month's period of intensive training in foreign funds control, BEW matters, and State Department matters. Mr. DuBois is working on this matter.

(c) Information to Latin American Missions. We have been continuously keeping State Department missions informed as to developments in freezing control in this country and have been receiving and compiling information received from the missions concerning developments in Latin America. A pamphlet is now being prepared for distribution to the missions summarizing what we have done to date; what each of the Latin American countries has done; and what further steps these countries might take. Messrs. DuBois and Rains are handling these matters.

(d) Special Mission to Central America. A member of this office, Mr. Mann, is at present in Central America with a representative of the State Department on a special mission to advise the local authorities and the American missions on the administration of the Proclaimed List and freezing control.

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(e) Proclaimed List Problems. Members of this office have prepared replies to inquiries concerning Proclaimed List problems and freezing control in relation to Latin American trade and financial transactions. Messrs. DuBois, Mann, Rains, Frampton, and Fisher have worked on these replies.

(f) Proclaimed List Clearance Committee. A member of this office, Mr. Rains, attended meetings of the Proclaimed List Clearance Committee.

(g) Additions to The Proclaimed List. During the month of March a member of this office, Mr. Frampton, attended the meetings of the Interdepartmental Proclaimed List Nominating Committee. On March 27, 1942, Supplement 2 to Revision I was published. This Supplement contains many additions and some deletions both for the American Republics and for the European countries and Turkey. Included are approximately 200 new listings for Ecuador which were added at the request of the Ecuadoran Government. Inclusion of these names on the List will enable the Government of Ecuador to bring these persons under its freezing control.

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(h) Enforcements and Diversions. Members of this office, Messrs. Fisher and Rains, have cooperated with the New York customs officials in arranging for the diversion of shipments to satisfactory consignees in cases where such shipments were afloat prior to the publication of the names of the consignees on the Proclaimed List or prior to discovery that a Proclaimed List national was interested in the shipment. Reports were received by telephone directly from the New York Customhouse and a member of this office called the shipper or freight forwarder, or in some cases the shipping line, suggesting that reasonable efforts be made to divert the shipments. The State Department has been notified promptly in all cases so that the American mission may be advised.

(i) Consultation with Enforcement Section. A member of this office, Mr. Fisher, acted as a consultant to the Enforcement Section of Foreign Funds Control on Proclaimed List matters. This work included reviewing correspondence, requesting investigations, consultation on individual cases, and analyzing and evaluating investigative reports.

(j) Lecture to American Censors. Lectures on the Proclaimed List were presented by members of this office, Messrs. Mann, Murphy, and Rains, at the Censor's School of the Board of Economic Warfare. This material was later edited by Messrs. Murphy, Rains, Fisher, and Frampton for use by the American censors as a guide on Proclaimed List matters.

62. Memorandum Re Work of Alien Property Custodian in Last War: A memorandum was prepared by Messrs. Kehl and Golding for distribution within the office with regard to the work of the Alien Property Custodian in the last war.

63. Investigation and Control of Business Enterprises:

(a) American Bosch Corporation (For description see January, 1942 report, Item 36(c)). Members of this staff continued the investigation of the American Bosch Corporation at Springfield, Massachusetts. The work consisted of an examination of records and witnesses, preparation of memoranda and other reports concerning the investigation of personnel. Messrs. Quint and Edelman worked on this.

(b) I. G. Farbenindustrie. Conferences were held with the Anti-Trust Division of the Department of Justice on the problems raised by cartel arrangements between the

Standard Oil Company of New Jersey and the I. G. Farbenindustrie. Messrs. Bernstein, Lawler, and Reeves handled this matter.

64. Currency Problems. Consideration is being given to a plan proposed by the Bank of Brazil in connection with United States and Brazilian control of United States currency notes. A program relating to the importation of all currency notes into the United States is being studied by Messrs. Luxford, DuBois, and Rains.

65. Netherlands Decree. A study is being made by Mr. DuBois concerning what should be done with respect to the Dutch assets covered by the Dutch decree.

66. Certifications Pursuant to Section 25(b) of the Federal Reserve Act (For description see January, 1942 report, Item 47; February, 1942 report, Item 51): Licenses and notifications to State Department were prepared and issued concerning accounts of Banque de Grece and De Javasche Bank. Mr. DuBois handled this.

67. McLaughlin v. Secretary of Treasury, etc. This is a suit by an attorney in Los Angeles, whose accounts were blocked by direction of the Treasury Department because of his connections with German steel interests, in which suit he seeks to enjoin the blocking of his

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accounts, alleging among other things that the freezing control cannot be applied to block accounts of American citizens. Case has been postponed until end of April. In the meantime, further investigation is being made by Treasury and papers and memoranda of law are being prepared in event case is tried in court. Messrs. Sherbondy, DuBois, Lesser, Ackerman, Murphy, Golding, Carlock, and Locker are working on this case.

68. Regulations Concerning Hearings. Consideration is being given to the issuance of regulations providing for a more formal method of giving hearings on applications for licenses. Mr. DuBois is working on this matter.

69. Remittances and Food Shipments Abroad. We attended meetings at the State Department covering the problem of permitting remittances abroad for prisoners of war, including civilian internees and for classes of non-American citizens. We also discussed the problem of food shipments abroad.

70. Use of Silver for Industrial Purposes (For description see February, 1942 report, Item 57): This office cooperated with the Opinions Section in the preparation

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of an opinion that the President has authority to direct that "free silver" in the Government stocks be transmitted to industrial defense plants for use in a manner which will permit substantially all of it to be returned at the termination of the war. Messrs. Aarons and Brenner worked on this opinion.

This office cooperated with the Legislative Section in the preparation of a draft of a bill providing for the sale of silver in the monetary stocks of the United States and for the suspension of certain sections of the Silver Purchase Act of 1934 and of the Act of July 6, 1939. Miss Hodel and Mr. Brenner handled this matter.

71. Litvinov Assignment - District of Columbia Bonds:
Procedure was suggested in connection with proposed disposition of the suit by Louis Pink, New York Superintendent of Insurance, against the District of Columbia (United States intervenor) relative to District of Columbia bonds which Pink had held prior to the Litvinov assignment as liquidator of the Russian Reinsurance Company. Mr. Aarons, Miss Goode and Mr. Mann worked out the procedure.

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72. Agreement for Financial Aid to China (For description see January, 1942 report, Item 51; February, 1942 report, Item 59): We concluded the negotiations with the Chinese with respect to this Agreement. The Agreement was executed on March 21, 1942. Mr. Bernstein handled the matter.

73. Sale of Gold to Cuba: Mr. Bernstein prepared, in conjunction with Dr. White's office, contract covering the sale of \$5 million of gold to Cuba, payment to be made 120 days after delivery of the gold.

TREASURY DEPARTMENT

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INTER OFFICE COMMUNICATION

DATE MAY 28 1942

TO Secretary Morgenthau
FROM Mr. Haas
Subject: The inventory situation.

In response to your request of May 27, I am submitting the following survey of the inventory situation, as revealed by available statistics.

General statement

(1) The size of the stock of goods accumulated in the hands of (a) manufacturers, (b) wholesale distributors, and (c) retailers, is an important factor in the timing of actual price inflation after the initial inflationary pressure has developed. Inflation, so far, has been restrained by the fact that most "scarce" articles -- aluminum kitchen ware, radios, rubber goods, etc. -- are still available in retail stores, although the production of such articles for civilian use has for some time been curtailed or eliminated. A representative of Macy's said this week that it would take perhaps a year for the current stocks of such articles to be sold out.

(2) The statistical data on inventories are incomplete, and because of price changes the reported dollar values do not directly indicate the actual quantities on hand. The available data, however, appear to warrant the following conclusions:

- (a) Retail stocks of goods generally have kept pace with the increase in sales volume. Confidential estimates of the Department of Commerce indicate an increase of 22 percent in total value of retail inventories at the end of March over the previous year. (Their estimates of retail sales, excluding automobiles, indicate a 21 percent increase in total retail sales over the same period).
- (b) Retail inventories have continued to increase in recent months. This has been particularly noticeable in department store stocks, which expanded sharply in the first 4 months of this year. At the end of April they were

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59 percent higher than a year ago in dollar value, and about 34 percent higher in actual quantity. Stocks of major household appliances showed the largest increase.

- (c) Wholesalers' inventories, showing an overall increase of 20 percent at the end of March, have about kept pace with the increase in sales. Indications of shortages, however, have begun to appear in shoes, and to some extent in hardware and house furnishings.
- (d) Inventories of manufacturers have increased sharply and at the end of March were 34 percent higher than a year ago, but they now reflect the production of war materials rather than civilian goods.

The inventory situationI Retail inventories

The most complete data on retail inventories are those for department stores. Stores of this type account for a considerable part of the retail sales of consumer goods, particularly of clothing and housefurnishings, and doubtless provide a good indication of trends in other types of retail stores. Department store stocks (in dollar value) have risen very sharply since the seasonal low was reached in January, and at the end of April were at a new peak for at least as far back as 1936. The Federal Reserve Board index of department store stocks shows the following trend in recent months:

End of month:	Unadjusted	Seasonally adjusted
1941		
April	76	74
1942		
January	83	93
February	97	102
March	111	108
April	121	117

The trend of department store stocks in relation to sales (both seasonally adjusted) is shown in Chart 1. It will be seen that stocks rose very sharply from January to April, while sales were declining from the January peak. The heavy sales in January were most pronounced in men's and women's clothing, which trade observers attributed in part to anticipatory buying and hoarding. The sales peak last August reflected buying in anticipation of increased excise taxes and other factors. Sales of major household appliances in August, for example, showed the extreme gain of 95 percent over August of the previous year.

Part of the increase in the dollar value of inventories, of course, has been due to increased prices. The Fairchild retail price index, which covers typical department store items, on May 1 this year stood 19 percent higher than on the same date a year earlier. This compares with an increase of 59 percent in the dollar value of department store stocks. In other words, an adjustment for increased prices, based on this index, would indicate that the actual volume of goods in department store stocks at the end of April was 34 percent higher than at that time a year ago.

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Similarly, the indicated volume of actual goods at the end of April (on a seasonally-adjusted basis) was 22 percent higher than at the end of January. Without seasonal adjustment, the increase would be even larger. This indicates that department stores have built up their stocks sharply in recent months.

In this connection, the following comment appeared in the textile section of the New York Journal of Commerce on May 20:

"Some weeks ago reference was made here to a broad expansion in retail buying, exceeding by far the rise in sales, and frequently reflecting the effort of big retail organizations to lay in heavy inventories. In numerous cases, it was then pointed out, this accumulation was being extended to the point of hoarding. Extreme cases were cited where in blankets and some other goods stores were leasing extra warehouse space and laying in supplies sufficient to carry them well through the winter of 1942-43."

What lines show most increase?

The Federal Reserve Board compiles data quarterly on department store stocks by departments. The most recent figures are for the end of January. (Data for the end of April will be compiled in a few weeks.) January figures for major departments and for selected sub-divisions are given in Table 1, which shows (1) the percentage increase in stocks on January 31, 1942 over the previous year, (2) the stocks last year as a ratio to sales in January, indicating the number of months' supply, and (3) the stocks this year as a ratio to sales in January.

It will be noted that the two largest increases in inventories were in major household appliances and in hosiery, the former showing an increase of 127 percent over the previous year and the latter 87 percent. Stores apparently stocked up heavily on such articles as refrigerators, washing machines, and other household appliances after curtailment orders were issued last fall. The stocks of these in January, as shown in the last column of the table, were equal to 3.3 months' supply at the January sales rate, as compared with 2.2 months' supply in the same month of the previous year. Substantial increases in the number of months' supply are also shown for hosiery and furniture.

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In connection with the increase in stocks of household appliances, the Cleveland Trust Company Bulletin of May 15 says: "The supplies of household appliances have been especially large in anticipation of the increased demand for them, and stocks have been stored in warehouses to meet future demands. The extraordinary production in the early months of last year, before the plants were turned over to the manufacture of war materials, made it possible for the stores to obtain these goods and increase their supplies of them."

On the other hand, noticeable decreases are shown for most items of men's and women's apparel, perhaps in part because of the heavy demand for those items during January.

The total shows but little change in the number of months' supply for all items on January 31, but in view of the reports of widespread stocking since that date, and the decline in sales (seasonally adjusted) since January, it is likely that the figures as of April 30 will show a relatively heavy inventory accumulation.

Estimated total retail stocks

Estimates of total retail inventories have been made by the Department of Commerce for the confidential use of the OPA and other Government agencies. These are shown in Table 2, with certain components for which separate estimates are available.

These estimates place the total value of retail inventories at the end of March at \$6,991,000,000, which was 22 percent above the figure for March 1941. It will be noted that this increase is considerably less than the increase of 41 percent shown by department store inventories in that period. The difference is accounted for partly by the inclusion of various types of stores which customarily carry limited stocks, such as food stores, filling stations, etc.

A statement on retail and wholesale inventories, to contain data as of the end of April, is now being prepared by the Department of Commerce, and may be available for confidential use in about a week.

II Wholesale inventories

Inventories of wholesale establishments probably do not entirely indicate supplies available for consumers, since part of the goods on hand doubtless represents materials and supplies for industrial purposes, and part represents goods destined for war uses. In Table 3 is shown the Department of Commerce figures on wholesale inventories for selected types of goods that will probably go largely to civilian consumers.

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It will be noted that in most instances wholesale stocks have kept pace with sales, and the ratio of stocks to sales at the end of March was practically unchanged from the previous year. In total, the stocks on hand on that date equalled 1.5 months' supply at the March rate of sales, as compared with 1.6 months' supply on the same date last year.

Exceptions are noticeable, however, in general hardware and in furniture and housefurnishings, both groups showing substantial declines in the ratio of stocks to sales. In the case of hardware, the increase of only 9 percent in the cost value of inventories probably means that the amount of goods on hand has declined, since prices of hardware have probably risen by substantially more than 9 percent.

Wholesale inventories of shoes and other footwear show some signs of an impending shortage. The value of inventories at the end of March was only 5 percent higher than a year earlier. Wholesale prices of shoes have risen nearly 16 percent in that period, thus indicating that the actual amount of shoes on hand has declined by 9 percent.

On the other hand, wholesale inventories of food products and of alcoholic beverages have increased sharply, and on the whole show a moderately larger increase than the increase in March sales.

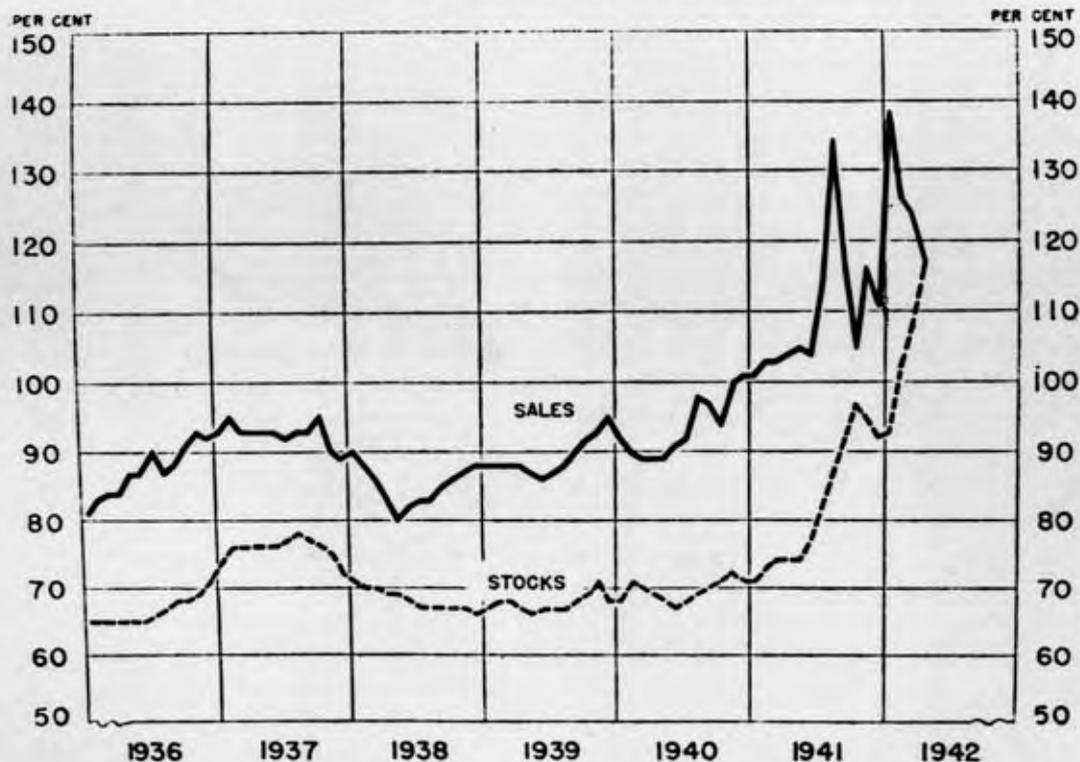
III Manufacturers' inventories

Figures on inventories of manufacturers are affected so much by the war program that they are probably of little value as an indication of supplies available for civilian use. The latest Department of Commerce data on manufacturers' inventories (as of the end of March) are given in Table 4 by industry groups.

It will be noted that the totals for both durable and non-durable goods continued to increase during the first quarter of the year, and at the end of March the manufacturers' inventories of both types of goods were one-third higher than in March 1941.

Reflecting the recent drain on steel supplies, inventories of manufacturers of iron and steel tended downward during the first three months of the year, and at the end of March were only 1.6 percent higher than a year earlier. Inventories of the transportation equipment industry (excluding automobiles)-- now the major war industry -- have been rising very sharply. At the end of March they were 106.5 percent higher than a year earlier, and stood at 738 percent of the 1939 monthly average.

DEPARTMENT STORE SALES AND STOCKS



Federal Reserve monthly indexes of value of sales and stocks, adjusted for seasonal variation, 1923-25 average = 100. Latest figures shown are for April 1942.

Table 1

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Department store stocks by major departments
and selected sub-divisions, end of January

	Percent increase in value of stocks, 1942 over 1941	Ratio of stocks to sales (Months' supply)	
		1941	1942
Grand total -- entire store	32	2.8	2.7
Main store -- total	31	3.0	2.8
Women's apparel and accessories	24	2.4	2.1
Coats and suits	15	1.4	1.0
Dresses	6	1.6	1.5
Hosiery (women's and children's)	87	2.5	3.2
Shoes (women's and children's)	16	5.3	4.2
Men's and boys' wear	23	4.2	3.3
Men's clothing	19	3.6	2.4
Men's furnishings, hats, caps	27	4.2	4.0
Boys' clothing and furnishings	28	5.2	4.5
Men's and boys' shoes and slippers	14	6.0	4.5
Housefurnishings	42	3.3	3.4
Furniture, beds, mattresses, springs	47	3.8	4.6
Domestic floor coverings	33	4.4	4.4
Major household appliances	127	2.2	3.3
Domestics, blankets, linens, etc.	24	1.9	1.6
Piece goods	29	3.5	3.2
Cotton wash goods	39	3.8	3.6
Small wares	26	3.4	3.3
Miscellaneous	35	3.6	4.1
Basement store -- total	38	2.2	2.2
Women's apparel and accessories	38	1.5	1.5
Men's and boys' clothing and furnishings	40	3.2	3.0
Housefurnishings	47	2.6	2.6
Piece goods	33	2.7	2.1
Shoes	23	3.6	3.2

Source: Federal Reserve Board.

CONFIDENTIAL

Table 2

Retail inventories, end of month
(Millions of dollars)

	1941	1942			Percent increase March 1942 over March 1941
	Mar.	Jan.	Feb.	Mar.	
Retail, total	5,728	6,620	6,712	6,991	22.0
Department stores	658	728	851	930	41.3
Automobiles	461	507	612	612 ^{1/}	32.8
Variety stores	177	212	215	208	17.5
Men's shoe stores, chain	71	73	82	86	21.1
Men's wear stores, chain	30	43	46	51	70.0

^{1/} Assumed unchanged from February.

Source: Department of Commerce estimates.

Table 3

Wholesalers' inventories by selected groups,
end of March

	Percent increase in cost value of stocks, 1942 over 1941	Ratio of stocks to sales $\frac{1}{2}$ (Months' supply)	
		1941	1942
Total	20	1.6	1.5
Dairy and poultry products	51	0.4	0.4
Groceries and foods, except farm products	30	1.6	1.8
Fats and meat products	37	0.7	0.7
Clothing and furnishings, except shoes	22	1.3	1.2
Shoes and other footwear	5	0.9	0.7
Textile goods	30	2.4	2.2
Beer	40	0.4	0.5
Wines and liquors	39	2.1	2.2
Tobacco and its products	27	0.6	0.6
Automotive supplies	16	2.3	2.6
Paints and varnishes	24	2.1	2.1
Electrical goods	20	1.0	1.1
General hardware	9	2.9	2.2
Lumber and building materials	8	1.6	1.4
Furniture and house furnishings	20	2.1	1.7
Drugs and sundries (liquor excluded)	17	1.8	1.7
Jewelry	10	2.6	2.4

/ Percentages obtained by dividing stocks by sales for an identical group of firms.

Source: Department of Commerce.

Table 4

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Indexes of the value of manufacturers' inventories, end of month,
 March 1941 and January to March 1942
 (Average month 1939 = 100)

Industry	1941		1942		Percent increase March 1942 over March 1941
	Mar.	Jan.	Feb.	Mar.(p)	
TOTAL, ALL INDUSTRIES	124	162	163	166	33.8
Total, durable goods	137	179	181	184	33.7
Total, nondurable goods	113	147	147	150	33.3
<u>Durable goods</u>					
Iron and steel and their products	123	127	126	125	1.6
Transportation equipment (except automobiles)	358	694	709	738	106.5
Electrical machinery	165	244	250	255	54.4
Other machinery	136	188	191	196	44.3
Automobiles and equipment	150	191	190	192	28.5
Other durable goods	113	140	141	141	25.1
<u>Nondurable goods</u>					
Food and kindred products	109	164	159	156	42.3
Textile-mill products	123	152	154	158	28.7
Paper and allied products	120	134	138	140	16.4
Chemicals and allied products	119	148	151	155	30.4
Petroleum refining	102	113	116	115	13.3
Rubber products	139	150	150	n.a.	-
Other nondurable goods	106	145	147	156	47.7

p) Preliminary

a. Not available

Source: Department of Commerce

never used

W. P. ... 5/28 - 262



THE SECRETARY OF THE TREASURY
WASHINGTON

MEMORANDUM FOR THE PRESIDENT:

Under the Executive Order creating the Office of the Alien Property Custodian, Mr. Crowley was given all of the authority conferred upon you under sections 5(b) and 3(a) of the Trading with the enemy Act except the limited powers under the original freezing order which you gave me prior to the passage of the First War Powers Act which so greatly expanded your powers in the field of freezing control.

At the present time much of the necessary authority which I am exercising was given to me by Mr. Crowley in an informal memorandum in which he reserves the right to revoke such powers at any time. Furthermore, Mr. Crowley can order me to turn over to him a billion dollars in gold, and several billion dollars in securities and bank balances, owned by the French, Belgians and the Dutch which are now controlled through the Treasury freezing powers. It is my understanding that you never intended the Alien Property Custodian to have this power.



- 2 -

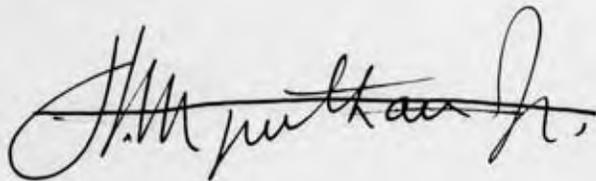
What I would like is an Executive Order which confers upon me equal powers under sections 3(a) and 5(b) of the Trading with the enemy Act. When this has been done, I should be in a position to work out with Mr. Crowley a satisfactory division of functions between the Treasury and the Alien Property Custodian, subject to your approval.

Pending a final allocation of the functions, the Treasury and the Alien Property Custodian will continue to function as at present and a press release would indicate that the purpose of the new Executive Order is to eliminate any possibility of legal attack on the Treasury freezing activities.

We have been discussing with the Alien Property Custodian a division of functions in which he would have full powers with respect to all properties owned by countries with which we are at war and in addition full powers with respect to all foreign-owned patents, copyrights, trade marks, and ships. This would leave for administration by the Treasury the property not allocated to the Alien Property Custodian for administration.

- 3 -

The Treasury would be doing essentially a freezing control job with respect to property of neutral countries and enemy-occupied countries, including a continued regulation of movements of currency and securities, and of trade and communications abroad, participating in the black list and censorship programs, the working out of a scorched earth policy for currency and securities in Hawaii, the handling of the property aspects of the evacuee program, and problems similar to those which we have been handling in the past and not included in the functions clearly envisaged for the Alien Property Custodian.

A handwritten signature in cursive script, appearing to read "J. M. Pugh, Jr.", is written across the lower half of the page. The signature is fluid and somewhat stylized, with a horizontal line crossing through the middle of the letters.

TREASURY DEPARTMENT

265

INTER OFFICE COMMUNICATION

DATE May 28, 1942

TO Secretary Morgenthau

FROM Mr. Kamarok

Subject: Shipment of Planes and Tanks to the U.S.S.R.

Summary

1. In the second third of May, only 9 bombers and 24 tanks were shipped to Russia.

2. There has been a drastic decrease in shipments to Russia in May, compared to the preceding months. With May two-thirds over, only 66 planes and only 77 tanks have been shipped.

3. Mr. Tickton informed me that he has heard that ships allocated for May shipments to Russia were diverted into other uses. He is making an investigation of the situation and will report to you on the matter.

- 2 -

Table A

Shipment of Planes and Tanks
from the United States
to the U.S.S.R.*

	<u>Shipments during May 10 - 20</u>	<u>Cumulative total January 1, 1942 to May 20, 1942</u>
<u>Planes</u>		
Pursuit	0	419
Bombers	<u>9</u>	<u>357</u>
Total Planes	9	776
<u>Tanks</u>		
Light	22	677
Medium	<u>2</u>	<u>572</u>
Total Tanks	24	1,249

* Based on export declarations received.

- 3 -

Table BShipment of Planes and Tanks to
the U.S.S.R. by months *

	<u>Fighters</u>	<u>Bombers</u>	<u>Total Planes</u>	<u>Light Tanks</u>	<u>Medium Tanks</u>	<u>Total Tanks</u>
January, 1942	56	4	60	20	22	42
February	123	115	238	172	38	210
March	68	170	238	159	258	417
April	120	54	174	287	216	503
May 1 - 20	<u>52</u>	<u>14</u>	<u>66</u>	<u>39</u>	<u>38</u>	<u>77</u>
Total 1942 to May 21	419	357	776	677	572	1,249

* Based on export declarations received

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DEPARTMENT OF STATE
WASHINGTON

May 28, 1942.

In reply refer to
FD

The Secretary of State presents his compliments to the Honorable the Secretary of the Treasury and encloses herewith a copy of despatch no. 261, and its enclosures, dated May 4, 1942, from the American Consulate General, Sydney, Australia, reporting on negotiation of dollar telegraphic transfers, checks drawn on the Treasurer of the United States and the sale of United States currency for official purposes; and the disposition of excess United States paper currency.

Enclosure:

From American Consulate General, Sydney,
no. 261, May 4, 1942, and enclosures.

Copy:bj:5-28-42

THE FOREIGN SERVICE
OF THE
UNITED STATES OF AMERICA

AMERICAN CONSULATE GENERAL
Sydney, Australia, May 4, 1942.

SUBJECT: Negotiation of Dollar Telegraphic Transfers, Checks drawn on the Treasurer of the United States and the sale of United States currency for official purposes; and the disposition of excess United States Paper Currency.

THE HONORABLE

THE SECRETARY OF STATE,
WASHINGTON.

SIR:

I have the honor to refer to the Department's telegram No. 154 of April 9, 1942, 2 p.m. transmitting a message from the United States Treasury Department on the above subject.

1/-2/ Following the receipt of the above-mentioned telegram the Consulate General held several discussions with the Commonwealth Bank of Australia, Sydney, and the decision reached by the Bank was conveyed to the Department in my telegram No. 242 of April 30, 1942, 4 p.m. My telegram was based upon a letter dated April 27, 1942, which was received by this office from the Commonwealth Bank of Australia, Sydney. A copy of this letter and its enclosure are forwarded herewith.

It will be noted that on and from May 1, 1942, the negotiation of dollar telegraphic transfers, checks drawn on the Treasurer of the United States and the sale of United States currency for official purposes will be at the rate of \$3.228 (formerly \$3.237), which will bring the rate precisely into line with the sterling rate of \$4.035 mentioned in the first paragraph of the Department's telegram No. 154.

3/ As mentioned in the letter from the Bank, United States currency will continue to be purchased from the public at the rate of \$3.2687, instead of \$3.288 as suggested to the Commonwealth Bank of Australia by the Bank of England. The continued use of the rate \$3.2687 was decided upon partly because stores and other organizations in Australia handling American currency have been educated by the Commonwealth Bank to accept such American currency at a value arrived at on the basis of \$3.2687. In this connection there is enclosed a card showing the value of American money in terms of Australian money, as issued by the Commonwealth Bank under date of February 14, 1942 after the rate of \$3.2687 had been established. These values soon became so well fixed in the minds of the public in Australia

that it was foreseen by the Commonwealth Bank that a change at this time possibly would create in the minds of those merchants who are inexperienced in the handling of foreign currency certain doubts as to the stability of the exchange value of American currency. This public rate at which the Bank will continue to purchase American currency (\$3.2687) is, of course, more favorable to American troops than a rate of \$3.288 would be.

The procedure to be followed by the Commonwealth Bank of Australia in disposing of excess United States paper currency as described in the Department's cable No. 154 is understood by this office and the Bank, and will be followed when the occasion arises.

The Consulate General takes this opportunity to inform the Department and the Treasury Department that the Commonwealth Bank of Australia, Sydney, has given its whole-hearted cooperation in this and other matters that have been the subject of discussion or negotiation between this office and the Bank.

Very respectfully yours,

True copy of the
original signed by

Ely E. Palmer
American Consul General

Enclosures:

As noted above.

WCF:mt

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To the Department of State in quadruplicate.
Copy to the Legation.

Copy:bj:5-28-42

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Enclosure No. 1 to Despatch No. 261 dated May 4, 1942, from
American Consulate General, Sydney, Australia. File 851.6.

COPY

COMMONWEALTH BANK OF AUSTRALIA

Sydney 27th April, 1942.

The Consul General,
American Consulate-General
SYDNEY, N.S.W.

Dear Sir,

Reference is made to your letter of the 13th instant and our subsequent discussions on rates and procedure in connection with the handling of transactions on behalf of the U.S. Armed Forces and connected Authorities and their personnel.

As advised you verbally, we have received cabled suggestions from the Bank of England in the matter, and for your confidential information a paraphrase of the cables is forwarded herewith.

We have agreed in principle to the Bank of England's proposals, a slight departure being that instead of altering our public buying rate for notes to \$3.288, we intend to continue the present more favourable rate of \$3.2687.

It will be seen then, that the only material change involved in our present procedure will be in respect of the rate for official business, which will be altered from \$3.237 to \$3.228. This rate will apply to all official transactions, including those with notes, both buying and selling.

It is also intended to apply this rate to the purchase of cheques, etc., drawn on the Treasurer of the U.S.A., and to remittances home by members of the personnel of the U.S. Armed Forces and connected Authorities.

We verbally intimated, we will advise you in good time before we avail ourselves of the machinery for clearance of dollar currency notes indicated in your letter previously referred to.

It is our intention to alter the rates as mentioned as from 1st May, 1942.

Yours faithfully,

(Sgd.) L. Rusden
For the Governor.

Encl.
Copy:lc:5/28/42

COPY

PARAPHRASE OF CABLES FROM BANK OF ENGLAND TO THE COMMONWEALTH
BANK OF AUSTRALIA.

The following suggested amendments are designed to afford favourable facilities to the U.S.A. Armed Forces and other official American Authorities.

It is hoped that you find it possible to adopt a similar procedure and in particular a uniform buying rate for dollars against local currency in line with our rate of \$4.035 (\$3.228 to the £. Australian) for official transactions.

As far as possible uniform rates throughout the sterling area are desirable, and suggest your buying rate for notes be based on the London official buying rate, viz. \$4.11 (\$3.288 to the £. Australian).

Balances of accounts comprising Pay and Allowances of members of the U.S. Armed Forces and other U.S. nationals engaged in operations relating to the war should be regarded as available at all times for transfer to the U.S.A.

As regards notes, the arrangement is that banks receiving the notes should pass them to a designated bank who will cut them in halves, stamp their name on each half, and forward them to the local U.S.A. Consul. The Consul will cable to U.S.A. and arrange telegraphic credit.

Official dollar drafts will be passed to the Consul, who will similarly arrange credit.

Three days Sight Drafts on the Secretary to the U.S. Navy Department are at present excluded from the arrangement. U.S.A. Treasury suggests that before negotiating any such drafts a local bank should arrange through a designated bank for the local U.S.A. Consul to cable the U.S.A. Treasury, describing the draft and requesting instructions.

The official rate will be extended to special missions, such as U.S.A. contractors engaged on official work.

SYDNEY,
27th April, 1942.

Copy:bj:5-28-42

BRIEF NOTES ON AUSTRALIAN MONEY.

The unit of Australian money is the pound note, just as the American dollar bill is the commonly known unit of American money.

The sub-divisions of the pound are shillings and pennies.

One pound (written £1) equals twenty shillings (written 20/-).

One shilling (1/-) equals twelve pennies (12d.).

Currency Notes (Similar to American Dollar Bills).

The currency notes most commonly in circulation are of the one pound and ten shilling values.

Coinage :

There are four silver coins in common circulation, as follows :-

The two shilling piece. (Five of these coins have the value of a ten shilling note and ten coins the value of a one pound note.)

The shilling. (Ten of these coins have the value of a ten shilling note and twenty have the value of a one pound note.)

The sixpenny piece (Two to a shilling). This coin has the value of six pennies or two threepenny pieces.)

The threepenny piece (Four to a shilling.) This coin has the value of three pennies.

There are two bronze coins, the penny and the halfpenny.

Enclosure No. 3 to Despatch No. 261 dated May 4, 1942,
from American Consulate General, Sydney, Australia.
File 85 6.

U.S.A. EXCHANGE TABLE.
CURRENCY NOTES

U.S.A. money can be exchanged for Australian money at any Bank in Australia.

Storekeepers will accept U.S.A. money in payment for purchases made. The storekeepers must turn over to their Banks the U.S.A. money received each day.

The values as stated in Australian money **MUST** be given for U.S.A. money by Banks and storekeepers. It is an offence against Australian laws for U.S.A. money to be exchanged at other than these official rates.

Commonwealth Bank of Australia
10th February, 1942.

TABLE OF U.S.A. - AUSTRALIAN EXCHANGE.

U.S.A.	equal	Australian
5 cents	equal	3½d.
10 "	"	7d.
25 "	"	1/6
50 "	"	3/-
75 "	"	4/7
1 dollar	"	6/1
2 dollars	"	12/2
3 "	"	18/4
4 "	"	£1/4/5
5 "	"	£1/10/7
6 "	"	£1/16/8
7 "	"	£2/2/10
8 "	"	£2/8/11
9 "	"	£2/15/-
10 "	"	£3/1/2
15 "	"	£4/11/9
20 "	"	£6/2/4
25 "	"	£7/12/11
30 "	"	£9/3/6
50 "	"	£15/5/11
100 "	"	£30/11/10

Example: Five dollars equal one pound ten shillings and seven pennies.

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YDEPARTMENT OF STATE
WASHINGTONIn reply refer to
FD 102.1/6567

May 28, 1942

The Secretary of State presents his compliments to the Honorable the Secretary of the Treasury and encloses copies of telegram no. 271, dated May 28, 1942, from the American Consulate, Sydney, Australia, reporting the aggregate amount of Treasury checks received from the Commonwealth Bank on May 27 as \$78,301.01.

Enclosure:

From Consulate, Sydney,
no. 271, May 28, 1942.

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This telegram must be paraphrased before being communicated to anyone other than a Governmental agency. (BR)

Sydney

Dated May 28, 1942

Rec'd 2:01 a.m.

Secretary of State,

Washington.

271, May 28, 10 a.m.

Referring to the Department's telegram no. 100, March 14, aggregate amount Treasury check received from Commonwealth Bank last night 78,301.01.

PALMER

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5-29-42

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DEPARTMENT OF STATE
WASHINGTON

May 28, 1942

In reply refer to
FD 845.5151/199

The Secretary of State presents his compliments to the Honorable the Secretary of the Treasury and encloses a copy of despatch No. 8, together with its enclosures, from the American Mission, New Delhi, India, concerning dollar accounts for American Military Forces in India.

Enclosure:

Despatch No. 8, from
Mission, New Delhi.

Copy:bj:5-29-42

OFFICE OF THE PERSONAL REPRESENTATIVE
OF THE PRESIDENT OF THE UNITED STATES

New Delhi,
May 5, 1942.

Subject: Dollar accounts for American Military Forces in India.

The Honorable

The Secretary of State,
Washington.

Sir:

I have the honor to refer to the Department's telegram No. 111 dated April 9, 2 p.m. and to previous correspondence concerning the rates established by the Reserve Bank of India for the purchase of dollar currency in India.

There are enclosed copies of circulars issued by the Reserve Bank of India to its own branches and to authorized dealers in foreign exchange, from which it will be seen that the buying rate for dollar currency has been raised from Rs 319 to Rs 322 per \$100 and that certain exemptions in connection with dollar banking accounts have been granted to "individual members of the United States Forces serving in India and civilians normally resident in the United States who are employed in United States bases in this country."

It is presumed that the regulations covered by these circulars are similar to those established in Great Britain for official American transactions in dollars and sterling. The description in the Indian regulations, however, of the persons to whom the regulations apply is rather vague. The Finance Department of the Government of India, in reply to an informal inquiry by this office as to whether the regulations would apply to American Consular officers and other non-military officials in India, stated that it believed that they would cover such cases and that if occasion for questioning the applicability of the regulations ever arose, they would undoubtedly be held to apply to all officials regardless of their military or non-military status.

Respectfully yours,

Enclosures:

1. Circular dated 17th April 1942 from Bombay Office of the Reserve Bank of India.
2. Circular dated 20th April 1942 from Delhi Office of the Reserve Bank of India.

851.5
NSH:rga
In quadruplicate.

Enclosure No. 1 to Despatch No. 8
from the Office of the Personal
Representative of the President of
the United States, New Delhi.
May 5, 1942.

Reserve Bank of India,
Exchange Control Department,
Central Office,
Bombay.

17th April 1942.

Exchange Control Circular No. 51.

The Assistant Controller,
Exchange Control Department,
Reserve Bank of India,
Bombay/Calcutta/Madras/Delhi/Karachi/Lahore/Shwabo.

With reference to our circular No. EC 29 of the 21st February 1942 we have to advise that it has now been decided to extend the arrangements for the purchase of U.S. dollar notes by the Reserve Bank to all our offices and to raise the rate of purchase to Rs.322 per 100 dollars.

2. The notes purchased by you should be debited to "Foreign notes purchased account" under the main head "Other Assets" and at the close of business on Friday each week a statement should be sent to Central Office showing the total of the notes purchased up to that date and the amount outstanding/the above account.

3. Persons tendering the notes should be asked to submit lists in duplicate giving numbers and full particulars of the notes in order to facilitate handling. The U.S. dollar notes, which must not be branded or written on or stamped, should be held in the strong room of the Banking Department for the present; instructions regarding their disposal will be issued in due course. Each parcel of notes should be given a serial number and entered in a special opening of the Bill Register. One copy of the accompanying list should be placed on a subsidiary file and the other copy should be placed with the relative parcel of notes in the strong room.

In this connection we enclose two circulars to authorised dealers and money changers which please distribute in your centre.

R. NATH
for Deputy Controller.

C O P Y

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RESERVE BANK OF INDIA
EXCHANGE CONTROL DEPARTMENT

Circular No. A.D. 35

To

All authorised dealers in foreign exchange.

Dear Sir,

With reference to our circular No. A.D. 20 authorised dealers are advised that it has now been decided to extend the arrangements for the purchase of U.S. dollar notes by the Reserve Bank to all our offices and that the rate has now been raised to Rs. 322 per \$100. Purchases of these notes for individual members of the U.S. Armed Forces and U.S. citizens normally resident in the U.S.A. employed in U.S. bases in this country referred to in our circular A.D. 34 of 1942 may therefore be made on the basis of this rate.

Yours faithfully,

RESERVE BANK OF INDIA
EXCHANGE CONTROL DEPARTMENT

Circular No. A.M. 11.

To

All authorised money changers.

Dear Sir,

With reference to our circular No. A.M. 5 authorised money changers are advised that it has now been decided to extend the arrangements for the purchase of U.S. dollar notes by the Reserve Bank to all our offices and that the rate has now been raised to Rs. 322 per \$100. Purchases of these notes for individual members of the U.S. Armed forces and U.S. citizens normally resident in the U.S.A. employed in U.S. bases in this country may therefore be made on the basis of this rate.

Yours faithfully,

C O P Y

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Enclosure No. 2 to Despatch No. 8
from the Office of the Personal
Representative of the President of
the United States, New Delhi
May 5, 1942.

RESERVE BANK OF INDIA
Exchange Control Department
DELHI

Telegrams
"RESERVIST"
Delhi

Post Box No. 139

20th April, 1942.

Circular No. A.D. 34.

To

All authorised dealers in foreign exchange.

Dear Sir,

Authorised dealers are informed that special arrangements have been made in regard to the accounts and the banking operations of individual members of the United States Forces serving in India and civilians normally resident in the United States who are employed in United States bases in this country. In cases where there is doubt as to whether a U.S. civilian is actually employed at a base on Government work, a reference should be made to the Officer Commanding of the base in the matter.

Authorised dealers may open accounts for such persons in rupees. Form QA 22 should be taken in respect of such accounts and provided this is done our previous approval will not be necessary to credits representing the proceeds of pay and allowances of the account holder, whether received in dollars, registered sterling or rupees. A report should, however, be made to the Reserve Bank in form A.7 as provided for hereafter for all such credits as well as for credits in respect of other remittances from outside India. Authorised dealers may sign these reports where it is not practicable to obtain the signature of the account holder.

Authorised dealers may also open U.S. \$ accounts for such persons if required. Dollar remittances representing pay and allowances and other dollar payments received from outside the sterling area may be credited to the account without exchange control formalities. There are no restrictions on debits to such accounts. Cheques in rupees may be drawn on the dollar accounts provided the payees are resident in the sterling area: in such cases the dollar amount will of course be taken as a purchase into the position of the authorised dealer.

Remittances & other transactions. Authorised dealers may provide the usual banking facilities including the encashment or negotiation of United States dollar notes or drafts for such persons whether account holders or not. Banks may exchange rupee notes and cheques into United States dollars (T.T., M.T., or drafts but not notes) for such persons provided they are reasonably satisfied that the monies so converted were received as pay and allowances.

Returns. Credits to rupee accounts representing the proceeds of pay and allowances should be reported on form A.7 to the Reserve Bank but our prior approval will not be necessary in such cases. Reports in this form should also be sent of all remittances from outside India whether in dollars, sterling or rupees received for credit of such accounts. The forms should furnish the account holder's name and service address in addition to the usual particulars regarding the purpose of the payment and the amount paid in.

Reports should be submitted of all sales of U.S. dollars to such persons on form A in the ordinary manner to the Reserve Bank but our prior approval will not be necessary. The form should furnish the applicant's name and service address in addition to the usual particulars regarding amount and the purpose for which the exchange is required.

A return should be submitted to the Reserve Bank of the total of the balances held at the close of business on the last working day of each month on the rupee accounts opened for such persons.

Exemption. Persons in this category are exempted from the requirements of Government of India Notification No. D/C. 3185-F of the 23rd September 1941 with respect to dollar balances.

Yours faithfully,

J. N. AHUJA
Assistant Controller.

RESERVE BANK OF INDIA
Exchange Control Department
Delhi

20th April 1942.

Circular No. A.D. 35

To

All authorised dealers in foreign exchange.

Dear Sir,

With reference to our circular No. A.D. 20 authorised dealers are advised that it has now been decided to extend the arrangements for the purchase of U.S. dollar notes by the Reserve Bank to all our offices and that the rate has now been raised to Rs. 322 per \$100. Purchases of these notes for individual members of the U.S. Armed Forces and U.S. citizens normally resident in the U.S.A. employed in U.S. bases in this country referred to in our circular A.D. 34 of 1942 may therefore be made on the basis of this rate.

Yours faithfully,

J. N. AHUJA
Assistant Controller.

Copy:bj:6-1-42

BRITISH MOST SECRET
U.S. SECRET

OPTFL No. 185

Following is supplementary resume of operational events covering period 21st May, 1942 - 28th May, 1942.

1. NAVAL

The outward and homeward Russian convoys sailed from ICELAND (7) and MURMANSK respectively on 21st May. The outward convoy of 35 ships was shadowed by aircraft from the morning of the 25th and by U-boats from the previous night. Attacks by 36 aircraft on the evening of the 25th resulted in one U.S. ship being damaged. During 26th and 27th May, there were at least 15 attacks by groups of 6 JU 88's and also on 27th 3 torpedo attacks. Presence in NARVIK area of pocket battleships LUTZOW and SCHEER with destroyers, necessitated large covering forces -- Russians also provided escort and air protection for later stage of passage and 20 Russian bombers attacked enemy Northern aerodromes on 27th. It is reported that from 1st April to 13th May 26 enemy convoys, 7 of which were single escorted ships, passed east of MALTA. Our aircraft and submarines made contact on 5 occasions, three of them being successful. During week ending 24th May about 70,000 tons of shipping were lost in the Atlantic.

15 attacks on U-boats by surface craft were reported during the week, of which 6 by U.S. forces. There were 21 attacks by aircraft, of which 7 by U.S. It is estimated that the Germans have about 130 submarines available for operations now and will possibly have a maximum of 200 by August. During the week ending 27th May 1,100 ships were convoyed, of which 9 were lost. During the week ending 23rd May, there were 652,001 tons of imports in convoy to the U.K., including 102,318 tons of oil.

Russian submarines are stated to claim during April 2 enemy merchant ships sunk, two submarines and 4 merchant ships probably sunk and one mine sweeper and 3 merchant ships possibly sunk.

2. MILITARY

RUSSIA. The Russian attack in the KHARKOV Sector has been halted. Nevertheless, it forced the Germans to employ armoured units which they were reserving for subsequent operations and which have now been reduced by casualties. The German claim that their counter-attack from the South has inflicted considerable losses on the Russian troops who had penetrated west of the DONETS towards KRASNOGRAD, although not fully confirmed, has at least some foundation. A German major offensive in the South (gr. undec.) in June is still considered the next probable move.

LIBYA. Enemy operations announced by preliminary moves on 26th started on 27th by

(a) A demonstration by motorised troops with some tanks west of GAZALA.

(b) An attack against the BIR HAKEIM position by one Italian armoured and one Italian motorised division, which was repulsed by Free French and Indian troops.

(c) A southward enveloping movement round BIR HAKEIM by a strong force of 2 German armoured divisions and one German light division. This force turning northwards, broke into 2 columns, the Eastern one directed against EL ADFM and the Western one towards ACROMA. The former was repulsed and then joined up with the Western column, which resulted in severe and prolonged fighting between armoured forces in the area southwest of ACROMA. Particulars of this fighting have been fully reported in the Daily OPTFL.

- 2 -

BURMA. The Japanese are patrolling between the CHINDWIN River and the Indian Frontier. From Eastern BURMA they are slowly continuing their advance into YUNNAN. The Monsoon is impeding operations.

EAST CHINA. Southwest of HANGCHOW the Japanese are attacking southwards with one to two divisions, and have reached KINHWA, their object being to forestall any attempt to bomb JAPAN from aerodromes in that area.

3. AIR OPERATIONS

WESTERN FRONT. Operations were greatly restricted by persistent bad weather. No night bombing of any consequence could be done, but 133 sea mines were laid.

LIBYA. From the start of the German move forward on 25th onwards our night bombers and fighters made intensive attacks on enemy landing grounds, armoured columns and motor supply columns, causing much damage and disorganization. Medium bombers operated against dumps, docks and railway communications in the BENGHAZI area.

MALTA. Enemy attacks were still further reduced, especially as regards the strength of fighter escorts, the daily average falling from about 80 to about 35.

RUSSIA. The German Air Force has about 2,300 aircraft deployed on the Russian Front, of which more than half are in the South. In support of the KERCH Peninsula attack, they are thought to have used about 600 on a 15-mile front, and to have put forward an intense effort, employing nearly all the available dive bombers and fighters. The Russian offensive at KHARKOV first met with little air opposition but early transfers from KERCH and possibly from other areas, enabled the Germans to slow up the Russian advance by giving their own troops strong close support in the battle area, and by striking heavily at Russian communications, especially the DONETS bridges. There is little doubt that the Russian attack came as a surprise, and has thrown out German dispositions for starting their main offensive in the South. The present German Air Forces on the Russian Front are still far below the peak reached during operations last summer, and are considered inadequate to meet large scale attacks on a number of widely separate sectors.

4. OPERATIONAL AIRCRAFT BATTLE CASUALTIES

Metropolitan Area

British In the air - fighters 8; coastal 5, total 13.

<u>Enemy</u>	<u>Destroyed</u>	<u>Probably Destroyed</u>	<u>Damaged</u>
Bombers	2	2	6
Fighters	6	1	21
Total	8	3	27

Middle East (including MALTA)

British In the air - on the ground

Bombers	6	1
Fighters	13	1
Total	19	2

<u>Enemy</u>	<u>Destroyed</u>	<u>Probably Destroyed</u>	<u>Damaged</u>
Bombers	10	2	5
Fighters	16	7	10
Total	26	9	15

Includes 4 destroyed and 1 damaged by A.A.

- 3 -

FAR EASTBritish and Allied in the Air Bombers 10, Fighters 2, Total 12.

<u>Enemy</u>	<u>Destroyed</u>	<u>Probably Destroyed</u>	<u>Damaged</u>
Bombers	1	0	1
Fighters	<u>7</u>	<u>11</u>	<u>0</u>
Total	8	11	1

Note: No account is taken of enemy aircraft destroyed on the ground in any theatre or of British naval aircraft casualties.

5. HOME SECURITY

Estimated civilian casualties for week ending 6 a.m., 27th - Killed, 10; severely wounded, 20.

NUMBER 33

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SECRET

COORDINATOR OF INFORMATION

THE WAR THIS WEEK

May 21-28, 1942



Printed for the Board of Analysts

Copy No. 6

The Secretary of the Treasury

MAY 21-28, 1942

SECRET

Coordinator of Information

THE WAR THIS WEEK

With a continuing lull in the Melanesian area and with a decline in the intensity of operations in the Burmese-Yunnan theater, the Japanese have shifted their attention momentarily to eastern China. Here apparently the immediate object of their operations is to eliminate the Allied air menace in the provinces of Fukien and Chekiang.

Meanwhile in the see-saw struggle about Kharkov it appears that the Germans have once more gained the initiative, although convincing indications of a major Nazi thrust are still lacking. On the propaganda front, it is reported that the Germans are seeking to add momentum to the current surge of war optimism in the United States, which has been stimulated by buoyant American exaggerations of Allied success. In the same connection, persistent American press discussion of the weakening of the German domestic and military position finds little substantiation in careful studies of the situation by experts.

In western Europe the Germans are playing the old game of divide and rule. With Laval still temporizing, the Nazis appear to welcome, if not to abet, the current Italian campaign for French territory. It remains to be seen whether this lever will prove sufficiently strong to force fresh concessions from Laval in the form of closer collaboration with Germany.

The only Allied success of real importance was the entry of Mexico into the war. Observers emphasize above all the political significance of that step, whose influence will be strongly felt throughout Latin America, it is believed.

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The Japanese Drive in Eastern China

While comparative quiet prevails on other Pacific fronts, the fighting in China has spread rapidly over the eastern provinces of Chekiang and Fukien and continues, somewhat abated, in Yunnan. In Chekiang, Japanese columns converging upon Kihwa have been thrown back with heavy losses, according to Chungking, although Tokyo insists that the town is surrounded and the Chinese are trapped. Another Japanese force has completed the occupation of islands near Foochow (Fukien), after debarking under cover of heavy naval and aerial bombardment. Foochow itself has also been under heavy fire, and newspaper despatches indicate that an expeditionary force is now massing at Formosa, possibly for an attempt to invade Fukien province through Foochow and Amoy.

Since the American air attack of April 18, the Japanese have systematically sought out and bombed airfields not only in Chekiang and Fukien but in Kiangsi, Kwangsi, and Hunan. Japanese planes made 54 flights over these five provinces during the month following April 18, according to one unofficial tabulation. Twenty-two towns were bombed. Kian in central Kiangsi (see map) was raided 13 times by a total of 182 planes, while Chuhsien also suffered heavily.

The present fighting in Chekiang province probably has as its principal objective the elimination of bases from which Japan could be bombed, although air distances even from Chekiang are at the outer limits of the tactical range of four-motored bombers. The maximum range of the heaviest four-motored bombers (allowing a gasoline margin for fighting at full throttle) is about 1000 miles, with a normal tactical radius of 750 to 900 miles. Tokyo is about 1100 miles from bases in Chekiang.

Of the eastern air bases in Chinese control, only those in Chekiang lie within practicable range of important targets in Japan (as the accompanying map indicates). Bases in Fukien, such as Kian, are too far distant for comfortable bombing of such targets as Tokyo and Osaka, the obvious industrial objectives on Honshu. Nagasaki, the shipbuilding and manufacturing center on Kyushu, is barely within the maximum range. From Lishui in Chekiang, however, Nagasaki would be comparatively accessible, as would Yawata, site of the very important Imperial Steel Mills. Targets on Formosa, of course, would be within easy range: either Taihoku, the chief city at the northern end of the island, or Takao, an important naval base in southwestern Formosa.

Chinese "Magnetic" Tactics

Operations in the eastern provinces are already settling into the familiar Chinese pattern of "magnetic" tactics, in Chungking parlance. The Japanese have been drawn out, their formations dispersed, and their communication lines over-extended. And now the Chinese are capitalizing on the enemy's exposure and attacking points in his rear, Chungking reports. One Chinese detachment has recaptured Sintang, cutting off the communications of a Japanese column engaged in the attack on Kinhwa.

Although the Chinese have reported 100,000 or more Japanese troops in action in northern Chekiang alone, observers are inclined to place the figure at possibly 50,000 troops. As a matter of fact, some observers believe that military action in the eastern area—either in Chekiang or Fukien—is not of primary importance in any scheme for concerted action to crush the Chungking regime. They point out that the Japanese at about this time last year occupied Foochow for a short period, later withdrawing voluntarily. The Japanese also staged at that time one of

their routine drives inland from Hangchow and the Chekiang coast.

In addition to destruction of the air bases, the Japanese may also seek to disrupt traffic on the railway west of Kihwa which carries important freight and connects with truck routes south and west through central Kiangsi. Further objectives may be the disruption of Chinese transport of salt from coastal works inland, where there is a serious shortage, and possibly the seizure of the winter wheat harvest.

New Threat to Changsha?

The Japanese have three times assaulted Changsha, strategic center on the Canton-Hankow railway. There is some evidence that a fresh drive on that city may be imminent. If the Japanese could seize Changsha and make themselves masters of both the Peiping-Hankow and Canton-Hankow railroads, they would possess a continuous rail route from Manchuria to Hongkong. The consequent saving in shipping and sea risks would be a notable gain. In addition, with this line in their hands, they would be in a position to cut off effectively eastern China from Chungking control.

An Irreparable Japanese Loss.

The Japanese suffered an irreparable loss of a unique character when they recently lost a 15,000-ton vessel by enemy action, according to a report by the Vichy ambassador in Tokyo. The latter declares that 2,000 expert technicians selected from various industries in Japan were lost from a total passenger list of 2400. The Japanese were sending these technicians to the conquered areas in the southwest Pacific where they were to reestablish and develop captured plants.

Fresh Soviet-Japanese Détente

The long-standing border dispute between the Soviet-sponsored Mongolian People's Republic and Japanese-sponsored Manchukuo is now settled, according to Tokyo and—with some reservations—Moscow as well. A protocol for demarcation of the mutual frontiers has been ratified by the governments of both of these remote "buffer" states. Following as it does the conclusion of the Russo-Japanese Fisheries' agreement on March 20, the ratification of the boundary treaty indicates that on the surface at least Russo-Japanese relations in the post-Pearl Harbor period have not deteriorated.

Tokyo made the announcement by radio May 15. Although a Moscow report has indicated that the protocol refers only to the Bor Nor section, and not the whole frontier, it seems likely that at least temporarily the ratification of the protocol formally solves one of the most troublesome of the border issues between Mongolia and Manchukuo. Serious incidents occurred along the border in 1935 and 1937, and those at Nomonhan in early 1939 assumed the proportions of an undeclared war. On September 15, 1939, a fortnight after the outbreak of the European war, Russia and Japan agreed to end hostilities and to form a joint commission to establish a frontier line.

Warning to India

Premier Tojo, warning that all British outposts for the protection of India are now in Japanese hands, has suggested to the Indians that they must either take "this golden opportunity" to eject foreign troops or suffer the consequences. Observers are not yet inclined to discount these threats too completely. The comparative lull in fighting on the Burma-Yunnan front may indicate that the relatively

large concentrations of Japanese troops in Burma will be turned against India, rather than China. A recent AVG raid on Japanese positions on the Yunnan front met little resistance, and despatches from Calcutta report that Japanese scouting parties are active in the Chittagong area. However, the British commander in this area still acknowledges no signs of enemy intention to launch a major offensive on India, according to newspaper reports.

A New Basis for Indian Cooperation?

In an address at Lahore in which he advocated a war federation of India, China, Iran, and Afghanistan, Pandit Jawaharlal Nehru made clear once again his position on the current conflict: "It was my ardent wish that India should have participated in this war." Nor did he question the motives of American aid in Indian defense—in contrast to a statement of Gandhi's a few weeks ago. Furthermore, while reiterating his inalterable opposition to the partition of India, Nehru seemed to offer some basis for compromise with the Moslem League by his statement that if "a majority of a particular territorial unit want separation, it cannot be denied them."

Such a speech may possibly suggest that Nehru is preparing to take a different line from Gandhi, now once again the dominant figure in Indian politics since the adoption by the Congress of his program of non-violent non-coöperation (*The War This Week*, April 30–May 7, pp. 9–11). An observer in New Delhi maintains that the only apparent way to counteract Gandhi's program would be for Nehru to combine with Jinnah, head of the Moslem League, and with Rajagopalachariar, moderate leader from Madras (who resigned from the Working Committee of the Congress in protest against its present program), to organize a national government. Other observers question the practicability of

cooperation between Jinnah and the other two leaders. They concede, however, that a coalition of Nehru, Rajagopalachariar and those who agree with them in support of full war against Japan might yet prove strong enough to combat Gandhi's present influence.

Turning of the Tide at Kharkov?

As the Russians reported the orderly evacuation of the last of their troops and equipment from the Kerch peninsula, there were indications that their offensive against Kharkov was likewise taking a turn for the worse. The ominous statement in a Soviet communiqué that Russian "troops entrenched themselves in occupied positions" suggested that the initiative had passed to the Germans. In one area the Soviets admitted that the Nazis had driven a "wedge" into their positions, and in the Izyum-Barvenkova sector south of Kharkov, the Red Army announced that its advanced units had "repelled fierce enemy infantry attacks." Meantime, the Nazis blandly claimed that the operations south of Kharkov had "developed into a battle of encirclement," threatening "the bulk of three Soviet armies, including strong tank forces."

The Allied press comforted itself with the reflection that the Russian assault on Kharkov might have disorganized the Nazi timetable for a spring offensive. On the other hand, according to despatches from Bern, German military circles predict that the Kharkov defensive will eventually develop into a crushing Nazi offensive—the operations around Kharkov being an interlude between the Soviet winter drive and the coming German offensive.

Ministerial Change in Finland

Despatches from Helsinki announce the resignation of Pekkala, Social Democratic minister of finance and reputedly a friend of the United States. Finland's outstanding Social Democrat, Väinö Tanner, has taken Pekkala's place, while a third member of the same party, Uuno Takki, will fill Tanner's former position as minister of commerce. The Social Democratic party, torn between patriotism and pro-democratic sympathies, in the past months has been an equivocal factor in Finnish foreign policy. In the cabinet, according to reports from Helsinki, Tanner has generally taken a stand midway between Ryti and Witting—pledged to active prosecution of the war to the bitter end—and Pekkala, who on several occasions has expressed disapproval of the German connection. With Pekkala now removed, the Finnish ministry apparently has attained a greater measure of agreement on the war issue.

Despatches from Helsinki continue to suggest, however, that the Finns will take no offensive action this summer. And despite reports of extensive German troop movements to Northern Finland, informed sources apparently believe that the Axis has insufficient land forces in the far north to attempt an offensive against Murmansk.

Dissenting Opinion on Nazi Plans

While Allied military opinion is almost unanimous in predicting a German effort to eliminate Russia from the war this summer, at least one close observer of Nazi air strength sees Britain as the next goal of German aggressive intentions. Taking the position that Russia is too extensive an area for the Nazis to occupy profitably, he believes that Hitler is likely to hold the Soviet forces for the next 12 months by an active defensive, improving particular positions by minor

operations against such points as Rostov. With about 150 divisions the Nazis can neutralize Russia, while using 70 to 80 elite divisions for a decisive blow against England.

In predicting this attack, our observer cites an astronomical figure for German air strength—more than double any of the estimates now current in Allied intelligence circles. He further envisages Nazi use of thousands of gliders for troop transport. The invasion might well start, he concludes, with the landing from gliders of innumerable guerrilla detachments, who would avoid large population centers and military camps, and concentrate on capturing airfields and destroying lines of communication.

There can be little argument with our observer's contention that the conquest of Britain would be a more decisive blow to the cause of the United Nations than the destruction of the Russian army. With the rapidly growing threat in the west removed, Hitler could then turn all his forces against the Soviet Union. But it is obvious that the Nazis' most logical military move is not necessarily the most feasible. Most military observers continue to believe that an attack on Britain this summer would be a foolhardy venture, while a full scale offensive against Russia would be a risk well worth taking.

The Nazi Propaganda of False Hopes

Extravagant radio claims of Russian successes—ostensibly from Soviet sources—may be simply a device of the Germans to break down the morale of their enemies, according to a despatch from London. Apparently these Soviet claims, faked by the Nazi radio, are calculated to raise inordinately the hopes of Russia's allies—only to have these replaced by anger and mutual recrimination when they fail to materialize. This technique has the further advantage of later presenting

the Germans with fictitious victories, the report continues. A similar technique of playing up the (very real) sufferings of the Nazi troops in the Russian snows last winter misled many people in Allied countries. The present program of deception is apparently not unconnected with the current rumors of a Nazi "peace offensive" and the loose talk of "victory in 1942" in the United States.

In fact as this American optimism is Axis-inspired, a Swedish correspondent in London of *Social Demokraten* discerns an Axis effort to stimulate over-confidence, slow down the American industrial effort, and lessen aid to Russia. The German radio, through its clandestine station, "Debunk," had itself come out only this last week with "action" appeals to Americans which lend credence to the view that this wave of optimism is not unwelcome in Berlin. The tenor of these appeals is simple: work more slowly, produce less, use passive resistance, and insist upon keeping troops, planes and ships at home.

A Wave of War Optimism Comes to America

The past two weeks have witnessed a surge of war optimism in this country. This American "victory panic", as our Swedish correspondent dubs it, reflects various developments—reports on the Battle of the Coral Sea, optimistic American official statements, the Russian "offensive" before Kharkov, and a vague feeling that the Germans are seriously weakening and that the crack-up may not be far off. This vein of optimism has developed despite the warning of the President that the war will be long and that the press should do its part by reducing individual victories to their proper proportions in the larger pattern of the struggle. A high point was reached when *Newsweek* carried as the title of its lead article: "Chance for Victory in 1942 Causes Allied Hopes to Soar."

Close observers of the German scene view such optimism as unsupported by their estimates of the German domestic and military situation or by any reasonable prophecy which can now be made. It would be idle to attempt to present an over-all picture of the German situation, but the Appendix deals with certain aspects of the picture to which the Coordinator's office has recently devoted careful study.

Laval on the Mat

Once again the Axis appears to be putting pressure on France, and rumors suggest that Laval, checked on every front, may be considering important concessions to the enemy. Laval had hoped to found a Latin bloc, some observers believe, based on his old close association with Italy. Instead Rome has seized the initiative. With new vigor she is demanding Nice, Corsica, and Tunis, "the rightful fruits of victory." It is stated in the press that Italy has sent Laval a detailed note on territorial demands, and has supported this by saber-rattling reviews of 300,000 troops massed in battle equipment near the French Alpine border. News of increased activity on the part of the Italian Commission in North Africa also comes from diplomatic sources, and there is apparently much talk of the possibility of Italian occupation of Tunis. Nevertheless, despite all these reports, it is still believed in some quarters that Mussolini may be using this issue rather as a way to resist sending men to Russia, alleging the need of troops at home to take over these French areas. Rumors suggest that Laval may be willing to negotiate over Tunis, but it is doubted in some circles if the Italians would be satisfied with less than Corsica and Nice.

Germany has apparently become increasingly dissatisfied with Laval, and it is perfectly possible that she is using these Italian demands as a lever to secure further French

collaboration, just as she is using the sinkings at Martinique to impose further strains on Franco-American relations. Although the German press has expressed approval of Italian claims, it seems reasonable to assume that the Nazis would withdraw their support of Rome if France were to make, for instance, important concessions regarding control of the French fleet. Following up this line, press despatches have gone so far as to suggest that Laval may be working toward another of his famous compromises, to permit German sailors to train at French naval yards and, it is assumed, to familiarize themselves with the operation of the French naval units now at Toulon.

French officials in North Africa are outspoken in their requests for American economic, and, if possible, military assistance. In Tunis civil and military authorities are making what preparations they can for resisting Italian designs, though recognizing that any effective stand would depend on outside support. Officials in Morocco feel that the Germans cannot spare the troops and the United States cannot spare the ships for invasion of that area. They have frankly remarked that, should American troops land in the region, the French would have to make a token resistance to avoid German reprisals; but these high Moroccan officials insist that their present cooperative neutrality is worth very considerable American economic assistance now.

Opinion at Dakar

At Dakar, where the French have thus far successfully opposed Nazi infiltration, it is believed that the authorities will obey any Vichy order sanctioned by Marshal Pétain, according to a recent report of a reliable and well-placed observer. The military, constantly training and on the alert, are resolved jealously to protect their territory, moved by a

mixture of patriotism and the habit of obedience to metropolitan France, according to our source. They hate the Germans and hope for a Nazi debacle, but they scorn the British for what is termed their hit-and-run attack of 1940. De Gaulle is not popular, either as a symbol or as an individual. Nor would the United States be welcome as an intruder. Moreover, behind every opinion lurks the whites' constant concern over the native problem—an unstable, treacherous 15 million who might become a very great danger and responsibility if the long-developed French colonial control were ever upset.

The Axis Moves in Libya

A large Axis armored column striking south of the British positions around Bir Hacheim, a point about forty miles southwest of Tobruk, has broken the relative quiet that has prevailed in Cyrenaica since Marshal Rommel made his exploratory thrusts on April 8. It is too early to judge whether these operations are of major importance, but they follow a period when the aerial neutralization of Malta has made possible reinforcement of Axis forces.

The action of the last few days apparently began with General Walther Nehring leading the African Corps on a sweep from Tengeder, on the southern end of the Derna-Mechili line behind which Axis units have been concentrating. A British communiqué announces that the attack has been met and repulsed.

This Axis advance follows a period of stepped-up RAF bombing, especially in the Martuba and Bengazi regions, reports of which have indicated Axis movements in the north. Although there are rumors of a general Axis drive in the Eastern Mediterranean, for which this attack to the south might be a diversion, it seems quite probable that this

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Axis thrust is only a reconnaissance in force similar to those of early April.

Turkey Pressed but Friendly

In Turkey the economic and food problems described last week have continued to be so acute that a rumor now suggests that Saracoglu, foreign minister and a respected administrator, may replace the present prime minister. This would be a move to quiet growing criticism of the touchy food problem, which was given a new edge by the recent one-third cut in the bread ration.

Apparently nothing in this situation, however, affects military or political policy. An experienced Turkish diplomat reiterated that the Turkish army, while probably unable to repel the Nazis, would fight and would force the Germans to use 30 divisions. The Turkish semi-official press and radio are cautiously neutral toward the Russo-German conflict, but increasingly cordial and optimistic about the American cause. Even the pro-Axis *Cumhuriyet* allowed favorable comment on our war effort. Current Turkish (and Egyptian) opinion of the British is apparently mixed—unflattering with respect to British land forces, but showing high regard for the British Navy.

In the area to the south the Axis has stepped up its radio activity. Taking advantage of the presence in Berlin of the exiled Iraq premier, Rashid Al-Gailani, and the Grand Mufti of Jerusalem, the Axis radio is giving more attention to the coming of the Germans to "liberate" Iran, Iraq, Palestine, Saudi Arabia, Syria and the Lebanon.

Mexico Enters the War

The significance of Mexico's entry into the war is above all political, rather than military and economic. Properly

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capitalized, Mexico's participation might be a powerful stimulus toward solidifying the entire hemisphere in the struggle against the Axis. Axis propaganda, especially in Argentina and Chile, has had considerable success in conjuring up the bogey of "Yankee Imperialism" and minimizing the example of the small Central American republics which have followed the United States into the war by describing them as "banana colonies" with no will of their own. But Mexico is no banana republic. She enjoys great prestige as the champion of Latin American independence. Mexico has proved time and time again that it is not afraid to brave the wrath of the "Colossus of the North". Hence, it will presumably be difficult to persuade Latin Americans that Mexico is merely doing the bidding of the United States.

There is every indication that Mexico itself will assume an active role in the task of promoting hemisphere solidarity. Mexico's entry into the war represents the triumph of the labor and liberal elements within the country over the conservative, clerical groups which have constantly obstructed effective cooperation between Mexico and the United Nations. The spearhead of the anti-Axis drive in Mexico has been Lombardo Toledano, supported by the Confederation of Mexican Workers (C. T. M.). Lombardo has undoubtedly been the most important single factor in determining Mexico's new status as a belligerent, and it is likely that he will press that advantage both abroad and at home.

As head of the Confederation of Latin American Workers (C. T. A. L.), with important affiliates in Chile, Argentina, and Colombia, and with smaller branches in a number of other South American countries, Lombardo can be expected to work through this organization to urge declarations of war against the Axis throughout South America. This campaign may begin with a special congress of the C. T. A. L. in Mexico City in the near future.

At home, Lombardo and the anti-Axis groups can also be expected to increase their pressure for a clean-up of Axis activities and a careful scrutiny of such organizations as the *Unión Nacional Sinarquista*, *Acción Nacional* and other smaller parties which are openly hostile or suspiciously cool toward the United States and its allies.

Drought and Rubber in Brazil

The critical drought now afflicting northeastern Brazil (*The War This Week*, May 14-21, p. 15) may prove to be a disaster not entirely devoid of benefits. As a relief measure for the local population, President Vargas has taken advantage of the situation to send additional laborers in to the Amazon to work in the rubber forests. A Brazilian estimate states there are some 30,000 laborers available for this transfer. A decree has been issued providing transportation by steamer from Fortaleza, capital of Ceara, to Belém at government cost. The Rubber Reserve Corporation of the United States is paying part of the transportation costs by river steamer to Manaus, and is assisting in the construction of barracks in that city to house the newcomers. The Brazilian government has also guaranteed the workers from Ceara a wage of thirty milreis for each daily tour through the rubber forests.

Mounting Crisis in Canada

Following the plebiscite of April 27, Canada may be on the threshold of one of the gravest crises in its history, according to a reliable observer just returned from Ottawa. In the plebiscite of April 27 Quebec alone of the nine provinces failed to release the government from its promises regarding conscription for overseas service. The government, and especially Prime Minister King, are faced with the dilemma either of enforcing conscription against the will of Quebec and

risking political disunity (or worse), or of postponing the application of that measure and being turned out of office by the English-speaking majority in Canada.

Dissatisfaction among Quebec's three million French-Canadians—a third of the Dominion's population—is more serious than at first supposed, and appears to be crystallizing into almost unanimous opposition. The resignation on May 12 of the leading French-Canadian member of the Cabinet, Minister of Transport P. J. Cardin, was followed on May 21 by the adoption of a motion, 67-7, in Quebec's provincial legislature urging the maintenance of the voluntary system. Although Mr. Cardin's resignation has been discounted as the action of a disgruntled politician, the solidity of the provincial legislature is imposing, and its opposition might have been even more radically expressed but for the tempering influence of Premier Godbout of Quebec.

English-speaking Canadians appear to have passed the point where compromise is likely. Should Prime Minister King—an adept compromiser—attempt to delay the enforcement of overseas conscription, the more militant members of his Cabinet, Minister of Munitions and Supply Howe, Minister of Defense Ralston, and Minister of Naval Services Macdonald, might now agree to shelve him. The only alternative to enactment and enforcement of a conscription measure in Quebec at all costs, according to the view expressed by some English-speaking Canadians, is the exclusion of Quebec from its provisions, either through non-enforcement or by provisions in the law itself. English-speaking Canadians in general are opposed to this solution, however, as creating an undesirable precedent. All competent authorities seem to agree that there is no immediate need for conscription, as the Canadian armed forces are getting all the men they need by the voluntary system at present. Overseas conscription is more than anything else a symbol of the total

war that Quebec alone of Canada's nine provinces is unwilling to wage.

Rumors of Violence in Quebec

One alarming symptom of the gathering storm in Quebec is rumors of possible violence. French-Canadians express fear that the armed mobile units of the air raid warden service, composed largely of young English-speaking hot-heads, might turn into anti-French-Canadian vigilante groups. On the other hand, the wealthier Anglo-Canadians in Montreal are openly saying that they expect their homes to be attacked by French-Canadian mobs. Such rumors, though probably completely unfounded, are an indication of the high inter-racial tension now existing in Quebec.

Another disturbing factor is the virulent campaign against any implementation of the conscription law now being conducted by the leading newspapers of the French-Canadian nationalist faction, especially *Le Devoir* of Montreal. The influence of the latter is especially great among the lower clergy of the province, who form the forefront of the anti-conscription movement.

Thoughtful French-Canadians point out that Quebec is in a state of bewilderment. Having put their faith in the Liberal government's promise never to introduce conscription, they cannot understand why that government now appears to be repudiating its anti-conscription pledges just as the Conservatives did in 1917. Public opinion in Quebec has not been sufficiently educated as to the necessities for this *volte face*. Whether enough time remains for a campaign of enlightenment is open to question. If nothing is done, according to our observer, extremist demagogues—of whom there are many in Quebec—will have an opportunity to disrupt the province and might conceivably even try to bring about secession.

APPENDIX

SOME ASPECTS OF THE GERMAN MILITARY AND DOMESTIC SITUATION

In recent surveys the Coordinator's office has devoted careful study to certain aspects of the contemporary German situation, both military and domestic. First, on the military side, evidence indicates that the British bombing campaign is distinctly less effective than press comment would suggest, the Coordinator's estimate on German casualties is much lower than those of the British, and the German oil position is shown to be stronger than is generally believed.

Effects of the British Air Offensive

A survey of the evidence by an air expert concludes that, at the present tempo, the British bombardment will have no major effect on the German War effort against Russia between now and the time when operations are curtailed by the winter. It is very easy, however, to exaggerate the amount of damage which would be done even if Anglo-American resources permit a notably heightened tempo of attack. The blitz on Coventry, most successful of all, reduced the town's activity index, based on electric power consumption, to 37 percent of its previous level. But electric power consumption had returned to normal in about five or six weeks. The conclusion is simple: the most damaging blitz of the war must be repeated every few weeks if the industrial activity of the target area is to be kept down to a damaging level.

German Casualties on the Russian Front

Optimistic estimates of German permanent casualties on the Russian front from British and other sources, run as high as 2,600,000. The estimate of the Coordinator's office, however, is only about 1,400,000. This figure is unquestionably a conservative one. While these higher estimates cannot be summarily dismissed, it is believed that they are based on total casualty figures which are too high and that the breakdowns of these figures utilize percentages of killed, missing, and totally disabled which are too great a proportion of total casualties.

It should be noted that any estimate of permanent losses does not include the important factor of men in hospitals. What may be called the "hospital pool," in a period of large-scale offensive operations such as the campaign of last fall in Russia, probably results in a constant drain of some 600,000-700,000 men on the strength of the German armed forces.

The German Oil Position

During the second half of 1941—at the height of the fighting in Russia—Germany's consumption of petroleum was approximately equal to Nazi production.

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according to a study prepared in the Economics Division of the Coordinator's office, while consumption last winter was considerably lower than current output.

From June to December of last year, petroleum consumption of the German ground and air forces on the Eastern Front probably amounted to about 430,000 tons a month—around 300,000 tons of which were for the ground forces alone. Combat vehicles accounted for about 70 percent of this latter figure, supply vehicles for the remainder. Divisions actively engaged in combat were responsible for more than 90 percent of the ground force consumption. Of the 130,000 tons consumed by the air force, almost all was for planes rather than for the supply service.

During this same period, military consumption elsewhere than on the Russian front amounted to about 225,000 tons a month, with civilian consumption 870,000 tons. The consumption total of 1.3 million tons a month was only slightly larger than the estimated production rate. Thus petroleum production and consumption were in approximate balance during that period of the war when Germany's military requirements were at their peak. At most the Nazis made no more than negligible withdrawals from stocks.

Although this report has not studied the period from December, 1941, to March, 1942, as carefully as the preceding period, it seems unlikely that military consumption of petroleum during the winter amounted to more than 420,000 tons a month. If civilian consumption continued at the rate of 870,000 tons a month, total consumption was approximately 1.1 million tons—as compared with a production of 1.3 million tons. The conclusion is inescapable that German petroleum stocks last winter were increasing at a rate of approximately 200,000 tons a month.

Party and Army

On the German home front, the Coordinator has devoted particular attention to the relations of the Nazi Party and the Army, to the German food position, and to German morale.

Certain writers have emphasized what they term a "fundamental opposition" between the Party and the Army. But the old independent Wehrmacht no longer exists. Since February 4, 1938, when Blomberg and Fritsch had to go, the German army has been pretty effectively Nazified from the top downward. For some years now the entire young manhood of Germany has passed through the pre-military training entrusted on January 19, 1939 to the SA. All the younger classes now in the Army are the products of Nazi training and education. Nothing is more certain than that the expansion of the 4000 commissioned officers of the old Reichswehr into the hundreds of thousands of officers of the present army has resulted in an immense strengthening of the position of the Nazi Party in the Army. Military Attaché reports agree that all the officers in the grades from major downward are solidly National Socialist.

The higher officers from colonel upward are still in the main the officers of the Reichswehr. Promotion in the German army is slow, even in time of war. Very few Nazis have found their way into the higher and highest grades. The officers of these grades are above all professionals with little or no political tradition behind them. It was only due to the lack of political leadership on the part of Hammerstein, Blomberg and Fritsch that the Army, unlike the Navy and the Air Corps, held aloof from the National Socialist movement. Hitler made an

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end of that aloofness on February 4, 1938, and he did it without resorting to one of Stalin's purges. The hostile officers were pensioned or gradually eliminated. It is safe to say that few enemies of Hitler remain among the higher officers. In the opinion of one very close and reliable observer of the German army, the relationship between the Party and the Army is no longer an issue of fundamental importance.

The German Food Position

The April change in German rations gave rise to optimistic comments in the press, even suggesting that Nazi food shortages might soon be serious. A recent analysis of the German food position by the Economics Division of the Coordinator's office, however, suggests a different situation (*The War This Week*, April 16-23, 1942, pp. 15-16). Germany's food position appears to be cared for through the year 1942-43, on the assumption that the same areas now available to her will continue to be. It is only after the end of the calendar year 1943 that the situation may become serious, and to a considerable extent this too may be avoided by a further reduction in rations, particularly for fats and oils and, in all probability, for meats. Such reductions might still be made without dealing a body blow to the efficiency of the German military and economic machine.

Considerations of German Morale

Intimately allied to such considerations as food rationing and British bombing is the problem of German morale. The view that serious fissures have already appeared in the morale front and that the Allies "can win the war by propaganda" is one of the favorite forms of contemporary wishful thinking.

It is unquestionably true that the German people, imbued with the notion that they were embarking on a short war of brilliant but inexpensive conquest, have been grievously disappointed. The reverses and serious losses suffered by the German Army in Russia must have had deep and disheartening effects on all strata of the German population. The prospect of another winter of war, and perhaps still another, is doubtless a nightmare to the great masses of the German people.

On the other hand, there is no convincing evidence that German morale has been seriously impaired. A recent survey in the Coordinator's office reveals widespread support of the existing regime in word and deed. There is grumbling and some dissidence among the aged, women, Austrians, South Germans, ardent Lutherans and Catholics, intellectuals, Jews and certain others. But apparently there is no justification for the view that the organizational efficiency of the regime has been impaired by this dissidence. The widespread fear that, in the event of defeat the German people will reap a peace of vengeance, has undoubtedly contributed to the creation of an attitude of grim determination to see the war through at all costs.

Resistance in the Occupied Territories

Recent discussions of alleged German weakness lay considerable emphasis on Nazi difficulties in the occupied territories. The implication is that certain of these countries are already developing within them significant instruments of

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revolt and that they are, therefore, increasingly ripe for Allied invasion. Three countries are central in this argument: Italy, France, and Norway. In none of them does the controlling authority (hence Nazi influence) seem to be threatened in any serious way.

The three fundamental forces in Italian life, namely, the monarchy (including the army), the fascist regime, and the Catholic Church, appear to be intact and to be united in an effort to preserve the integrity of the kingdom and the power of the present government against foreign and domestic enemies, according to one close student of Italy.

The foreign enemies include the nations with which Italy is at war and may also include Italy's ally, Germany, whose increasing power in the peninsula is a matter of great concern to Italian ruling circles. At the moment, this concern takes the form of limiting German control in Italy rather than of repudiating the German alliance which, from many points of view, has proved helpful to Italy (as, for example, in the Greek and North African campaigns). Curiously enough, even in non-fascist or mild anti-fascist circles, Mussolini is looked upon as a bulwark against overbearing German control in Italy.

Monarchy and Church in Italy

The Savoy Monarchy, with its deep roots in Italian life, still has considerable prestige among the people and still commands the unquestioned loyalty of the army, our observer continues. The strongest elements in the army appear to be intact and to be still in Italy. The monarchy and the fascist regime need each other. To be sure, even if the fascist regime should fall, the monarchy could hope to survive because it might be able to count on the army and wide popular support.

The Catholic Church and the fascist regime have been and are on friendly terms, he notes. The Church, even more than the monarchy, can pursue an independent policy, even if fascism should fall. It must not be forgotten that the clergy in Italy—including the hierarchy—is predominantly Italian and feels a great sense of patriotism towards Italy.

The fear of national humiliation, of chaos or revolution (Communism), is one of the strong bonds which unite the forces of fascism, the monarchy and the Church at the present time. No organized anti-fascist movement, strong enough to seize power, seems to exist in Italy today. There appears to be no immediate prospect that the fascist regime will be overthrown.

All the above is subject to qualification dictated by a constantly changing world and Italian situation, our observer concludes. The most important qualification is this: the return of Laval to power has created an "opening" which affords the best opportunity for a diplomatic anti-Nazi offensive in Italy since that country entered the war.

Confusion and Weakness in France

At least three elements in the current French situation tend to discount optimistic views of the early crystallization of French resistance to the Nazis. First, the political orientation of Laval remains undefined. He has yet to embark on an overt policy of collaboration. The second factor, a logical result of the first,

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is a confusion in the minds of the French people themselves. Reports from Vichy suggest that certain French civilian and military authorities, although not in sympathy with Laval himself, are still unwilling to believe that he will play the Germans' game completely.

The third factor is an apparent disinclination for organized revolt on the part of the French masses. A recent report from Vichy suggests that the French people will not dare to move until the Americans and British have established a second front in their country. Such a lack of initiative is not unconnected with the widespread malnutrition in both zones of France. The United Nations can scarcely rely on men weakened by hunger spontaneously to foment internal revolt on any significant scale.

Potential Norwegian Resistance

It is clear that since February there has been a marked deterioration of the relations between the Quisling regime and the people. Quisling, who is said to have gained the support of a scant one percent of the people, has met mounting hostility since the failure of his February trip to Berlin. This has been sharpened by his recent actions against the clergy and teachers of Norway. New food restrictions and persecution have also increased the provocation to revolt. There also exists an intelligent, disciplined Underground movement, engaged in disseminating information, planning sabotage, and collecting arms for the day of Allied invasion.

However, as a recent study in the Coordinator's office shows, all this opposition to Nazi rule and these preparations for armed revolt, do not threaten Germany's present strategy in Scandinavia. It is the Quisling government, not the German occupying forces, which is embarrassed by the uncooperativeness of the Norwegian civilians. Norwegians, who six months ago looked forward to an Anglo-American invasion in the spring of 1942, now hardly dare hope for it this summer. Commando raids, while in theory a reminder to the Norwegians that they are not forgotten, have become increasingly embarrassing to the Underground, since they offer an excellent excuse to the Germans for widespread arrests in reprisal. In any event, they are only local in character and do not afford an opportunity for the Norwegians themselves to hamper Hitler's plans.

Since February the Germans are estimated to have raised their forces in Norway to a total of about eight or nine divisions. They are steadily improving communications, especially with the far north. They are obviously in a position to tighten up their control of the civilian population at any time, as is seen in reported plans for clearing certain coastal areas. There is, moreover, considerable danger of any action that would prematurely expose the Underground to the Nazi authorities.

In sum, it is clear that Norwegian resistance is stiffening as the pressure increases, and it may be that the deteriorating position of the Quisling regime will bring some kind of a governmental reshuffling; but there does not appear to be any evidence that effective Nazi control of Norway is cracking, or will crack unless there is an Allied invasion or a withdrawal of German forces.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE May 28, 1942

TO Secretary Morgenthau
FROM Mr. Kamarck

Subject: Summary of Military Reports

British Survey of Military Situation

A. Russia

A large-scale German offensive in Russia still seems probable in June. Its opening date, however, may have been delayed by the Russian attacks near Kharkov.

B. Mediterranean

A move by Germany against Turkey, Cyprus or Syria this summer seems unlikely. An assault on Malta is still possible. Rommel's offensive in Libya, even if successful, could not be extended as far as the Nile Delta before autumn.

C. India

It is improbable that the Japanese will attempt a land advance from Burma into India for two months at least.

D. China

The Japanese are unlikely, apart from the possible occupation of Yunnan Province, to advance farther into China from the south.

E. Southwest Pacific

The Japanese appear to have temporarily abandoned their plans for advancing farther towards the supply route from America to Australia.

(Comment: The British analysis has proved to have a high

degree of accuracy in the past. The general picture for the summer is, therefore: concentration by Germany on Russia, action by Japan in the northern Pacific, rather than in the Indian Ocean or the southern Pacific.)

(U.K. Operations Report, May 14-21, 1942)

Northern Supply Route to Russia

At the present time, the supply route to Russia is quite vulnerable to German air attack. There is a long period of daylight and the polar ice belt forces the convoys to pass within easy range of the German air bases in Norway. As the summer advances, the ice belt will move northwards and conditions should improve. Archangel will be free of ice by the end of May. During the winter, port facilities have been improved and Archangel is better served by railroad than Murmansk. It is also farther from enemy air bases.

During the evening of May 25, a convoy to Russia was attacked for a period of three hours by a total of 32 torpedo and dive bombers. The only casualty was an American ship which fractured a steam pipe and is being towed back to England.

One of the bombers was certainly, and four more probably, destroyed.

The two German pocket battleships, the Admiral Scheer and the Luetzow with four destroyers were observed in Narvik on May 26. (The British Intelligence sources are either very good, or the British made a good estimate of the situation. It will be remembered that they reported that the Luetzow was on its way to Narvik before the ship had even rounded the southern tip of Norway.)

(U.K. Operations Report, May 14 - 21; May 26,27, 1942)